

Solera National Bancorp, Inc.  
Form 10-Q  
May 14, 2012

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q  
(Mark one)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2012

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 000-53181

SOLERA NATIONAL BANCORP, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation  
or organization)

02-0774841  
(IRS Employer Identification No.)

319 S. Sheridan Blvd.  
Lakewood, CO 80226  
303-209-8600

(Address and telephone number of principal executive offices and principal place of business)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

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

Edgar Filing: Solera National Bancorp, Inc. - Form 10-Q

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the last practicable date: As of May 10, 2012, 2,553,671 shares of the registrant's common stock, \$0.01 par value, were issued and outstanding.

---

---

---

FORM 10-Q  
SOLERA NATIONAL BANCORP, INC.

INDEX

		PAGE
	INTRODUCTORY NOTE. CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION AND RISK FACTORS	3
	PART I -FINANCIAL INFORMATION	4
ITEM 1.	FINANCIAL STATEMENTS (unaudited)	4
	Balance Sheets as of March 31, 2012 and December 31, 2011	4
	Statements of Operations and Comprehensive Income (Loss) for the Three Months Ended March 31, 2012 and 2011	5
	Statements of Changes in Stockholders' Equity for the Three Months Ended March 31, 2012 and 2011	6
	Statements of Cash Flows for the Three Months Ended March 31, 2012 and 2011	7
	UNAUDITED CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS	9
ITEM 2.	MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	29
ITEM 3.	QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	40
ITEM 4.	CONTROLS AND PROCEDURES	40
	PART II -OTHER INFORMATION	41
ITEM 1.	LEGAL PROCEEDINGS	41
ITEM 1A.	RISK FACTORS	41
ITEM 2.	UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS	41
ITEM 3.	DEFAULTS UPON SENIOR SECURITIES	41
ITEM 4.	MINE SAFETY DISCLOSURE	41
ITEM 5.	OTHER INFORMATION	41

ITEM 6.	EXHIBITS	41
SIGNATURES		42
EXHIBIT INDEX		43

**INTRODUCTORY NOTE. CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION AND RISK FACTORS**

This Quarterly Report on Form 10-Q contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995 about Solera National Bancorp, Inc. (the “Company”) and our subsidiary, Solera National Bank (the “Bank,” collectively with the Company, sometimes referred to as “we,” “us” and “our”) that are subject to risks and uncertainties. Forward-looking statements include information concerning future financial performance, business strategy, projected plans and objectives. Statements preceded by, followed by or that otherwise include the words “anticipates,” “believes,” “estimates,” “expects,” “intends,” “plans,” “may increase,” “may fluctuate” and similar expressions, and future or conditional verbs such as “will,” “should,” “would,” and “could” are generally forward-looking in nature and not historical facts. Actual results may differ materially from those projected, implied, anticipated or expected in the forward-looking statements. Readers of this quarterly report should not rely solely on the forward-looking statements and should consider all uncertainties and risks throughout this report. The statements are representative only as of the date they are made, and Solera National Bancorp, Inc. undertakes no obligation to update any forward-looking statement.

These forward-looking statements, implicitly and explicitly, include the assumptions underlying the statements and other information with respect to the Company's beliefs, plans, objectives, goals, expectations, anticipations, estimates, financial condition, results of operations, future performance and business, including management's expectations and estimates with respect to revenues, expenses, return on equity, return on assets, efficiency ratio, asset quality and other financial data and capital and performance ratios.

Although the Company believes that the expectations reflected in the forward-looking statements are reasonable, these statements involve risks and uncertainties that are subject to change based on various important factors, some of which are beyond the control of the Company. The following factors, among others, could cause the Company's results or financial performance to differ materially from its goals, plans, objectives, intentions, expectations and other forward-looking statements:

management of Solera National Bank may be unable to limit credit risk associated with our loan portfolio, which would affect the Company's profitability;

general economic conditions in the U.S. and within our market area may be less favorable than expected, causing an adverse impact on our financial performance;

the Company is subject to extensive regulatory oversight, which could restrain our growth and profitability;

the Company could face potential regulatory actions if we fail to comply with our Consent Order;

interest rate volatility could adversely impact our business;

the Company may not be able to raise additional capital on terms favorable to us;

the Company continues to hold other real estate owned which has led to increased operating costs and vulnerability to declines in real estate values;

the liquidity of our common stock is affected by its limited trading market; and

the Company faces competition from a variety of competitors.

For a discussion of these and other risks and uncertainties that could cause actual results to differ from those contained in the forward-looking statements, see “Risk Factors” in Item 1A of the Company’s 2011 Annual Report filed on Form 10-K with the SEC, which is available on the SEC’s website at [www.sec.gov](http://www.sec.gov). All forward-looking statements are qualified in their entirety by this cautionary statement, and the Company undertakes no obligation to revise or update this Quarterly Report on Form 10-Q to reflect events or circumstances after the date hereof. New factors emerge from time to time, and it is not possible for us to predict which factors, if any, will arise. In addition, the Company cannot assess the impact of each factor on the Company’s business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

## PART I — FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS (unaudited)

Solera National Bancorp, Inc.

Balance Sheets as of March 31, 2012 and December 31, 2011  
(unaudited)

(\$ in thousands, except share data)	March 31, 2012	December 31, 2011
<b>ASSETS</b>		
Cash and cash equivalents	\$ 729	\$ 1,800
Interest-bearing deposits with banks	357	1,357
Investment securities, available-for-sale	84,498	83,195
Gross loans	55,086	55,645
Net deferred expenses/(fees)	1	(77 )
Allowance for loan and lease losses	(1,077 )	(1,067 )
Net loans	54,010	54,501
Federal Home Loan Bank (FHLB) and Federal Reserve		
Bank stocks	1,148	1,134
Bank-owned life insurance	2,008	—
Other real estate owned	1,776	1,776
Premises and equipment, net	571	599
Accrued interest receivable	666	584
Other assets	411	420
Total assets	\$ 146,174	\$ 145,366

## LIABILITIES AND STOCKHOLDERS' EQUITY

## Deposits

Noninterest-bearing demand	\$ 3,217	3,550
Interest-bearing demand	8,724	9,355
Savings and money market	57,503	58,854
Time deposits	49,688	47,225
Total deposits	119,132	118,984

## Securities sold under agreements to repurchase and federal funds purchased

Securities sold under agreements to repurchase and federal funds purchased	663	253
Accrued interest payable	62	56
Accounts payable and other liabilities	368	534
FHLB advances	6,500	6,500
Total liabilities	\$ 126,725	\$ 126,327

## COMMITMENTS AND CONTINGENCIES (see Note 10)

## STOCKHOLDERS' EQUITY

Common stock, \$0.01 par value; 5,000,000 shares authorized; 2,553,671 shares issued and outstanding	\$ 26	\$ 26
--	-------	-------

Edgar Filing: Solera National Bancorp, Inc. - Form 10-Q

Additional paid-in capital	26,159	26,146
Accumulated deficit	(7,679 )	(7,640 )
Accumulated other comprehensive income	943	507
Total stockholders' equity	\$ 19,449	\$ 19,039
Total liabilities and stockholders' equity	\$ 146,174	\$ 145,366

See Notes to Consolidated Financial Statements.



Solera National Bancorp, Inc.

Statements of Operations and Comprehensive Income (Loss) for the Three Months Ended March 31, 2012 and 2011 (unaudited)

(\$ in thousands, except share data)	For the Three Months Ended March 31,	
	2012	2011
<b>INTEREST INCOME:</b>		
Interest and fees on loans	\$788	\$824
Interest on investment securities	503	673
Dividends on FHLB and Federal Reserve Bank stocks	8	9
Other interest income	2	1
Total interest income	1,301	1,507
<b>INTEREST EXPENSE:</b>		
Deposits	300	369
FHLB advances	31	57
Securities sold under agreements to repurchase and federal funds purchased	1	4
Total interest expense	332	430
<b>NET INTEREST INCOME BEFORE PROVISION</b>	<b>969</b>	<b>1,077</b>
Provision for loan and lease losses	-	-
<b>NET INTEREST INCOME AFTER PROVISION</b>	<b>969</b>	<b>1,077</b>
<b>NONINTEREST INCOME:</b>		
Service charges and fees	15	18
Other income	9	-
Gain / (loss) on available-for-sale securities	114	(2)
Total noninterest income	138	16
<b>NONINTEREST EXPENSE:</b>		
Salaries and employee benefits	567	705
Occupancy	127	133
Professional fees	144	126
Other general and administrative	308	312
Total noninterest expense	1,146	1,276
<b>LOSS BEFORE INCOME TAXES</b>	<b>(39)</b>	<b>(183)</b>
Provision for income taxes	-	-
<b>NET LOSS</b>	<b>\$(39)</b>	<b>\$(183)</b>
<b>OTHER COMPREHENSIVE INCOME, NET OF TAX:</b>		
Change in net unrealized gains on securities	550	73
Less: Reclassification adjustment for net (gains) / losses included in net loss	(114)	2
<b>OTHER COMPREHENSIVE INCOME</b>	<b>\$436</b>	<b>\$75</b>
<b>COMPREHENSIVE INCOME / (LOSS)</b>	<b>\$397</b>	<b>\$(108)</b>
<b>NET LOSS AVAILABLE TO COMMON STOCKHOLDERS</b>	<b>\$(39)</b>	<b>\$(183)</b>
<b>LOSS PER COMMON SHARE:</b>		
Basic (2,553,671 weighted-average common shares)	\$(0.02)	\$(0.07)
Diluted (2,553,671 weighted-average diluted shares)	\$(0.02)	\$(0.07)

See Notes to Consolidated Financial Statements.

5

---

Solera National Bancorp, Inc.

Statements of Changes in Stockholders' Equity for the Three Months Ended March 31, 2012 and 2011  
(unaudited)

(\$ in thousands, except share data)	Shares Outstanding	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total
Balance at December 31, 2010	2,553,671	\$26	\$25,980	\$ (7,882 )	\$ 201	\$18,325
Stock-based compensation	-	-	61	-	-	61
Comprehensive loss:						
Net loss	-	-	-	(183 )	-	(183 )
Other comprehensive income	-	-	-	-	75	75
Total comprehensive loss						(108 )
Balance at March 31, 2011	2,553,671	\$26	\$26,041	\$ (8,065 )	\$ 276	\$18,278
Balance at December 31, 2011	2,553,671	\$26	\$26,146	\$ (7,640 )	\$507	\$19,039
Stock-based compensation	-	-	13	-	-	13
Comprehensive income:						
Net loss	-	-	-	(39 )	-	(39 )
Other comprehensive income	-	-	-	-	436	436
Total comprehensive income						397
Balance at March 31, 2012	2,553,671	\$26	\$26,159	\$ (7,679 )	\$943	\$19,449

See Notes to Consolidated Financial Statements.

## Solera National Bancorp, Inc.

Statements of Cash Flows for the Three Months Ended March 31, 2012 and 2011  
(unaudited)

(\$ in thousands)	For the Three Months Ended March 31,	
	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net loss	\$(39 )	\$(183 )
Adjustments to reconcile net loss to net cash (used in) / provided by operating activities:		
Depreciation and amortization	34	60
Net accretion of deferred loan fees/expenses	(5 )	(12 )
Net amortization of premiums on investment securities	366	149
(Gain) / loss on available-for-sale investment securities	(114 )	2
Federal Home Loan Bank stock dividend	(1 )	(1 )
Recognition of stock-based compensation on stock options	13	61
Increase in bank-owned life insurance cash surrender value	(8 )	—
Changes in operating assets and liabilities:		
Accrued interest receivable	(82 )	56
Other assets	9	20
Accrued interest payable	6	(12 )
Accounts payable and other liabilities	(155 )	70
Deferred loan fees/expenses, net	(73 )	5
Net cash (used in) / provided by operating activities	\$(49 )	\$215
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of investment securities, available-for-sale	\$(12,203 )	\$(14,844 )
Proceeds from sales of investment securities, available-for-sale	7,483	11,350
Proceeds from maturities/calls/pay downs of investment securities, available-for-sale	3,601	3,048
Loan payments received / (originations funded), net	569	699
(Purchase) / redemption of Federal Reserve Bank stock	(13 )	54
Purchase of bank-owned life insurance	(2,000 )	—
Purchase of premises and equipment	(6 )	—
Maturity of interest-bearing deposits with banks	1,000	—
Net cash (used in) / provided by investing activities	\$(1,569 )	\$307
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net increase in deposits	\$148	\$3,497
Net increase in securities sold under agreements to repurchase and federal funds purchased	410	614
Repayment of FHLB advances	—	(4,500 )
Principal payments on capital lease	(11 )	(11 )
Net cash provided by / (used in) financing activities	\$547	\$(400 )
Net (decrease) / increase in cash and cash equivalents	\$(1,071 )	\$122
<b>CASH AND CASH EQUIVALENTS</b>		
Beginning of period	1,800	936

End of period  
(continued)

\$729

\$1,058

7

---

Solera National Bancorp, Inc.

Statements of Cash Flows for the Three Months Ended March 31, 2012 and 2011, (continued)  
(unaudited)

(\$ in thousands) For the Three Months  
Ended March 31,  
2012            2011

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

Cash paid during the period for:

Interest	\$ 326	\$ 442
Income taxes paid	\$—	\$—
Non-cash investing transactions:		
Unrealized gain on investment securities, available-for-sale	\$436	\$75

See Notes to Consolidated Financial Statements.

SOLERA NATIONAL BANCORP, INC.

UNAUDITED CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 — SUMMARY OF ORGANIZATION

Solera National Bancorp, Inc. (the “Company”), is a Delaware corporation that was incorporated in 2006 to organize and serve as the holding company for Solera National Bank (the “Bank”), a national bank that opened for business on September 10, 2007. Solera National Bank is a full-service community, commercial bank headquartered in Lakewood, Colorado primarily serving the six-county Denver metropolitan area.

NOTE 2 — BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting only of normal recurring adjustments) which, in the opinion of management, are necessary to present fairly the financial position of the Company as of March 31, 2012, and the results of its operations for the three months ended March 31, 2012 and 2011. Cash flows are presented for the three months ended March 31, 2012 and 2011. Certain reclassifications have been made to the consolidated financial statements and related notes of prior periods to conform to the current presentation. These reclassifications had no impact on stockholders’ equity or net loss for the periods. Additionally, certain information and footnote disclosures normally included in financial statements have been condensed or omitted pursuant to rules and regulations of the U.S. Securities and Exchange Commission. The Company believes that the disclosures in the unaudited condensed consolidated financial statements are adequate to make the information presented not misleading. However, these unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2011.

The Company received approval as a bank in organization in the first quarter of 2007, conducted an initial closing of its common stock offering and commenced banking operations during the third quarter of 2007. The attainment of sustained profitable operations are dependent on future events, including the successful execution of the Company’s business plan and achieving a level of revenue adequate to support the Company’s cost structure.

Critical Accounting Policies

The following is a description of the Company’s significant accounting policies used in the preparation of the accompanying consolidated financial statements.

Provision and allowance for loan and lease losses: Implicit in the Company’s lending activities is the fact that loan and lease losses will be experienced and that the risk of loss will vary with the type of loans being made and the creditworthiness of the borrowers over the terms of the loans. The allowance for loan and lease losses represents the Company’s recognition of the risks of extending credit and its evaluation of the loan portfolio. The evaluation of the allowance is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. The allowance for loan and lease losses is maintained at a level considered adequate to provide for probable loan and lease losses based on management’s assessment of various factors affecting the loan portfolio, including a review of problem loans, business conditions, historical loss experience, evaluation of the quality of the underlying collateral, and holding and disposal costs. In addition, because the Bank has limited history on which to base future loan and lease losses, a comparison of peer group allowance ratios to gross loans is made with the intention of maintaining similar levels until the Bank has sufficient historical data to see trends in our own loss history. The allowance for loan and lease losses is increased by provisions charged to expense and reduced by loans and leases charged-off, net of recoveries. Loan and lease losses are charged against the allowance for loan and lease

losses when management believes the balance is uncollectible.

9

---



The Company has established a formal process for determining an adequate allowance for loan and lease losses. The allowance for loan and lease losses calculation has two components. The first component represents the allowance for loan and lease losses for impaired loans; that is loans where the Company believes collection of the contractual principal and interest payments is not probable. To determine this component of the calculation, impaired loans and leases are individually evaluated by either discounting the expected future cash flows or determining the fair value of the collateral, if repayment is expected solely from collateral. The fair value of the collateral is determined using internal analyses as well as third-party information, such as appraisals. That value, less estimated costs to sell, is compared to the recorded investment in the loan and any shortfall is charged-off. Unsecured loans and loans that are not collateral-dependent are evaluated by calculating the discounted cash flow of the payments expected over the life of the loan using the loan's effective interest rate and giving consideration to currently existing factors that would impact the amount or timing of the cash flows. The shortfall between the recorded investment in the loan and the discounted cash flows, or the fair value of the collateral less estimated costs to sell, represents the first component of the allowance for loan and lease losses.

The second component of the allowance for loan and lease losses represents contingent losses – the estimated probable losses inherent within the portfolio due to uncertainties. Factors considered by management to estimate inherent losses include, but are not limited to, 1) historical and current trends in downgraded loans; 2) the level of the allowance in relation to total loans; 3) the level of the allowance in relation to the Bank's peer group; 4) the levels and trends in non-performing and past due loans; and 5) management's assessment of economic conditions and certain qualitative factors as defined by bank regulatory guidance, including but not limited to, changes in the size, composition and concentrations of the loan portfolio, changes in the legal and regulatory environment, and changes in lending management. The qualitative factors also consider the risk elements within each segment of the loan portfolio. The primary risk comes from the difference between the expected and actual cash flows of the borrower and is influenced by the type of collateral securing the loans. For real estate secured loans, conditions in the real estate markets as well as the general economy influence real estate values and may impact the Company's ability to recover its investment due to declines in the fair value of the underlying collateral. The risks in non real-estate secured loans include general economic conditions as well as interest rate changes. We aggregate our loans into portfolio segments including: Commercial Real Estate Secured; Residential Real Estate Secured; Commercial and Industrial; and Consumer. We then evaluate the above factors by segment and assign probable loss ranges to each segment. The aggregate of these segments represents the contingent losses in the portfolio.

The recorded allowance for loan and lease losses is the aggregate of the impaired loan and lease component and the contingent loss component. Our methodology for estimating the allowance has not changed during the current or prior reporting period and is consistent across all portfolio segments and classes of loans.

At March 31, 2012, the Company had an allowance for loan and lease losses of \$1.1 million. Management believes that this allowance for loan and lease losses is adequate to cover probable losses based on currently available evidence. Future additions to the allowance for loan and lease losses may be required based on management's continuing evaluation of the inherent risks in the portfolio. Additional provisions for loan and lease losses may need to be recorded if the economy declines, asset quality deteriorates, or the loss experience changes.

Loans receivable: Loans receivable that the Company has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding unpaid principal balances net of any deferred fees or costs, and reduced by any charge-offs and the allowance for loan and lease losses.

Credit and loan decisions are made by management and the Board of Directors in conformity with loan policies established by the Board of Directors. The Company's practice is to charge-off any loan or portion of a loan when the loan is determined by management to be uncollectible due to the borrower's failure to meet repayment terms, the borrower's deteriorated financial condition, the depreciation of the underlying collateral, the loan's classification as a

loss, or for other reasons.

The Company considers a loan to be impaired when it is probable that the Company will be unable to collect all amounts due (principal and interest) according to the contractual terms of the loan agreement. Measurement of impairment is based on the expected future cash flows of an impaired loan, which are to be discounted at the loan's effective interest rate, or measured by reference to an observable market value, if one exists, or the fair value of the collateral for a collateral-dependent loan. The Company selects the measurement method on a loan-by-loan basis except that collateral-dependent loans for which foreclosure is probable are measured at the fair value of the collateral. The Company recognizes interest income on impaired loans based on its existing methods of recognizing interest income on nonaccrual loans (see Interest and fees on loans, below).

Interest and fees on loans: Interest income is recognized daily in accordance with the terms of the note based on the outstanding principal balance. Loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. The accrual of interest on loans is discontinued when principal or interest is 90 days past due based on contractual terms of the loan or when, in the opinion of management, there is reasonable doubt as to collectability. When loans are placed on nonaccrual status, all interest previously accrued but not collected is reversed against current period interest income. Income on nonaccrual loans is subsequently recognized only to the extent that cash is received and the loan's principal balance is deemed collectible. Interest accruals are resumed on such loans only when they are brought current with respect to interest and principal and when, in the judgment of management, the loans are estimated to be fully collectible as to all principal and interest.

Generally, for all classes of loans, loans are considered past due when contractual payments are delinquent by 30 days or more.

Loan origination fees and certain direct origination costs are capitalized and recognized as an adjustment of the yield of the related loan using the effective interest method and without anticipating prepayments.

Share-based compensation: The Company grants stock options as incentive compensation to employees and directors. The cost of employee/director services received in exchange for an award of equity instruments is based on the grant-date fair value of the award, which is determined using a Black-Scholes-Merton model. This cost, net of estimated forfeitures, is expensed to salaries and employee benefits over the period in which the recipient is required to provide services in exchange for the award, generally the vesting period.

Estimation of fair value: The estimation of fair value is significant to a number of the Company's assets, including available-for-sale investment securities. These are all recorded at either fair value or at the lower of cost or fair value. Furthermore, accounting principles generally accepted in the United States require disclosure of the fair value of financial instruments as a part of the notes to the consolidated financial statements. Fair values are volatile and may be influenced by a number of factors, including market interest rates, prepayment speeds, discount rates and the shape of the yield curve. Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the most advantageous market for the asset or liability in an orderly transaction between market participants. The fair value hierarchy requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair values:

Level 1 inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the Company has – the ability to access at the measurement date.

Level 2 inputs are other than quoted prices included in Level 1 that are observable for the asset or liability either 2 – directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 valuation is generated from model-based techniques that use at least one significant assumption not observable 3 – in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

Impairment of investment securities: Investment securities are evaluated for impairment on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation to determine whether a decline in their value below amortized cost is other-than-temporary. Securities are evaluated for impairment utilizing criteria such as the magnitude and duration of the decline, current market conditions, payment history, the credit worthiness of

the obligor, the intent of the Company to retain the security or whether it is more likely than not that the Company will be required to sell the security before recovery of the value, as well as other qualitative factors. If a decline in value below amortized cost is determined to be other-than-temporary, which does not necessarily indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not favorable, the security is reviewed in more detail in order to determine the portion of the impairment that relates to credit (resulting in a charge to earnings) versus the portion of the impairment that is noncredit related (resulting in a charge to accumulated other comprehensive income). If it is more likely than not that sale of the security will be required prior to recovery of its amortized cost, the entire impairment is recognized in earnings equal to the difference between the amortized cost basis and the fair value. A credit loss is determined by comparing the amortized cost basis to the present value of cash flows expected to be collected, computed using the original yield as the discount rate.

## Recently Issued Accounting Pronouncements

In May 2011, the FASB issued an accounting standards update intended to improve the comparability of fair value accounting and reporting requirements between United States Generally Accepted Accounting Principles (U.S. GAAP) and International Financial Reporting Standards (IFRS). Additional disclosures required by the update are incorporated in Note 11 and include: (i) disclosure of quantitative information regarding the unobservable inputs used in any Level 3 measurement including an explanation of the valuation techniques used and the sensitivity to changes in the values assigned to unobservable inputs; (ii) categorization by level for the fair value of financial instruments; and (iii) instances where the fair values disclosed for non-financial assets were based on a highest and best use assumption when in fact the assets are not being utilized in that capacity. The amendments in the update are effective for the Company's interim and annual reports beginning with the first quarter 2012. The provisions of this update did not have a material impact on the Company's financial position, results of operations or cash flows but did cause changes to the Company's fair value disclosure (see Note 11).

In June 2011, the FASB issued an accounting standards update to increase the prominence of items included in Other Comprehensive Income and facilitate the convergence of U.S. GAAP with IFRS. The update prohibits continued exclusive presentation of Other Comprehensive Income in the statement of stockholders' equity. The update requires that all non-owner changes in stockholders' equity be presented in either a single continuous statement of comprehensive income or in two separate but continuous statements. The amendments in the update are effective for the Company's interim and annual reports beginning with the first quarter 2012. The provisions of this update did not have a material impact on the Company's financial position, results of operations or cash flows but did cause changes to the presentation of the Company's Statements of Operations.

During the first quarter 2012, the FASB issued other accounting standards updates which may impact the banking community or other entities but do not, and are not expected to, have a material impact on our financial position, results of operations or cash flows.

## NOTE 3 — INVESTMENTS

The amortized costs and estimated fair values of investment securities as of March 31, 2012 and December 31, 2011 are as follows:

(\$ in thousands)	Amortized Cost	March 31, 2012		Estimated Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
Securities available-for-sale:				
Corporate	\$ 14,708	\$ 295	\$(262)	\$ 14,741
State and municipal	11,050	220	(80)	11,190
Residential agency mortgage-backed securities ("MBS")	57,797	811	(41)	58,567
Total securities available-for-sale	\$ 83,555	\$ 1,326	\$(383)	\$ 84,498

Edgar Filing: Solera National Bancorp, Inc. - Form 10-Q

(\$ in thousands)

	December 31, 2011			Estimated Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Securities available-for-sale:				
Corporate	\$15,117	\$161	\$(460)	\$14,818
State and municipal	3,691	198	(4)	3,885
Residential agency MBS	63,880	747	(135)	64,492
Total securities available-for-sale	\$82,688	\$1,106	\$(599)	\$83,195

The amortized cost and estimated fair value of debt securities by contractual maturity at March 31, 2012 and December 31, 2011 are shown below. The timing of principal payments received differs from the contractual maturity because borrowers may be required to make contractual principal payments and often have the right to call or prepay obligations with or without call or prepayment penalties. As a result, the timing with which principal payments are received on mortgage-backed securities ("MBS") is not represented in the tables below. For instance, we received \$3.6 million in proceeds from the maturity/call/prepayment of securities during the three months ended March 31, 2012 (see our Consolidated Statements of Cash Flows on page 7) versus no dollars contractually maturing within one year as set forth in the table below.

(\$ in thousands)

	March 31, 2012		December 31, 2011	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Securities available-for-sale:				
Due within one year	\$—	\$—	\$—	\$—
Due after one year through five years	6,987	7,122	8,540	8,583
Due after five years through ten years	20,417	20,546	13,799	13,720
Due after ten years	56,151	56,830	60,349	60,892
Total securities available-for-sale	\$83,555	\$84,498	\$82,688	\$83,195

The following tables show the estimated fair value and gross unrealized losses, aggregated by investment category and length of time the individual securities have been in a continuous loss position as of March 31, 2012 and December 31, 2011.

(\$ in thousands)	March 31, 2012			December 31, 2011			Total		
	Less than 12 months			12 months or more			Total		
Description of securities:	Estimated Fair Value	Unrealized Losses	# of Securities	Estimated Fair Value	Unrealized Losses	# of Securities	Estimated Fair Value	Unrealized Losses	# of Securities
Corporate	\$ 1,506	\$ (44 )	3	\$ 4,282	\$ (218 )	7	\$ 5,788	\$ (262 )	10
State and municipal	5,005	(80 )	9	—	—	—	5,005	(80 )	9
Residential agency MBS	11,287	(41 )	12	—	—	—	11,287	(41 )	12
Total temporarily-impaired	\$ 17,798	\$ (165 )	24	\$ 4,282	\$ (218 )	7	\$ 22,080	\$ (383 )	31

(\$ in thousands)	December 31, 2011			December 31, 2011			Total		
	Less than 12 months			12 months or more			Total		
Description of securities:	Estimated Fair Value	Unrealized Losses	# of Securities	Estimated Fair Value	Unrealized Losses	# of Securities	Estimated Fair Value	Unrealized Losses	# of Securities
Corporate	\$ 1,506	\$ (44 )	3	\$ 4,282	\$ (218 )	7	\$ 5,788	\$ (262 )	10
State and municipal	5,005	(80 )	9	—	—	—	5,005	(80 )	9
Residential agency MBS	11,287	(41 )	12	—	—	—	11,287	(41 )	12
Total temporarily-impaired	\$ 17,798	\$ (165 )	24	\$ 4,282	\$ (218 )	7	\$ 22,080	\$ (383 )	31

Edgar Filing: Solera National Bancorp, Inc. - Form 10-Q

				Value			Value		
Corporate	\$ 4,033	\$ (180 )	8	\$ 4,220	\$ (280 )	7	\$ 8,253	\$ (460 )	15
State and municipal	502	(4 )	1	—	—	—	502	(4 )	1
Residential agency									
MBS	18,266	(135 )	20	—	—	—	18,266	(135 )	20
Total									
temporarily-impaired	\$ 22,801	\$ (319 )	29	\$ 4,220	\$ (280 )	7	\$ 27,021	\$ (599 )	36

Management evaluates investment securities for other-than-temporary impairment taking into consideration the extent and length of time the fair value has been less than cost, the financial condition of the issuer, whether the Company has the intent to retain the security and whether it is more-likely-than-not that the Company will be required to sell the security before recovery of the value, as well as other qualitative factors. As of March 31 2012, no declines were deemed to be other than temporary. The seven corporate securities that were in a continuous loss position for 12 months or longer at March 31, 2012 and December 31, 2011 fluctuated in value primarily as a result of changes in market interest rates rather than due to a material deterioration in credit quality. Further, the Company has the intent to hold the securities in an unrealized loss position as of March 31, 2012 and does not anticipate that these securities will be required to be sold before recovery of value, which may be upon maturity. Accordingly, the securities detailed in the table above, are not other than temporarily impaired. Similarly, management's evaluation of the securities in an unrealized loss position at December 31, 2011, determined these securities were not other than temporarily impaired.

During the first quarter of 2011, the Company recognized other-than-temporary impairment of approximately \$67,000 related to five securities that management had the intent to sell before recovery of value. No other securities were determined to be other than temporarily impaired.

The Company recorded a net unrealized gain in the investment portfolio of \$943,000 at March 31, 2012, an 86% increase over the \$507,000 net unrealized gain at December 31, 2011.

Sales of available-for-sale securities were as follows:

(\$ in thousands)	Three Months Ended March 31,	
	2012	2011
Proceeds	\$ 7,483	\$ 11,350
Gross gains	\$ 114	\$ 146
Gross losses	\$ —	\$ (81 )

Realized gains and losses on sales are computed on a specific identification basis based on amortized cost on the date of sale.

Securities with carrying values of \$20.5 million at March 31, 2012 and \$20.4 million at December 31, 2011, were pledged as collateral to secure public deposits, borrowings from the FHLB, repurchase agreements and for other purposes as required or permitted by law.

#### NOTE 4 — LOANS

The following table sets forth the composition of the loan portfolio according to the loan's purpose, which may differ from the categorization of the loan in subsequent tables which categorize the loan according to the underlying collateral:

(\$ in thousands)	March 31,	December
	2012	31, 2011
Commercial real estate ("CRE")	\$ 37,265	\$ 37,862
Commercial and industrial	5,790	5,971
Residential real estate	10,704	10,460
Construction and land development	1,275	1,307
Consumer	52	45
GROSS LOANS	55,086	55,645



Edgar Filing: Solera National Bancorp, Inc. - Form 10-Q

Net deferred loan expenses / (fees)	1	(77 )
Allowance for loan and lease losses	(1,077 )	(1,067 )
<b>LOANS, NET</b>	<b>\$ 54,010</b>	<b>\$ 54,501</b>

During the first quarter of 2012, the Bank purchased one loan with a principal balance of approximately \$500,000. No loans were purchased during the first quarter of 2011.

In the ordinary course of business, and only if consistent with permissible exceptions to Section 402 of the Sarbanes-Oxley Act of 2002, the Bank may make loans to directors, executive officers, principal stockholders (holders of more than five percent of the outstanding common shares) and the businesses with which they are associated. In the Company's opinion, all loans and loan commitments to such parties are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons.

There were approximately \$301,000 and \$481,000 in loans receivable from related parties at March 31, 2012 and December 31, 2011, respectively.

The Company's loan portfolio generally consists of loans to borrowers within Colorado. Although the Company seeks to avoid concentrations of loans to a single industry or based upon a single class of collateral, the Company's loan portfolio consists primarily of real estate loans secured by real estate located in Colorado, making the value of the portfolio more susceptible to declines in real estate values and other changes in economic conditions in Colorado. No single borrower can be approved for a loan over the Bank's current legal lending limit of approximately \$2.5 million. This regulatory requirement helps to ensure the Bank's exposure to one individual customer is limited.

#### NOTE 5 — ALLOWANCE FOR LOAN AND LEASE LOSSES

Activity in the allowance for loan and lease losses for the three months ended March 31, 2012 and 2011 is summarized as follows:

(\$ in thousands)	Three Months Ended	
	March 31,	
	2012	2011
Balance, beginning of period	\$ 1,067	\$ 1,175
Charge-offs	(3 )	—
Recoveries	13	—
Provision for loan and lease losses	—	—
Balance, end of period	\$ 1,077	\$ 1,175

The following allowance for loan and lease loss disclosures are broken out by portfolio segment. Portfolio segment is defined, under current U.S. GAAP, as the level of aggregation used by the Company to calculate its allowance for loan and lease losses. Our portfolio segments are based on how loans are categorized on the Consolidated Report of Condition and Income, as set forth by banking regulators, (the "Call Report"), which is primarily based on the collateral securing the loan. We have four main portfolio segments as follows:

Commercial Real Estate (CRE) Secured – loans secured by nonfarm, nonresidential properties  
 Residential Real Estate Secured – loans secured by 1-4 family residential properties or land  
 Commercial and Industrial – loans to businesses not secured by real estate, and  
 Consumer – loans to individuals not secured by real estate.

The portfolio segment categorization of loans differs from the categorization shown in Note 4 – Loans. Portfolio segment categorization is based on the Call Report and the loan's underlying collateral while the loan categorization in Note 4 – Loans is based on the loan's purpose as determined during the underwriting process.

The tables below provide a rollforward, by portfolio segment, of the allowance for loan and lease losses for the three months ended March 31, 2012 and 2011, respectively.

Rollforward of Allowance for Loan and Lease Losses by Portfolio Segment

(\$ in thousands)	March 31, 2012				
	Commercial	Residential	Commercial	Consumer	Total
	Real Estate Secured	Real Estate Secured	and Industrial		
Balance at December 31, 2011	\$ 726	\$ 244	\$ 97	\$—	\$ 1,067
Charge-offs	—	—	—	(3 )	(3 )
Recoveries	—	13	—	—	13
Provision for loan and lease losses	(27 )	(10 )	33	4	—
Balance at March 31, 2012	\$ 699	\$ 247	\$ 130	\$ 1	\$ 1,077

Rollforward of Allowance for Loan and Lease Losses by Portfolio Segment

(\$ in thousands)	March 31, 2011				
	Commercial	Residential	Commercial	Consumer	Total
	Real Estate Secured	Real Estate Secured	and Industrial		
Balance at December 31, 2010	\$ 360	\$ 478	\$ 336	\$ 1	\$ 1,175
Charge-offs	—	—	—	—	—
Recoveries	—	—	—	—	—
Provision for loan and lease losses	58	23	(81 )	—	—
Balance at March 31, 2011	\$ 418	\$ 501	\$ 255	\$ 1	\$ 1,175

The following tables present the ending balance in loans and allowance for loan and lease losses, broken down by portfolio segment as of March 31, 2012 and December 31, 2011. The tables also identify the recorded investment in loans and the related allowance that correspond to individual versus collective impairment evaluation as derived from the Company's methodology of estimating the allowance for loan and lease losses (see additional discussion about our allowance methodology under Note 2: Critical Accounting Policies, Provision and allowance for loan and lease losses).

Ending Balances in Loans and Allowance for Loan and Lease Losses by Portfolio Segment

(\$ in thousands)	March 31, 2012				
	Commercial	Residential	Commercial	Consumer	Total
	Real Estate Secured	Real Estate Secured	and Industrial		
<b>Loans</b>					
Individually evaluated for impairment	\$ 647	\$—	\$ 332	\$—	\$ 979
Collectively evaluated for impairment	33,780	15,193	5,082	52	54,107
<b>Total</b>	<b>\$ 34,427</b>	<b>\$ 15,193</b>	<b>\$ 5,414</b>	<b>\$ 52</b>	<b>\$ 55,086</b>
<b>Allowance for loan losses</b>					
Individually evaluated for impairment	\$ 11	\$—	\$ 44	\$—	\$ 55
Collectively evaluated for impairment	688	247	86	1	1,022
<b>Total</b>	<b>\$ 699</b>	<b>\$ 247</b>	<b>\$ 130</b>	<b>\$ 1</b>	<b>\$ 1,077</b>

## Ending Balances in Loans and Allowance for Loan and Lease Losses by Portfolio Segment

(\$ in thousands)	December 31, 2011				Total
	Commercial Real Estate Secured	Residential Real Estate Secured	Commercial and Industrial	Consumer	
<b>Loans</b>					
Individually evaluated for impairment	\$ 274	\$—	\$ 336	\$—	\$ 610
Collectively evaluated for impairment	35,159	14,586	5,245	45	55,035
<b>Total</b>	<b>\$ 35,433</b>	<b>\$ 14,586</b>	<b>\$ 5,581</b>	<b>\$ 45</b>	<b>\$ 55,645</b>
<b>Allowance for loan losses</b>					
Individually evaluated for impairment	\$—	\$—	\$—	\$—	\$—
Collectively evaluated for impairment	726	244	97	—	1,067
<b>Total</b>	<b>\$ 726</b>	<b>\$ 244</b>	<b>\$ 97</b>	<b>\$—</b>	<b>\$ 1,067</b>

The remaining tables in the allowance for loan and lease losses footnote provide detail about loans according to their class, rather than their segment, as reflected above. The class level provides more detail than the portfolio segment level. The following tables contain reconciliation information between the portfolio segment levels and class levels:

## Reconciliation between Portfolio Segment and Class

March 31, 2012 (Principal Balance)

(\$ in thousands)	Class	Portfolio Segment				Total
		Commercial Real Estate Secured	Residential Real Estate Secured	Commercial and Industrial	Consumer	
	CRE – owner occupied	\$ 16,792	\$—	\$—	\$—	\$ 16,792
	CRE – non-owner occupied	16,907	—	—	—	16,907
	Commercial and industrial	—	—	5,414	—	5,414
	Residential real estate	—	14,646	—	—	14,646
	Construction and land development	728	547	—	—	1,275
	Consumer	—	—	—	52	52
	<b>Total</b>	<b>\$ 34,427</b>	<b>\$ 15,193</b>	<b>\$ 5,414</b>	<b>\$ 52</b>	<b>\$ 55,086</b>

## Reconciliation between Portfolio Segment and Class

December 31, 2011 (Principal Balance)

(\$ in thousands)	Class	Portfolio Segment				Total
		Commercial Real Estate Secured	Residential Real Estate Secured	Commercial and Industrial	Consumer	
	CRE – owner occupied	\$ 16,337	\$—	\$—	\$—	\$ 16,337
	CRE – non-owner occupied	18,367	—	—	—	18,367
	Commercial and industrial	—	—	5,581	—	5,581
	Residential real estate	—	14,008	—	—	14,008
	Construction and land development	729	578	—	—	1,307
	Consumer	—	—	—	45	45
	<b>Total</b>	<b>\$ 35,433</b>	<b>\$ 14,586</b>	<b>\$ 5,581</b>	<b>\$ 45</b>	<b>\$ 55,645</b>

## Impaired Loans

The following tables provide detail of impaired loans broken out according to class as of March 31, 2012 and December 31, 2011. The class level represents a slightly more detailed level than the portfolio segment level. There were four impaired loans, totaling \$979,000, as of March 31, 2012 compared to three impaired loans totaling \$610,000 as of December 31, 2011. The recorded investment represents the customer balance less any partial charge-offs and excludes any accrued interest receivable since the majority of the loans were on nonaccrual status and therefore did not have interest accruing. The unpaid principal balance represents the unpaid principal prior to any partial charge-off.

## Impaired Loans by Class as of March 31, 2012

(\$ in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment YTD	Interest Income Recognized YTD
Impaired loans with no related allowance					
CRE – owner occupied	\$—	\$—	\$—	\$—	\$—
CRE – non-owner occupied	251	471	—	265	—
Commercial and industrial	243	243	—	243	—
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Total	\$494	\$714	\$—	\$508	\$—
Impaired loans with a related allowance					
CRE – owner occupied	\$—	\$—	\$—	\$—	\$—
CRE – non-owner occupied	396	396	11	397	3
Commercial and industrial	89	89	44	90	2
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Total	\$485	\$485	\$55	\$487	\$5
Total impaired loans					
CRE – owner occupied	\$—	\$—	\$—	\$—	\$—
CRE – non-owner occupied	647	867	11	662	3
Commercial and industrial	332	332	44	333	2
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Total	\$979	\$1,199	\$55	\$995	\$5

## Impaired Loans by Class as of December 31, 2011

(\$ in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment YTD	Interest Income Recognized YTD
Impaired loans with no related allowance					
CRE – owner occupied	\$—	\$—	\$—	\$—	\$—
CRE – non-owner occupied	274	494	—	345	—
Commercial and industrial	336	336	—	517	15
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Total	\$610	\$830	\$—	\$862	\$ 15
Impaired loans with a related allowance					
CRE – owner occupied	\$—	\$—	\$—	\$—	\$—
CRE – non-owner occupied	—	—	—	—	—
Commercial and industrial	—	—	—	—	—
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Total	\$—	\$—	\$—	\$—	\$—
Total impaired loans					
CRE – owner occupied	\$—	\$—	\$—	\$—	\$—
CRE – non-owner occupied	274	494	—	345	—
Commercial and industrial	336	336	—	517	15
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Total	\$610	\$830	\$—	\$862	\$ 15

As of both March 31, 2012 and December 31, 2011, the impaired loans without a valuation allowance did not have a related allowance because they have either been partially charged-off, bringing them to their net realizable value, or are well-secured.

Troubled debt restructurings (TDRs) are included in impaired loans above. No loans were modified as TDRs during the three months ended March 31, 2012. The Company has not committed additional funds to any of the borrowers whose loans are classified as a TDR. A TDR is considered to be in payment default once it is 90 days past due under the modified terms or when the loan is determined to be uncollectible and is classified as loss and charged-off. None of the Company's loans restructured in the last 12 months have subsequently defaulted.

## Age Analysis of Loans

The following tables summarize, by class, our past due and nonaccrual loans as of the dates indicated.

(\$ in thousands)	30-59 Days Past Due	60-89 Days Past Due	Past Due 90 Days or More and Still Accruing	Nonaccrual	Total Past Due and Nonaccrual	Current	Total
CRE – owner occupied	\$—	\$—	\$—	\$—	\$—	\$16,792	\$16,792
CRE – non-owner occupied	—	—	396	251	647	16,260	16,907
Commercial and industrial	169	—	—	332	501	4,913	5,414
Residential real estate	—	—	—	—	—	14,646	14,646
Construction and land development	—	—	—	—	—	1,275	1,275
Consumer	—	—	—	—	—	52	52
<b>Total</b>	<b>\$169</b>	<b>\$—</b>	<b>\$396</b>	<b>\$583</b>	<b>\$1,148</b>	<b>\$53,938</b>	<b>\$55,086</b>

(\$ in thousands)	30-59 Days Past Due	60-89 Days Past Due	Past Due 90 Days or More and Still Accruing	Nonaccrual	Total Past Due and Nonaccrual	Current	Total
CRE – owner occupied	\$—	\$1,040	\$—	\$—	\$1,040	\$15,297	\$16,337
CRE – non-owner occupied	—	—	—	274	274	18,093	18,367
Commercial and industrial	—	—	—	336	336	5,245	5,581
Residential real estate	139	170	—	—	309	13,699	14,008
Construction and land development	—	—	—	—	—	1,307	1,307
Consumer	—	—	—	—	—	45	45
<b>Total</b>	<b>\$139</b>	<b>\$1,210</b>	<b>\$—</b>	<b>\$610</b>	<b>\$1,959</b>	<b>\$53,686</b>	<b>\$55,645</b>

## Credit Quality Information

The Company uses the following definitions for risk ratings, which are consistent with the definitions used in supervisory guidance and are the same for all classes of loans:

**Special Mention:** Loans in this category have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment at some future date.

Substandard: Loans in this category are inadequately protected by the current sound worth and paying capacity of the borrower or of the collateral pledged, if any. These loans have well-defined weaknesses that jeopardize the liquidation of the debt and have the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

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

Loss: Loans in this category are deemed not collectible and are charged-off.

Loans not meeting any of the definitions above are considered to be pass rated loans.



As of March 31, 2012, and based on the most recent analysis performed during the month of March 2012, the recorded investment in each risk category of loans by class of loan is as follows:

(\$ in thousands)	Special				Total
	Pass	Mention	Substandard	Doubtful	
CRE – owner occupied	\$ 13,512	\$ 1,759	\$ 1,521	\$—	\$ 16,792
CRE – non-owner occupied	15,549	1,107	251	—	16,907
Commercial and industrial	4,825	169	331	89	5,414
Residential real estate	13,989	—	657	—	14,646
Construction and land development	395	—	880	—	1,275
Consumer	52	—	—	—	52
Total	\$48,322	\$3,035	\$ 3,640	\$89	\$55,086

As of December 31, 2011, and based on the most recent analysis performed during the month of December 2011, the recorded investment in each risk category of loans by class of loan is as follows:

(\$ in thousands)	Special				Total
	Pass	Mention	Substandard	Doubtful	
CRE – owner occupied	\$ 14,068	\$ 1,135	\$ 1,134	\$—	\$ 16,337
CRE – non-owner occupied	15,395	1,796	1,176	—	18,367
Commercial and industrial	5,021	—	560	—	5,581
Residential real estate	13,344	—	664	—	14,008
Construction and land development	232	—	1,075	—	1,307
Consumer	45	—	—	—	45
Total	\$48,105	\$2,931	\$ 4,609	\$—	\$55,645

#### NOTE 6 — BANK-OWNED LIFE INSURANCE

During the first quarter of 2012, the Company invested \$2.0 million in bank-owned life insurance on certain key employees. Bank-owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value. Increases in the cash surrender value are recognized as other noninterest income.

#### NOTE 7 — DEPOSITS

Deposits are summarized as follows:

(\$ in thousands)	March 31, 2012		December 31, 2011	
	Amount	% of Total	Amount	% of Total
Noninterest-bearing demand	\$3,217	3 %	\$3,550	3 %
Interest-bearing demand	8,724	7	9,355	8
Money market accounts	10,151	8	9,781	8
Savings accounts	47,352	40	49,073	41
Time deposits, less than \$100,000	4,640	4	5,193	4
Time deposits, \$100,000 or more	45,048	38	42,032	36
Total deposits	\$ 119,132	100 %	\$ 118,984	100 %



In the ordinary course of business, certain officers, directors, stockholders, and employees of the Bank have deposits with the Bank. In the Bank's opinion, all deposit relationships with such parties are made on substantially the same terms including interest rates and maturities, as those prevailing at the time for comparable transactions with other persons. The balance of related party deposits at both March 31, 2012 and December 31, 2011 was approximately \$4.3 million.

#### NOTE 8 — STOCK-BASED COMPENSATION

Under the terms of the Company's Stock Incentive Plan, (the "Plan"), employees may be granted both nonqualified and incentive stock options and directors and other consultants, who are not also officers or employees, may only be granted nonqualified stock options. The Board reserved approximately 510,700 shares of common stock for issuance under the Plan. Of that, approximately 479,000 are issued and outstanding, leaving approximately 31,000 available for future grants as of March 31, 2012. The Plan provides for options to purchase shares of common stock at a price not less than 100% of the fair market value of the stock on the date of grant. Stock options expire no later than ten years from the date of the grant and generally vest over four years. The Plan provides for accelerated vesting if there is a change of control, as defined in the Plan. The Company recognized stock-based compensation cost of approximately \$13,000 and \$61,000 during the three months ended March 31, 2012 and 2011, respectively. No tax benefit related to stock-based compensation will be recognized until the Company demonstrates an ability to maintain profitability.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes-Merton option pricing model. The Company granted 43,750 options during the first quarter 2012 as incentive compensation to employees and 45,000 nonqualified stock options to Directors.

During the three months ended March 31, 2012, 3,750 options were forfeited and 6,042 vested options expired unexercised. During the first quarter 2011, 14,020 options were forfeited and no vested options expired unexercised. No options were exercised during the three months ended March 31, 2012 or 2011. The Company recognized expense for approximately 4,500 options, representing a pro-rata amount of the options earned during the first quarter of 2012 that are expected to vest. As of March 31, 2012, there was approximately \$107,000 of total unrecognized compensation cost related to the outstanding stock options that will be recognized over a weighted-average period of 1.9 years.

The following is a summary of the Company's outstanding stock options and related activity for the three months ended March 31, 2012:

	Options	Weighted-Average Grant Date Fair Value	Weighted-Average Exercise Price
Outstanding at December 31, 2011	400,312	\$ 1.93	\$ 7.62
Granted	88,750	0.62	3.17
Exercised	—	—	—
Forfeited	(3,750 )	0.55	3.00
Expired	(6,042 )	1.83	8.14
Outstanding at March 31, 2012	479,270	\$ 1.70	\$ 6.85

The following is a summary of the Company's outstanding stock options and related activity for the three months ended March 31, 2011:

Options

		Weighted-Average Grant Date Fair Value	Weighted-Average Exercise Price
Outstanding at December 31, 2010	367,790	\$ 2.43	\$ 8.31
Granted	41,000	0.64	3.00
Exercised	—	—	—
Forfeited	(14,020 )	2.29	8.90
Expired	—	—	—
Outstanding at March 31, 2011	394,770	\$ 2.33	\$ 8.89

## NOTE 9 — NONINTEREST EXPENSE

The following table details the items comprising other general and administrative expenses:

(\$ in thousands)	Three Months Ended		Increase/ (Decrease)
	2012	March 31, 2011	
Other general and administrative expenses:			
Data processing	\$74	\$78	\$(4)
FDIC assessment	47	79	(32)
Regulatory and reporting fees	33	34	(1)
OREO expense	22	7	15
Loan and collection expenses	31	13	18
Directors' fees	20	24	(4)
Marketing and promotions	19	16	3
Telephone/communication	12	12	—
Travel and entertainment	12	10	2
Printing, stationery and supplies	6	7	(1)
Dues and memberships	5	6	(1)
Franchise taxes	2	4	(2)
Insurance	12	6	6
ATM and debit card fees	4	4	—
Postage and shipping	3	4	(1)
Training and education	3	4	(1)
Miscellaneous	3	4	(1)
Total	\$308	\$312	\$(4)

## NOTE 10 — COMMITMENTS AND CONTINGENCIES

The Company is a party to credit related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments consist of commitments to extend credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The Company's exposure to credit loss is represented by the contractual amount of these commitments. The Company follows the same credit policies in making commitments as it does for on-balance-sheet instruments.

At March 31, 2012 and December 31, 2011, \$5.5 million and \$6.3 million, respectively, in unfunded commitments were outstanding whose contract amounts represent credit risk.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the commitments do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained is based on management's credit evaluation. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment and income producing commercial properties.

## NOTE 11 — FAIR VALUE

The Company carries its available-for-sale securities at fair value. Fair value measurement is obtained from independent pricing services which utilize 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 bonds' terms and conditions, among other things. As of March 31, 2012 and December 31, 2011, all of the Company's available-for-sale securities were valued using Level 2 inputs.

Impaired loans are evaluated and valued at the time the loan is identified as impaired, at the lower of cost or fair value. Fair value is measured based on the value of the collateral securing these loans or the present value of expected cash flows and is classified as Level 3 in the fair value hierarchy. Collateral may be real estate and/or business assets including equipment, inventory and/or accounts receivable and is determined based on appraisals performed by qualified licensed appraisers hired by the Company. Appraised and reported values may be adjusted based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client and client's business. Such discounts are typically significant and result in a Level 3 classification of the inputs for determining fair value. Impaired loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly.

Other real estate owned is valued at the time the loan is foreclosed upon and the asset is transferred to other real estate owned. The value is based primarily on third party appraisals, less costs to sell. The appraisals may be adjusted based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client and client's business. Such discounts are typically significant and result in a Level 3 classification of the inputs for determining fair value. Other real estate owned is reviewed and evaluated on at least an annual basis for additional impairment and adjusted accordingly.

#### Assets and Liabilities Measured on a Recurring Basis

Assets and liabilities measured at fair value on a recurring basis are summarized below:

(\$ in thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets at March 31, 2012				
Investment securities, available-for-sale:				
Corporate	\$—	\$14,741	\$ —	\$14,741
State and municipal	—	11,190	—	11,190
Residential agency MBS	—	58,567	—	58,567
Total	\$—	\$84,498	\$ —	\$84,498
Assets at December 31, 2011				
Investment securities, available-for-sale:				
Corporate	\$—	\$14,818	\$ —	\$14,818
State and municipal	—	3,885	—	3,885
Residential agency MBS	—	64,492	—	64,492
Total	\$—	\$83,195	\$ —	\$83,195

There were no transfers in or out of the levels during the periods presented.

#### Assets and Liabilities Measured on a Nonrecurring Basis

Assets and liabilities measured at fair value on a nonrecurring basis are summarized below:

(\$ in thousands)	Quoted Prices in Active	Significant Other Observable	Significant Unobservable Inputs	Total
-------------------	-------------------------------	------------------------------------	---------------------------------------	-------

Edgar Filing: Solera National Bancorp, Inc. - Form 10-Q

	Markets for Identical Assets (Level 1)	Inputs (Level 2)	(Level 3)	
Assets at March 31, 2012				
Impaired loans (Financial)	\$—	\$—	\$ 718	\$718
Other real estate owned (Non-financial)	\$—	\$—	\$ 1,989	\$1,989
Assets at December 31, 2011				
Impaired loans (Financial)	\$—	\$—	\$ 311	\$311
Other real estate owned (Non-financial)	\$—	\$—	\$ 1,989	\$1,989



Impaired loans, which are measured for impairment using either the fair value of collateral or present value of expected cash flows, had carrying amounts at March 31, 2012 totaling \$979,000 after partial charge-offs of \$220,000, which were recorded in 2011. In addition, these loans have specific valuation allowances of \$55,000 at March 31, 2012 and \$37,000 of estimated selling costs which reduced the carrying value. Of the \$979,000 of impaired loans at March 31, 2012, \$736,000 were carried at fair value adjusted for the aforementioned charge-offs, estimated selling costs and specific valuation allowance. The remaining \$243,000 was carried at cost at March 31, 2012, as the fair value of collateral or expected cash flows on these loans exceeded the book value.

Impaired loans at December 31, 2011 had carrying amounts totaling \$610,000 after partial charge-offs of \$220,000. These impaired loans had no specific valuation allowance at December 31, 2011. In addition, impaired loans had \$37,000 of estimated selling costs which reduced the carrying value. Of the \$610,000 of impaired loans at December 31, 2011, \$274,000 were carried at fair value adjusted for the aforementioned charge-offs, estimated selling costs and specific valuation allowance. The remaining \$336,000 were carried at cost at December 31, 2011, as the fair value of collateral or expected cash flows on these loans exceeded the book value.

Other real estate owned (OREO) is real property taken by the Company either through foreclosure or through deed in lieu of foreclosure. The fair value of OREO is based on property appraisals adjusted at management's discretion to reflect further decline in fair value since the time the appraisal analysis was completed, if warranted. Therefore, the inputs used to determine the fair value of OREO fall within Level 3. OREO had a carrying amount of \$1.8 million at both March 31, 2012 and December 31, 2011, based on the current appraisals less reasonable costs to sell of approximately \$253,000 for the Company's two OREO properties. This value included partial charge-offs of \$40,000 which were recorded during 2011.

The following table provides information describing the valuation process used to determine recurring and nonrecurring fair value measurements categorized within Level 3 of the fair value hierarchy:

Asset Type	Valuation Method	Unobservable Inputs	Range
Impaired Loans	Property appraisals	Management discount for property type and/or recent market volatility	0 % - 20 % discount
	Discounted cash flow	Estimated loss probability based on management's knowledge of client or client's business	0 % - 50 % discount
OREO	Property appraisals	Management discount for property type, recent market volatility, and/or management's knowledge of client or client's business	0 % - 20 % discount

#### Fair Value of Financial Instruments

Disclosure of fair value information about financial instruments, whether or not recognized in the consolidated balance sheets, for which it is practicable to estimate such value is required by U.S. GAAP. Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instrument. Because no market value exists for a significant portion of the financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of

various financial instruments, and other factors. These estimates are subjective in nature, involve uncertainties and matters of judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value information is not required to be disclosed for certain financial instruments and all nonfinancial instruments. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the financial instruments held by the Company. Fair value estimates are based on financial instruments both on and off the balance sheet without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Additionally, tax consequences related to the realization of the unrealized gains and losses can have a potential effect on fair value estimates and have not been considered in many of the estimates.

The following methods and assumptions were used to estimate the fair value of significant financial instruments:

Cash and cash equivalents: The carrying amounts of cash and due from banks approximate their fair values.

Interest-bearing deposits with banks: The carrying amount of interest-bearing deposits with banks approximates fair values due to the relatively stable level of short-term interest rates.

Investment securities: Fair value measurement is obtained from independent pricing services which utilize 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 bonds' terms and conditions, among other things.

Loans, net: The fair value of fixed rate loans is estimated by discounting the future cash flows using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are estimated to be equivalent to carrying values. Variable rate loans that are currently priced at their contractual floor or ceiling, and thus similar to fixed rate loans, are reviewed to determine the interest rate that would be currently offered on similar credits. If the current floor/ceiling rate is equivalent to current market rates, fair value is estimated to be equivalent to carrying value. If the current market rates differ from the loan's current rate, the contractual cash flows are discounted using the current market rate to derive the loan's estimated fair value. Both the estimated fair value and the carrying value have been reduced by specific and general reserves for loan losses.

Investment in FHLB and Federal Reserve Bank stocks: It is not practical to determine the fair value of bank stocks due to the restrictions placed on the transferability of FHLB stock and Federal Reserve Bank stock.

Bank-owned life insurance: The carrying amount of bank-owned life insurance is based on the cash surrender value of the policies which is a reasonable estimate of fair value.

Accrued interest receivable: The carrying value of interest receivable approximates fair value due to the short period of time between accrual and receipt of payment.

Deposits: The fair value of noninterest-bearing demand deposits, interest-bearing demand deposits and savings and money market accounts is determined to be the amount payable on demand at the reporting date. The fair value of fixed rate time deposits is estimated using a discounted cash flow calculation that applies interest rates currently being offered for deposits of similar remaining maturities. Carrying value is assumed to approximate fair value for all variable rate time deposits.

Securities sold under agreements to repurchase: The carrying amount of securities sold under agreements to repurchase approximates fair value due to the short-term nature of these agreements, which generally mature within one to four days from the transaction date.

Federal funds purchased: The carrying amount of federal funds purchased approximates fair value due to their short-term nature.

Federal Home Loan Bank advances: Fair value of the Federal Home Loan Bank advances is estimated using a discounted cash flow model based on current market rates for similar types of borrowing arrangements including similar remaining maturities.

Accrued interest payable: The carrying value of interest payable approximates fair value due to the short period of time between accrual and payment.

Loan commitments: The fair values of commitments are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. The difference between the carrying value of commitments to fund loans or standby letters of credit and their fair values are not significant and, therefore, are not included in the following table.

The carrying amounts and estimated fair values of financial instruments are summarized as follows:

(\$ in thousands)	Carrying Value	Fair Value Measurements at March 31, 2012			
		Level 1	Level 2	Level 3	Total
<b>Financial Assets:</b>					
Cash and cash equivalents	\$729	\$729	\$—	\$—	\$729
Interest-bearing deposits with banks	357	—	357	—	357
Investment securities	84,498	—	84,498	—	84,498
Loans, net	54,010	—	—	54,196	54,196
FHLB and FRB stocks	1,148	—	—	NA	NA
Bank-owned life insurance	2,008	—	—	2,008	2,008
Accrued interest receivable	666	—	503	163	666
<b>Financial Liabilities:</b>					
Deposits, demand, savings and money market	\$69,444	\$—	\$69,444	\$—	\$69,444
Time deposits	49,688	—	50,473	—	50,473
Securities sold under agreements to repurchase	253	—	253	—	253
Federal funds purchased	410	410	—	—	410
FHLB advances	6,500	—	6,693	—	6,693
Accrued interest payable	62	—	62	—	62

(\$ in thousands)	Carrying Value	Fair Value Measurements at December 31, 2011			
		Level 1	Level 2	Level 3	Total
<b>Financial Assets:</b>					
Cash and cash equivalents	\$1,800	\$1,800	\$—	\$—	\$1,800
Interest-bearing deposits with banks	1,357	—	1,357	—	1,357
Investment securities	83,195	—	83,195	—	83,195
Loans, net	54,501	—	—	54,788	54,788
FHLB and FRB stocks	1,134	—	—	NA	NA
Accrued interest receivable	584	—	423	161	584
<b>Financial Liabilities:</b>					
Deposits, demand, savings and money market	\$71,759	\$—	\$71,759	\$—	\$71,759
Time deposits	47,225	—	47,917	—	47,917
Securities sold under agreements to repurchase	253	—	253	—	253
FHLB advances	6,500	—	6,692	—	6,692
Accrued interest payable	56	—	56	—	56

#### NOTE 12 – LEGAL CONTINGENCIES

In the ordinary course of our business, we are party to various legal actions, which we believe are incidental to the operation of our business. Although the ultimate outcome and amount of liability associated with these legal actions, if any, cannot presently be ascertained with certainty, in the opinion of management, based upon information currently available to us, any resulting liability is not likely to have a materially adverse effect on the Company's consolidated financial position, results of operations or cash flows.

#### NOTE 13 – CONSENT ORDER

On December 16, 2010, pursuant to a Stipulation and Consent to the Issuance of a Consent Order, Solera National Bank consented and agreed to the issuance of an Amended Consent Order (the "Consent Order") by the Office of the Comptroller of the Currency (OCC). The Consent Order replaced and superseded the consent order entered into on March 18, 2010 by the Bank. The provisions of the Consent Order shall remain effective and enforceable, except to the extent that, and until such time as, any provisions of the Consent Order have been amended, suspended, waived, or terminated in writing by the OCC. The Consent Order is based on the findings of the OCC during an examination that began on September 6, 2010 and requires the Bank to submit written plans within certain timeframes to address the following items, among others: compliance with the Bank Secrecy Act, revisions to the Bank's loan policy and procedures, weaknesses in the Bank's credit risk management and underwriting, and credit risk associated with the Bank's Home Equity Line of Credit portfolio. For a complete description of the items in the Stipulation and Consent Order please see Exhibits 10.16 and 10.17 to our Annual Report on Form 10-K, filed with the SEC on March 27, 2012.

Since the completion of the examination, the Bank and its Board of Directors have taken steps to address the findings of the examination and have addressed the matters in the Consent Order by the respective deadline dates. The Bank did not admit any wrongdoing in entering into the Consent Order, and in connection with the actions outlined in the Consent Order, is committed to establishing stronger banking practices.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis presents the Company's consolidated financial condition as of March 31, 2012 and results of operations for the three months ended March 31, 2012 and 2011. The discussion should be read in conjunction with the financial statements and the notes related thereto which appear elsewhere in this Quarterly Report on Form 10-Q.

### Executive Overview

We are a Delaware corporation that was incorporated to organize and serve as the holding company for Solera National Bank, a national bank that opened for business on September 10, 2007. Solera National Bank is a full-service commercial bank headquartered in Lakewood, Colorado primarily serving the six-county Denver metropolitan area. Our main banking office is located at 319 S. Sheridan Blvd., Lakewood, Colorado 80226. Our telephone number is (303) 209-8600.

Earnings are derived primarily from net interest income, which is interest income less interest expense, and noninterest income earned from gains on sales of investment securities, increased cash surrender value on bank-owned life insurance policies, and banking service fees, offset by noninterest expense and provision for loan losses. As the majority of assets are interest-earning and liabilities are interest-bearing, changes in interest rates impact net interest margin. We manage interest-earning assets and interest-bearing liabilities to reduce the impact of interest rate changes on operating results.

We offer a broad range of commercial and consumer banking services to small and medium-sized businesses, licensed professionals and individuals who are particularly responsive to the personalized service that Solera National Bank provides to its customers. We believe that local ownership and control allows the Bank to serve customers efficiently and effectively. Solera National Bank competes on the basis of providing a unique and personalized banking experience combined with a broad range of services, customized and tailored to fit the individual needs of its clients. While the Bank seeks to serve the entire market, it focuses on serving the local Hispanic and other minority populations which it believes are currently underserved. Since opening the bank in September of 2007, management has successfully executed its strategy of delivering prudent and controlled growth to efficiently leverage the Company's capital and expense base with the goal of achieving sustained profitability.

Since we operate in Colorado, our operating results are significantly influenced by economic conditions in Colorado, particularly the health of the real estate market. Additionally, we are subject to competition from other financial institutions and are impacted by fiscal and regulatory policies of the federal government as well as regulatory oversight by the Office of the Comptroller of the Currency, (the "OCC").

### Comparative Results of Operations for the Three Months Ended March 31, 2012 and 2011

The following discussion focuses on the Company's financial condition and results of operations for the three months ended March 31, 2012 compared to the financial condition and results of operations for the three months ended March 31, 2011.

Net loss for the quarter ended March 31, 2012 was \$39,000, or (\$0.02) per share, compared with net loss of \$183,000, or (\$0.07) per share, for the first quarter of 2011. The \$144,000 favorable variance in the first quarter 2012 compared to the first quarter 2011 was primarily the result of the following: 1) a \$116,000 favorable variance in realized gains on available-for-sale securities, 2) a \$138,000 favorable variance in salaries and employee benefits, partially offset by 3) a \$108,000 unfavorable variance in net interest income after provision for loan and lease losses. These variances

are explained in more detail in the ensuing discussion.



As of March 31, 2012, the Company had total assets of \$146.2 million, an increase of \$808,000, or 0.6%, from December 31, 2011. Net loans decreased 0.9%, from \$54.5 million at December 31, 2011 to \$54.0 million at March 31, 2012. Similarly, the Company's total deposits remained relatively unchanged growing 0.1% to \$119.1 million as of March 31, 2012.

The following table presents, for the periods indicated, average assets, liabilities and stockholders' equity, as well as the components of net interest income and the resultant annualized yields / costs expressed in percentages.

Table 1

(\$ in thousands)	Three Months Ended March 31, 2012			Three Months Ended March 31, 2011		
	Average Balance	Interest	Yield / Cost	Average Balance	Interest	Yield / Cost
Assets:						
Interest-earning assets:						
Gross loans, net of unearned fees	\$54,541	\$788	5.81 %	\$58,181	\$824	5.74 %
Investment securities**	83,555	503	2.42	73,940	673	3.69
FHLB and FRB stocks	1,139	8	2.86	1,158	9	3.13
Federal funds sold	623	—	0.23	610	—	0.22
Interest-bearing deposits with banks	412	2	1.97	399	1	0.58
Total interest-earning assets	140,270	\$1,301	3.73 %	134,288	\$1,507	4.55 %
Noninterest-earning assets	4,335			3,151		
Total assets	\$144,605			\$137,439		
Liabilities and Stockholders' Equity:						
Interest-bearing liabilities:						
Money market and savings deposits	\$58,660	\$111	0.76 %	\$60,290	\$179	1.20 %
Interest-bearing checking accounts	8,969	19	0.87	11,425	33	1.19
Time deposits	47,195	170	1.45	37,937	157	1.68
Securities sold under agreements to repurchase and federal funds purchased	509	1	0.78	600	2	1.13
FHLB advances	6,500	31	1.90	6,431	57	3.62
Other borrowings	26	—	8.89	71	2	9.55
Total interest-bearing liabilities	121,859	\$332	1.10 %	116,754	\$430	1.49 %
Noninterest-bearing checking accounts	3,219			2,304		
Noninterest-bearing liabilities	452			339		
Stockholders' equity	19,075			18,042		
Total liabilities and stockholders' equity	\$144,605			\$137,439		
Net interest income		\$969			\$1,077	
Net interest spread		2.63 %			3.06 %	

---

Net interest margin	2.78	%	3.25	%
---------------------	------	---	------	---

\*\*Yields on investment securities have not been adjusted to a tax-equivalent basis.

The following table presents the dollar amount of changes in interest income and interest expense for the major categories of interest-earning assets and interest-bearing liabilities. The information details the changes attributable to a change in volume (i.e. change in average balance multiplied by the prior-period average rate) and changes attributable to a change in rate (i.e. change in average rate multiplied by the prior-period average balance). There is a component that is attributable to both a change in volume and a change in rate. This component has been allocated proportionately to the rate and volume columns.

Table 2

(\$ in thousands)	Three Months Ended March 31, 2012 Compared to Three Months Ended March 31, 2011		
	Net Change	Rate	Volume
<b>Interest income:</b>			
Gross loans, net of unearned fees	\$(36 )	\$9	\$(45 )
Investment securities	(170 )	(273 )	103
FHLB and FRB stocks	(1 )	(1 )	—
Federal funds sold	—	—	—
Interest-bearing deposits with banks	1	1	—
<b>Total interest income</b>	<b>\$(206 )</b>	<b>\$(264 )</b>	<b>\$58</b>
<b>Interest expense:</b>			
Money market and savings deposits	\$(68 )	\$(63 )	\$(5 )
Interest-bearing checking accounts	(14 )	(8 )	(6 )
Time deposits	13	(17 )	30
Securities sold under agreements to repurchase and federal funds purchased	(1 )	2	(3 )
F HLB advances	(26 )	(26 )	—
Other borrowings	(2 )	—	(2 )
<b>Total interest expense</b>	<b>\$(98 )</b>	<b>\$(112 )</b>	<b>\$14</b>
<b>Net interest income</b>	<b>\$(108 )</b>	<b>\$(152 )</b>	<b>\$44</b>

#### Net Interest Income and Net Interest Margin

Net interest income is the difference between interest and fee income, principally from loan and investment security portfolios, and interest expense, principally on customer deposits and borrowings. Net interest income is our principal source of earnings. Changes in net interest income result from changes in volume, spread and margin. Volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities. Spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities. Margin refers to net interest income divided by average interest-earning assets, and is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities.

For the three months ended March 31, 2012, the Company's net interest income decreased \$108,000, or 10%, compared to the three months ended March 31, 2011. The Company experienced a 47 basis point decrease in net interest margin declining from 3.25% for the first quarter 2011 to 2.78% for the first quarter 2012. The decrease was primarily due to the rate on interest-bearing assets declining by more than the rate on interest-bearing liabilities, combined with an unfavorable shift in volume from higher-yielding loans to lower-yielding investment securities.



Most notable was the unfavorable decrease in yield on the Company's investment securities, down 127 basis points from the prior year which was primarily attributable to the sale of longer-maturity, higher-yielding investments, along with principal payments received on mortgage-backed securities, which were reinvested in bonds that are earning at historically low rates. This unfavorable decrease in rate was partially offset by a favorable decrease in the cost of interest-bearing liabilities, which declined 39 basis points from the comparable period in the prior year. Contributing most significantly to the decline in interest-bearing liability costs was the \$68,000 decrease in interest expense related to money market and saving deposits which is a direct result of management's efforts to re-price many of its deposit products from higher promotional rates to lower, yet still competitive, rates following general market interest rate declines. Additionally, the Company realized a \$26,000 favorable decrease on the cost of FHLB advances due to the restructuring of \$3.5 million in fixed-rate advances during the fourth quarter 2011 that reduced the effective interest rate from 4.37% to 2.14% and extended the average maturity of those borrowings.

The combination of the aforementioned factors resulted in further compression in the Company's net interest spread (the yield earned on interest-earning assets less the cost of interest-bearing liabilities) which declined 43 basis points from 3.06% for the quarter ended March 31, 2011 to 2.63% for the quarter ended March 31, 2012.

#### Provision for Loan Losses

We determine a provision for loan losses that we consider sufficient to maintain an allowance to absorb probable losses inherent in our portfolio as of the balance sheet date. For additional information concerning this determination, see the section of this discussion and analysis captioned "Financial Condition, Allowance for Loan and Lease Losses."

During the first quarter of 2012, we did not recognize any provision for loan losses reflecting minimal change in the size of the Bank's loan portfolio and what we believe to be stabilizing asset quality. See additional discussion below under Financial Condition, Loan Portfolio.

#### Noninterest Income

Noninterest income for the quarter ended March 31, 2012 was \$138,000, an increase of \$122,000 from \$16,000 for the first quarter 2011. The Company sold securities for gains of \$114,000 during the first quarter 2012. This compared to net gains on the sale of investment securities of \$65,000 during the first quarter 2011 offset by \$67,000 of other-than-temporary impairment recognized on five securities which the Company did not have the intent to hold until recovery of value. Gains on the sale of securities are not part of the Bank's expected ongoing operations and should not be considered recurring. Additionally, the Company recognized \$9,000 of other income during the first quarter 2012, compared to \$0 during the first quarter 2011 primarily due to increases in the cash surrender value of bank-owned life insurance which the Company purchased during the first quarter 2012.

Service charges on deposits remained relatively unchanged from first quarter 2011 decreasing \$3,000 during first quarter 2012.

#### Noninterest Expense

Our total noninterest expense for the quarter ended March 31, 2012 was \$1.1 million, a decrease of \$130,000, or 10%, from the quarter ended March 31, 2011. The variance was due to a decrease in salaries and employee benefits of \$138,000, or 20%, primarily from \$88,000 in severance incurred during the first quarter 2011 to the Bank's former executive vice president and chief lending officer, along with a reduction of \$48,000 in stock option expense during the first quarter 2012.

Occupancy expense remained constant quarter-over-quarter decreasing only \$6,000, or 5%, primarily due to a lease extension that was negotiated at reduced rates.

Professional fees increased \$18,000, or 14%, quarter-over-quarter primarily due to an increase in costs associated with internal audits, which is the result of changes in the timing of these reviews which historically have not occurred during the first quarter.

Other general and administrative expenses remained relatively unchanged from the first quarter 2011 decreasing \$4,000 or 1%, quarter-over-quarter, as detailed in the following table:

(\$ in thousands)	Three Months Ended		Increase/ (Decrease)
	March 31,		
Other general and administrative expenses:	2012	2011	
Data processing	\$ 74	\$ 78	\$ (4 )
FDIC assessment	47	79	(32 )
Regulatory and reporting fees	33	34	(1 )
OREO expense	22	7	15
Loan and collection expenses	31	13	18
Directors' fees	20	24	(4 )
Marketing and promotions	19	16	3
Telephone/communication	12	12	—
Travel and entertainment	12	10	2
Printing, stationery and supplies	6	7	(1 )
Dues and memberships	5	6	(1 )
Franchise taxes	2	4	(2 )
Insurance	12	6	6
ATM and debit card fees	4	4	—
Postage and shipping	3	4	(1 )
Training and education	3	4	(1 )
Miscellaneous	3	4	(1 )
Total	\$ 308	\$ 312	\$ (4 )

The most significant changes included a \$32,000 decrease in FDIC assessments due primarily to a change in the assessment methodology which, beginning in the second quarter 2011, moved from being based on total deposit liabilities to being based on average consolidated total assets which resulted in a favorable shift for the Company. This cost savings was partially offset by a \$15,000 increase in OREO expenses related to the Company's increase in OREO. We expect this trend to continue to impact our 2012 operating results as we incur costs such as taxes, insurance, operating, repair, etcetera on these properties. Similarly, the \$18,000 increase in loan and collection expense was primarily related to increased workout costs associated with problem loans. Finally, the Company experienced a \$6,000 increase in insurance costs directly related to increased insurance coverage obtained during the third quarter 2011. As reflected in the table above, all other costs remained consistent with the first quarter 2011.

#### Income Taxes

No federal or state tax expense has been recorded for the three months ended March 31, 2012 and 2011, based upon significant operating loss carry-forwards that can be used to offset approximately \$3.4 million of taxable income for federal tax purposes. Since it is uncertain that the Company will achieve sustained profitability, the deferred tax benefit accumulated to date has a full valuation allowance so that the net deferred tax benefit at March 31, 2012 and December 31, 2011 is \$0.

#### Financial Condition

At March 31, 2012, the Company had total assets of \$146.2 million, an \$808,000 increase from \$145.4 million in total assets at December 31, 2011. As of March 31, 2012, stockholders' equity was \$19.4 million a \$410,000 increase over \$19.0 million at December 31, 2011. The increase was primarily due to the \$436,000 of other comprehensive income related to changes in the fair value of available-for-sale securities in addition to \$13,000 of stock-based compensation

expense related to the Company's stock incentive plan and offset by the \$39,000 loss for the three months ended March 31, 2012.

Key Ratios

Ratio:	March 31, 2012		December 31, 2011	
Return on Average Assets	(0.03	)%	0.17	%
Return on Average Equity	(0.20	)%	1.29	%
Average Equity to Average Assets	13.19	%	13.39	%



## Federal Home Loan Bank (FHLB) and Federal Reserve Bank Stocks

At March 31, 2012, the Bank had a total of \$1.1 million invested in FHLB and Federal Reserve Bank stocks carried at cost consisting of \$500,000 in Federal Reserve Bank stock and \$648,000 in FHLB stock. These investments allow Solera National Bank to conduct business with these entities. As of March 31, 2012, the Federal Reserve Bank stock was yielding an average rate of 6.0% and the FHLB stock was yielding an average rate of 0.7%.

## Investment Securities

Our investment portfolio serves as a source of interest income, a source of liquidity and a management tool for managing interest rate sensitivity. We manage our investment portfolio according to a written investment policy approved by our Board of Directors.

At March 31, 2012, Solera National Bank's securities consisted of available-for-sale securities of \$84.5 million. The following tables set forth the estimated market values and approximate weighted average yields of the debt securities in the investment portfolio by contractual maturity at March 31, 2012 and December 31, 2011:

		At March 31, 2012							
(\$ in thousands)		Within One Year		After One Year but within Five Years		After Five Years but within Ten Years		After Ten Years	
Securities available-for-sale	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	
Corporate	\$ —	— %	\$ 5,326	3.35 %	\$ 9,415	3.99 %	\$ —	— %	
State and municipal	—	—	1,796	4.33	7,672	3.71	1,722	2.93	
Residential agency MBS	—	—	—	—	3,459	2.80	55,108	2.16	
Total	\$ —	— %	\$ 7,122	3.59 %	\$ 20,546	3.69 %	\$ 56,830	2.19 %	

  

		At December 31, 2011							
(\$ in thousands)		Within One Year		After One Year but within Five Years		After Five Years but within Ten Years		After Ten Years	
Securities available-for-sale	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	
Corporate	\$ —	— %	\$ 6,794	3.39 %	\$ 8,024	4.14 %	\$ —	— %	
State and municipal	—	—	1,789	4.33	2,096	4.39	—	—	
Residential agency MBS	—	—	—	—	3,600	2.86	60,892	2.00	
Total	\$ —	— %	\$ 8,583	3.59 %	\$ 13,720	3.84 %	\$ 60,892	2.00 %	



## Loan Portfolio

The following table presents the composition of our loan portfolio by category as of the dates indicated:

(\$ in thousands)	March 31, 2012		December 31, 2011		
	Amount	% of Total	Amount	% of Total	%
Commercial real estate	\$37,265	68	% \$37,862	68	%
Commercial and industrial	5,790	11	5,971	11	
Residential real estate	10,704	19	10,460	19	
Construction and land development	1,275	2	1,307	2	
Consumer	52	—	45	—	
GROSS LOANS	55,086	100	% 55,645	100	%
Deferred loan expenses / (fees), net	1		(77 )		
Allowance for loan and lease losses	(1,077 )		(1,067 )		
LOANS, NET	\$54,010		\$54,501		

As of March 31, 2012, net loans were \$54.0 million, relatively unchanged from \$54.5 million at December 31, 2011. Net loans were 37% of total assets at both March 31, 2012 and December 31, 2011. The Bank closed approximately \$1.3 million in new originations during the quarter which was offset by approximately \$1.8 million in loan pay downs, primarily the result of intense competition for strong loan customers.

Loan concentrations are considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities that would cause them to be similarly impacted by economic or other conditions. The Company's loan portfolio generally consists of loans to borrowers within Colorado. Although the Company seeks to avoid concentrations of loans to a single industry or based upon a single class of collateral, the Company's loan portfolio consists primarily of real estate loans secured by real estate located in Colorado, making the value of the portfolio more susceptible to declines in real estate values and other changes in economic conditions in Colorado. No single borrower can be approved for a loan over the Bank's current legal lending limit of approximately \$2.5 million. This regulatory requirement helps to ensure the Bank's exposure to one individual customer is limited.

Management may renew loans at maturity when requested by a customer whose financial strength appears to support such a renewal or when such a renewal appears to be in the best interest of Solera National Bank. Solera National Bank requires payment of accrued interest in such instances and may adjust the rate of interest, require a principal reduction, or modify other terms of the loan at the time of renewal.

The following tables set forth information at March 31, 2012 and December 31, 2011, regarding the dollar amount of loans maturing in the Bank's portfolio based on the contractual terms to maturity. The tables do not give effect to potential prepayments or contractual principal payments.

(\$ in thousands)	March 31, 2012				
	<1 Year	1 - 5 Years	5 - 15 Years	Over 15 Years	Total Loans
Commercial real estate	\$1,909	\$12,220	\$22,636	\$500	\$37,265
Commercial and industrial	2,710	3,078	2	—	5,790
Residential real estate	—	2,478	1,193	7,033	10,704
Construction and land development	1,124	151	—	—	1,275
Consumer	20	22	—	10	52
Gross Loans Receivable	\$5,763	\$17,949	\$23,831	\$7,543	\$55,086



(\$ in thousands)	December 31, 2011				Total Loans
	<1 Year	1 - 5 Years	5 – 15 Years	Over 15 Years	
Commercial real estate	\$805	\$13,064	\$23,993	\$—	\$37,862
Commercial and industrial	2,422	2,787	762	—	5,971
Residential real estate	—	2,461	1,200	6,799	10,460
Construction and land development	1,150	157	—	—	1,307
Consumer	11	24	—	10	45
Gross Loans Receivable	\$4,388	\$18,493	\$25,955	\$6,809	\$55,645

#### Nonperforming Loans, Leases and Assets

Nonperforming assets consist of loans and leases on nonaccrual status, loans 90 days or more past due and still accruing interest, loans that have been restructured resulting in a reduction or deferral of interest or principal, other real estate owned (OREO), and other repossessed assets. As of March 31, 2012, there were \$2.8 million in nonperforming assets.

The following table summarizes information regarding nonperforming assets:

(\$ in thousands)	March 31, 2012	December 31, 2011		
Nonaccrual loans and leases	\$583	\$610		
Other impaired loans	396	—		
Total nonperforming loans	979	610		
Other real estate owned	1,776	1,776		
Total nonperforming assets	\$2,755	\$2,386		
Nonperforming loans	\$979	\$610		
Allocated allowance for loan and lease losses to nonperforming loans	55	—		
Net investment in nonperforming loans	\$924	\$610		
Accruing loans past due 90 days or more	\$396	\$—		
Loans past due 30-89 days	\$169	\$1,349	(1)	
Loans charged-off, year-to-date	\$3	\$276		
Recoveries, year-to-date	(13)	(13)	)	)
Net charge-offs, year-to-date	\$(10)	\$263	)	)
Allowance for loan and lease losses	\$1,077	\$1,067		
Allowance for loan and lease losses to loans, net of deferred fees/expenses	1.96	1.92	%	%
Allowance for loan and lease losses to nonaccrual loans	185.73	174.92	%	%
Allowance for loan and lease losses to nonperforming loans	110.01	174.92	%	%
Nonaccrual loans to loans, net of deferred fees/expenses	1.06	1.10	%	%
Loans 30-89 days past due to loans, net of deferred fees/expenses	0.31	2.43	%	%
Nonperforming assets to total assets	1.88	1.64	%	%

(1) The \$1.3 million of past due loans at December 31, 2011 were brought current as of January 10, 2012.



Federal regulations require that each insured financial institution classify its assets on a regular basis. In addition, in connection with examinations of insured institutions, regulatory examiners have authority to identify problem assets and, if appropriate, classify them. The Bank has established three classifications for potential problem assets: “substandard,” “doubtful” and “loss.” Loans classified as “substandard” are those loans with well-defined weaknesses, such that future capacity to repay the loan has been negatively impacted. Loans classified as “doubtful” are those loans that have characteristics similar to substandard loans, but the weaknesses have moved to the point where complete collection of the obligation from all sources is unlikely and a portion of the principal may be charged-off. Although loans classified as substandard do not duplicate loans classified as doubtful, both substandard and doubtful loans may include some loans that are past due at least 90 days, are on nonaccrual status or have been restructured. Loans classified as “loss” are those loans that are in the process of being charged-off. At March 31, 2012, Solera National Bank had substandard loans totaling \$3.6 million, a doubtful loan totaling \$89,000, and no loans classified as loss. Of the \$3.6 million in substandard loans, only \$494,000 was 30 days or more past due. As of December 31, 2011, the Bank had \$4.6 million classified as substandard and no loans classified as doubtful or loss.

#### Allowance for Loan and Lease Losses

Implicit in Solera National Bank’s lending activities is the fact that loan losses will be experienced and that the risk of loss will vary with the type of loan being made and the creditworthiness of the borrower over the term of the loan. To reflect the currently perceived risk of loss associated with the loan portfolio, additions are made to the allowance for loan and lease losses in the form of direct charges against income to ensure that the allowance is available to absorb possible loan losses. The Bank’s allowance for estimated loan and lease losses is based on a number of quantitative and qualitative factors. Factors used to assess the adequacy of the allowance for loan and lease losses are established based upon management’s assessment of the credit risk in the portfolio, historical loan loss, changes in the size, composition and concentrations of the loan portfolio, general economic conditions, and changes in the legal and regulatory environment, among others. In addition, because the Bank has a limited history on which to base future loan losses, a comparison of peer group allowance ratios to gross loans is made with the intention of maintaining similar levels of reserves.

Provisions for loan and lease losses may be provided both on a specific and general basis. Specific and general valuation allowances are increased by provisions charged to expense and decreased by charge-offs of loans, net of recoveries. Specific allowances are provided for impaired loans for which the expected loss is measurable. General valuation allowances are provided based on a formula that incorporates the factors discussed above. The Bank periodically reviews the assumptions and formula by which additions are made to the specific and general valuation allowances for losses in an effort to refine such allowances in light of the current status of the aforementioned factors.

The amount of the allowance equals the cumulative total of the provisions made from time to time, reduced by loan charge-offs and increased by recoveries of loans previously charged-off. The allowance was \$1.1 million, or 1.96% of outstanding principal as of March 31, 2012. We did not recognize any provision for loan and lease losses during the first quarter of 2012 or 2011 reflecting stabilizing asset quality and minimal change in the size of the Bank’s loan portfolio.

The following table sets forth the allowance for loan and lease losses activity for the first quarter 2012 and 2011:

(\$ in thousands)	March 31, 2012	March 31, 2011		
Balance at beginning of period	\$1,067	\$1,175		
Provision charged to expense	—	—		
Loans charged-off:				
Commercial real estate	—	—		
Commercial and industrial	—	—		
Residential real estate	—	—		
Construction and land development	—	—		
Consumer	(3 )	—		
Total loans charged-off	(3 )	—		
Recoveries on loans previously charged-off:				
Commercial real estate	13	—		
Commercial and industrial	—	—		
Residential real estate	—	—		
Construction and land development	—	—		
Consumer	—	—		
Total recoveries	13	—		
Balance at end of period	\$1,077	\$1,175		
Net charge-offs to average gross loans	—	%	—	%

Credit and loan decisions are made by management and the Board of Directors in conformity with loan policies established by the Board of Directors. Solera National Bank's practice is to charge-off any loan or portion of a loan when the loan is determined by management to be uncollectible due to the borrower's failure to meet repayment terms, the borrower's deteriorating or deteriorated financial condition, the depreciation of the underlying collateral, the loan's classification as a loss, or other reasons.

#### Off-Balance-Sheet Arrangements

In the ordinary course of business, the Company enters into various off-balance-sheet commitments and other arrangements to extend credit that are not reflected in the consolidated balance sheets of the Company. The business purpose of these off-balance-sheet commitments is the routine extension of credit. The total amounts of off-balance-sheet financial instruments with credit risk were \$5.5 million and \$6.3 million as of March 31, 2012 and December 31, 2011, respectively.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Commitments also include revolving lines of credit arrangements and unused commitments for commercial and real estate secured loans. Since many of the commitments are expected to expire without being drawn upon, the commitments do not necessarily represent future cash requirements.

The Company faces the risk of deteriorating credit quality of borrowers to whom a commitment to extend credit has been made; however, no significant credit losses are expected from these commitments and arrangements.





## Borrowings

As of March 31, 2012, the Bank had \$6.5 million in fixed-rate borrowings from the Federal Home Loan Bank of Topeka (FHLB) with varying maturity dates between June 2014 and November 2017 and a weighted-average effective interest rate of 1.90%.

The Bank has also established unsecured Federal Funds lines-of-credit totaling \$9.1 million with various correspondent banks. Additionally, the Bank has access to the Federal Discount window. As of March 31, 2012, the Company had \$410,000 outstanding on these lines.

## Loan Commitments

At March 31, 2012, the Company had \$5.5 million in outstanding loan origination commitments. Management believes Solera National Bank has sufficient funds available to meet current origination and other lending commitments.

## Capital Resources and Capital Adequacy Requirements

The risk-based capital regulations established and administered by the federal banking regulatory agencies are applicable to Solera National Bank. Risk-based capital guidelines are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks, to account for off-balance-sheet exposure, and to minimize disincentives for holding liquid assets. Under the regulations, assets and off-balance-sheet items are assigned to broad risk categories, each with appropriate weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance-sheet items. Under the prompt corrective action regulations, to be adequately capitalized a bank must maintain minimum ratios of total capital to risk-weighted assets of 8.0%, Tier 1 capital to risk-weighted assets of 4.0%, and Tier 1 capital to total average assets of 4.0%. Failure to meet these capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on Solera National Bank's financial statements.

In December 2010, the OCC established minimum capital ratios on the Bank which require Tier 1 capital to average assets of 9.0% and total risk-based capital to risk-weighted assets of 12.0%. As of March 31, 2012, the Bank's ratios are substantially over these revised thresholds. A well-capitalized institution must maintain a minimum ratio of total capital to risk-weighted assets of at least 10.0%, a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, and a minimum ratio of Tier 1 capital to total average assets of at least 5.0% and must not be subject to any written order, agreement, or directive requiring it to meet or maintain a specific capital level.

The following table summarizes the ratios of the Bank and the regulatory minimum capital requirements at March 31, 2012:

(\$ in thousands)	Risk-based		Leverage	
	Tier 1	Total capital	Tier 1	
Actual regulatory capital	\$ 16,197	\$ 17,268	\$ 16,197	
Well-capitalized requirement	5,140	8,566	7,233	
Excess regulatory capital	\$ 11,057	\$ 8,702	\$ 8,964	
Capital ratios	18.9	% 20.2	% 11.2	%
Minimum capital requirement	4.0	% 8.0	% 4.0	%
Individual minimum capital requirement <sup>1</sup>	NA	12.0	% 9.0	%
Well-capitalized requirement	6.0	% 10.0	% 5.0	%

1 In December 2010, the OCC established these minimum capital ratios for the Bank.

#### Liquidity

The primary source of liquidity for the Company is dividends paid by Solera National Bank. However, Solera National Bank is currently restricted from paying dividends until we have received prior written determination of no supervisory objection from the Assistant Deputy Comptroller of the Western Division of the OCC.

Solera National Bank's liquidity is monitored by its staff, the Asset Liability Committee and the Board of Directors, who review historical funding requirements, the current liquidity position, sources and stability of funding, marketability of assets, options for attracting additional funds, and anticipated future funding needs, including the level of unfunded commitments.

Solera National Bank's primary sources of funds are retail and commercial deposits, loan and securities repayments, other short-term borrowings, and other funds provided by operations. While scheduled loan repayments and maturing investments are relatively predictable, deposit flows and early loan prepayments are more influenced by interest rates, general economic conditions, and competition. Solera National Bank will maintain investments in liquid assets based upon management's assessment of (1) the need for funds, (2) expected deposit flows, (3) yields available on short-term liquid assets, and (4) objectives of the asset/liability management program.

Additionally, the Company is a member of the Certificate of Deposit Account Registry Service ("CDARS®") program. Through CDARS®, the Bank's customers can increase their FDIC insurance by up to \$50 million through reciprocal deposit accounts. This is accomplished by the Bank entering into reciprocal depository relationships with other member banks. The individual customer's large deposit is broken into amounts below the \$250,000 FDIC-insured amount and placed with other banks that are members of the network. The reciprocal member bank issues deposits in amounts that ensure the entire deposit is eligible for FDIC insurance. These sources provide secondary liquidity to the Company to service its depositors' needs. As of March 31, 2012 and December 31, 2011, the Bank had \$10.2 million and \$11.8 million, respectively, in CDARS® deposits.

As loan demand increases, greater pressure will be exerted on Solera National Bank's liquidity. Solera National Bank does not intend to aggressively pursue lending opportunities if sufficient funding sources (e.g., deposits, Federal Funds, etc.) are not available. As of March 31, 2012, the loan to deposit ratio was only 46%, a slight decrease from 47% at December 31, 2011.

The Bank is a member of the FHLB of Topeka, which gives the Bank access to a secured line of credit with approximately \$52.0 million of available funding as of March 31, 2012, subject to the availability of sufficient collateral to pledge against such borrowings. Additionally, the Bank has approved, unsecured federal funds purchase lines totaling \$9.1 million with three correspondent banks. These lines either expire during 2012, or can be terminated at any time; however, it is not anticipated that these lines will be terminated and the Bank expects to be approved for new lines once the existing lines expire. The Bank also has the ability to borrow at the Federal Reserve Discount Window on a secured basis.

The Company had cash and cash equivalents of \$729,000, or 0.5% of total assets, at March 31, 2012. Additionally, the Company had \$84.5 million in available-for-sale investment securities, or 58% of total assets, at March 31, 2012. Management believes Solera National Bank will have adequate liquidity to meet anticipated future funding needs.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a smaller reporting company, the Company is not required to provide the information required by this Item.

### ITEM 4. CONTROLS AND PROCEDURES

#### Disclosure Controls and Procedures

Management is responsible for maintaining effective disclosure controls and procedures. As of the end of the period covered by this Quarterly Report on Form 10-Q, management evaluated the effectiveness and operation of the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)). Based on that evaluation, both the Company's Principal Executive Officer and Principal Accounting and Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective to ensure that the information required to be disclosed by the Company in reports that are filed or submitted under the Exchange Act are recorded, processed, summarized and reported to management within the time periods specified in the Securities and Exchange

Commission's rules and forms and that such information is accumulated and communicated to management as appropriate to allow timely decisions regarding disclosure.

#### Changes in Internal Control over Financial Reporting

There have been no changes in internal controls over financial reporting during the Company's last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Not applicable.

ITEM 1A. RISK FACTORS

As a smaller reporting company, the Company is not required to provide the information required by this Item.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURE

Not applicable.

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS

Please see the exhibit index following the signature page of this Report.

SOLERA NATIONAL BANCORP, INC.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SOLERA NATIONAL BANCORP, INC.  
(Registrant)

Dated: May 14, 2012

/s/ Douglas Crichfield  
Douglas Crichfield  
President and Chief Executive Officer  
(Principal Executive Officer)

Dated: May 14, 2012

/s/ Robert J. Fenton  
Robert J. Fenton  
Executive Vice President, Chief Financial  
Officer  
(Principal Accounting and Financial  
Officer)

## EXHIBIT INDEX

Exhibit Number	Description of Exhibit
<u>31.1</u> *	Certification pursuant to Rule 13a-14(a) of the Securities Exchange Act.
<u>31.2</u> *	Certification pursuant to Rule 13a-14(a) of the Securities Exchange Act.
<u>32.1</u> *	Certification pursuant to Rule 13a-14(b) of the Securities Exchange Act and 18 U.S.C. §1350.
101.INS**	XBRL Instance Document
101.SCH**	XBRL Taxonomy Extension Schema Document
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase
101.LAB**	XBRL Taxonomy Extension Label Linkbase
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase
101.DEF**	XBRL Taxonomy Extension Definition Linkbase document
(*)	Filed herewith.
(**)	Pursuant to applicable securities laws and regulations, we are deemed to have complied with the reporting obligation relating to the submission of interactive data files in such exhibits and are not subject to liability under any anti-fraud provisions of the federal securities laws as long as we have made a good faith attempt to comply with the submission requirements and promptly amend the interactive data files after becoming aware that the interactive data files fail to comply with the submission requirements. In accordance with Rule 406T of Regulation S-T, the information in these exhibits is furnished and deemed not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, except as expressly set forth by specific reference in such filing.