PINNACLE FINANCIAL PARTNERS INC
Form 10-K
February 19, 2009

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)**
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2008
OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d)**
OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________ to __________
Commission File Number: 000-31225

(Exact name of registrant as specified in charter)

Tennessee	62-1812853
(State or other jurisdiction of incorporation)	(I.R.S. Employer Identification No.)
211 Commerce Street, Suite 300, Nashville, Tennessee	37201
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: (615) 744-3700
Securities registered pursuant to Section 12 (b) of the Act:

Title of Each Class	Name of Exchange on which Registered
Common Stock, par value $1.00	Nasdaq Global Select Market

Securities registered to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No þ
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ
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 þ No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (Section 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this

Form 10-K. o

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

Large accelerated filer o	Accelerated filer þ	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity as of the last business day of the registrant s most recently completed second fiscal quarter: $421,537,320 as of June 30, 2008.

APPLICABLE ONLY TO CORPORATE REGISTRANTS

Indicate the number of shares outstanding of each of the registrant s classes of common stock, as of the latest practicable date: 23,996,927 shares of common stock as of January 31, 2009.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Shareholders, scheduled to be held April 21, 2009, are incorporated by reference into Part III of this Form 10-K.

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FORWARD-LOOKING STATEMENTS

Pinnacle Financial Partners, Inc. (Pinnacle Financial) may from time to time make written or oral statements, including statements contained in this report which may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The words expect, anticipate, intend, plan, believe, seek, estimate and similar expressions are in identify such forward-looking statements, but other statements not based on historical information may also be considered forward-looking. All forward-looking statements are subject to risks, uncertainties and other facts that may cause the actual results, performance or achievements of Pinnacle Financial to differ materially from any results expressed or implied by such forward-looking statements. Such factors include, without limitation, (i) deterioration in the financial condition of borrowers resulting in significant increases in loan losses and provisions for those losses, (ii) continuation of the historically low short-term interest rate environment, (iii) the inability of Pinnacle Financial to continue to grow its loan portfolio at historic rates in the Nashville-Davidson-Murfreesboro-Franklin MSA and the Knoxville MSA, (iv) increased competition with other financial institutions, (v) deterioration or lack of sustained growth in the national or local economies including the Nashville-Davidson-Murfreesboro-Franklin MSA and the Knoxville MSA, (vi) rapid fluctuations or unanticipated changes in interest rates, (vii) the development of any new market other than Nashville or Knoxville, (viii) a merger or acquisition, (ix) any activity in the capital markets that would cause Pinnacle Financial to conclude that there was impairment of any asset including intangible assets and (x) changes in state and Federal legislation, regulations or policies applicable to Banks and other financial services providers, including regulatory or legislative developments arising out of current unsettled conditions in the economy. Many of such factors are beyond Pinnacle Financial s ability to control or predict, and readers are cautioned not to put undue reliance on such forward-looking statements. Pinnacle Financial disclaims any obligation to update or revise any forward-looking statements contained in this release, whether as a result of new information, future events or otherwise.

PART I

Unless this Form 10-K indicates otherwise or the context otherwise requires, the terms we, our, us, Pinnacle Financial Partners or Pinnacle Financial as used herein refer to Pinnacle Financial Partners, Inc., which we sometimes refer to as Pinnacle National, our bank subsidiary or our bank and its other subsidiaries. References herein to the fiscal years 2004, 2005, 2006, 2007 and 2008 mean our fiscal years ended December 31, 2004, 2005, 2006, 2007 and 2008, respectively.

ITEM 1. BUSINESS

OVERVIEW

Pinnacle Financial Partners is Tennessee s second-largest bank holding company, with $4.8 billion in assets as of December, 31, 2008. Incorporated on February 28, 2000, the holding company is the parent company of Pinnacle National and owns 100% of the capital stock of Pinnacle National. The firm started operations on October 27, 2000, with one office in Nashville, Tenn., and has since grown to 33 offices, including 31 in eight rapidly growing Middle Tennessee counties. The firm also has two offices in Knoxville, Tenn., the state s third-largest banking market, and plans to expand to a total of five offices in Knoxville by the end of 2010.

The firm operates as a community bank primarily in urban markets. As an urban community bank, Pinnacle provides the personalized service most often associated with small community banks, while offering the sophisticated products and services, such as investments and treasury management, more typically offered by large regional and national banks. This approach has enabled Pinnacle Financial to move clients from the three vulnerable regional and national banks that, despite significant market share losses over the last eight years, still possess more than 45% market share in the Nashville MSA. As a result, in less than ten years, Pinnacle has grown to the fourth largest market share in this desirable market.

Withstanding Market Turbulence

Despite the turbulence in financial markets and the financial services industry, Pinnacle s credit quality measures continue to outperform those of its primary competitors in the Nashville MSA. Pinnacle attributes this historical performance to sound credit policy, as well as its approach of hiring the best financial services professionals in the market. Hiring only experienced lenders with large client followings has enabled Pinnacle to further its growth without experiencing significant credit quality related losses like many other financial institutions of similar size or that operate in Pinnacle s market areas.

Pinnacle also believes that its markets are in good position to weather the national economic downturn. While the local Nashville and Knoxville economies are not as robust as in previous periods, as residential real estate construction and development continues to soften in both the Nashville and Knoxville MSAs, we believe these markets will perform well in comparison to other United States markets of similar size.

Growth through Acquisition and Successful Integration

In 2007, Pinnacle acquired Mid-America Bancshares Inc. (Mid-America), a $1.12 billion, two-bank holding company with 14 offices in rapidly growing counties within the Nashville MSA that complemented Pinnacle s existing footprint. Mid-America was the parent of PrimeTrust Bank and Bank of the South, both of which had a growth rate in the top 10 in the country for banks chartered in 2001. The acquisition closed on November 30, 2007, and Pinnacle integrated operations of PrimeTrust and Bank of the South into Pinnacle National on February 29, 2008. We believe we successfully integrated PrimeTrust and Bank of the South as a result of:

1. Achievement of all major integration milestones on time,

2. Achievement of the financial synergies that were proposed at the time the Mid-America transaction was announced,

3. No degradation in service quality as measured by internal client surveys, and

4. Continued loan growth for the combined firm at rates exceeding those of the previous period.

This experience with the Mid-America merger mirrors the successful integration in 2006 of Cavalry Bancorp, Inc. (Cavalry). Cavalry was a one-bank holding company headquartered in Rutherford County, one of the fastest growing counties in Tennessee at the time of the acquisition. In that acquisition, we met synergy targets and achieved all major milestones while significantly increasing market share. Furthermore, we do not believe we have lost, or will lose, any significant revenue producers or clients as a result of the Mid-America integration.

On July 2, 2008, we announced the merger of Murfreesboro, Tenn. based Beach & Gentry Insurance LLC (Beach & Gentry). Beach & Gentry merged with Miller & Loughry Insurance Services Inc. The combined company took the name Miller Loughry Beach Insurance Services, Inc. and has consolidated offices in Pinnacle Financial s offices in Murfreesboro.

Opportunity. We believe there are major trends in the Nashville and Knoxville MSA s that strengthen our strategic market position as a locally-managed community bank:

Clients generally perceive that service levels at large banks are declining. We believe this is largely attributable to cost savings initiatives and/or merger-related integration issues resulting from consolidation in the bank and brokerage industries. Additionally, business owners want a reliable point of contact that is knowledgeable about their business and the financial products and services that are important to the success of their business. Nashville is dominated by three large regional bank holding companies that are headquartered elsewhere, each of whom is experiencing declining market share trends in the Nashville market over the last eight years; and

There is significant growth in the demand for convenient access to financial services, particularly through ATMs, telephone banking, remote deposit capture and Internet banking. We have developed best-in-class products and services in these areas, including free ATM usage and a comprehensive Internet banking suite of products.

Our primary market segments, which are small businesses with annual sales from $1 million to $50 million, real estate professionals and consumers that are not price-based shoppers, are more likely to be disaffected by the banking industry s perceived decline in customer service and lack of financial product sophistication. To overcome these client perceptions and attract business from these market segments, our approach is to hire only seasoned professionals, from both the banking and brokerage industries, and strategically design our banking, investment and insurance products to meet the expected needs of our targeted market segments. As an example, we consider our consumer brokerage and corporate treasury management products to be at least at parity with the large regional banks that dominate our target segment in the Nashville and Knoxville markets. Our advantage is that we have both the sophisticated product offering and the exceptional service level provided by local financial advisors working hand-in-hand with the client on an ongoing basis. Accordingly, our marketing philosophy is centered on delivering exceptional service and effective financial advice through highly trained personnel who understand and care about the broad financial needs and objectives of our clients.

Business Strategies. To carry out our marketing philosophy, our specific business strategies have been and will continue to be:

Hire and retain highly experienced and qualified banking and financial professionals with successful

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track records and, for client contact personnel, established books of business with small businesses, real estate professionals and affluent households within the Nashville and Knoxville MSAs. On average, our senior client contact associates have in excess of 20 years experience in their local market. We have also achieved an annual associate retention rate of approximately 90 percent. We believe we will continue to experience success in attracting more market-best associates to our firm as well as retaining our highly experienced and successful group of associates. Our compensation has traditionally included cash incentives and equity based awards to all associates to facilitate this employment philosophy and our compensation expense has traditionally been higher than our peers as a result.

Provide individualized attention with consistent, local decision-making authority and capitalize on customer dissatisfaction that we believe exists and has been caused by what we believe to be our competitors less than satisfactory response to the financial needs of today s sophisticated consumers and small- to medium-sized businesses. Since we began our company, we have historically surveyed our customers on numerous matters related to their relationship with us. Better than 97 percent of these surveys indicate that Pinnacle is recognizably better than our competitors.

Offer a full line of financial services to include traditional depository and credit products, as well as sophisticated investment, trust and insurance products and services. Brokerage products are offered through dual employees licensed by Raymond James Financial Services. As of December 31, 2008, Pinnacle National s brokerage division, Pinnacle Asset Management, had accumulated approximately $686 million in brokerage assets and in 2008 and 2007, was the top producer among Raymond James Financial Services branches nationwide. Additionally, our trust department had accumulated approximately $588 million in trust assets under management at December 31, 2008. We use our trust department, Pinnacle Asset Management and our insurance agency subsidiary, Miller Loughry and Beach Insurance Services, Inc., to provide a broad array of sophisticated and convenient investment and insurance products and services.

Offer extraordinary convenience by building a distribution system with online banking, telephone banking, remote deposit services and global access to ATMs to provide options for clients to access financial services 24/7.

We believe our business strategies allow us to effectively distinguish ourselves from other financial institutions operating within the Nashville and Knoxville MSAs and successfully attract and retain business relationships with small businesses and affluent households.

Market Area. Our markets of Nashville and Knoxville are two of the top three banking market areas in Tennessee.

Nashville MSA

The Nashville MSA, Pinnacle s primary market area, includes Davidson County and twelve surrounding counties. This area represents a geographic area that covers approximately 4,000 square miles and a population in excess of 1.5 million people. For Pinnacle, we concentrate our market efforts on Davidson, Rutherford, Williamson, Sumner, Wilson, Cheatham, Dickson and Bedford counties which represent 90% of the Nashville MSA s population base and 93.6% of the deposit base (based on June 30, 2008 FDIC information).

Nashville is the capitol of Tennessee and an important transportation, business and tourism center within the United States. Additionally, the metropolitan Nashville area has attracted a number of significant business relocations resulting in an expansion of its labor force into many different industry sectors. Nashville is frequently recognized as one of America s top cities.

§ In 2008, *Forbes* magazine ranked Nashville among the Best Places for Business and Careers based on job and income growth, as well as migration trends.

§ In December 2008, Marketwatch.com ranked Nashville No. 8 nationally in its Top 10 Cities for Business ranking because of Nashville s robust industry sectors.

- § In 2008, Nashville ranked among the top 100 places in live in America based on education, employment, economy, crime, parks, recreation and housing.
- § In its Best Cities for Relocating Families ranking, *Primacy* ranked Nashville No. 20 nationally among large market cities based on factors such as home prices, appreciation rates and property taxes.

- § In November 2008, *Site Selection*, an Atlanta-based magazine that annually ranks states attractiveness to investors, placed Tennessee in second place as to investor attractiveness.

Over the last few years, the Nashville area has been chosen by such companies as Louisiana Pacific, Nissan North America, CareMark and Dell to relocate their U.S. headquarters or to significantly expand their operations.

Our primary service area s economic strength comes from its large employer base, which includes several large enterprises such as Vanderbilt University and Medical Center, HCA Inc., Saturn Corporation and Nissan Motor Manufacturing Corporation USA. Also, there are currently more than 300 healthcare companies in the Nashville area. We anticipate that Nashville will continue to attract businesses due to the relatively low cost of doing business here and the presence of a well-trained labor force, which in turn, should increase the demand for depository and lending services within our market at a pace faster than national averages. In comparing Nashville MSA deposits as of June 30, 2007 to those at June 30, 2008, the Nashville MSA deposits were $972 million higher in 2008 than in 2007, which reflects a 3.2% growth rate.

Knoxville MSA

The Knoxville MSA, where Pinnacle established its de novo presence in 2007, includes five counties with a total population of 682,000 in 2007. According to a Labor Market Assessment of the Greater Knoxville Region conducted for the Knoxville Area Chamber Partnership in 2006, the area s population is growing faster than the state or national growth rates. The study indicates the population is projected to increase by 5.8%, compared to 4.3% for Tennessee and 4.8% nationally, between 2006 and 2011. In 2008, *Primacy* ranked Knoxville No. 4 among middle market cities based on factors such as home prices, appreciation rates and property taxes.

The business climate in the Knoxville MSA has earned the area a reputation for being a good choice for relocation. For instance, *Expansion Management* magazine named the Knoxville metropolitan area 3rd among all mid-sized cities in the nation in its annual Best Metro for Business and Expansion 2007 competition, and in 2008 *Forbes* ranked Knoxville No. 10 in its ranking of Best Places for Business and Careers.

Among the leading companies that have relocated significant operations to the Knoxville area are Brinks Home Security, SYSCO Corporation, Reily Foods and Exedy America. The area was already home to corporate headquarters such as Panasonic Electronic Devices, Regal Corp., Scripps Networks, Sea Ray Boats, Pilot Oil, Ruby Tuesday and the Tennessee Valley Authority.

The region is also home to the University of Tennessee flagship campus and Oak Ridge National Laboratory and Y-12 National Security Complex. These institutions should help to continue to spur growth in the Knoxville MSA.

Competitive Conditions. The Nashville MSA banking market is very competitive, with 59 financial institutions with over $31.4 billion in deposits in the market as of June 30, 2008, up from approximately $30.6 billion at June 30, 2007 according to FDIC data. As of June 30, 2008, approximately 65.2% of this deposit base was controlled by large, multi-state banks headquartered outside of Nashville, which included the following six banks, Regions Financial (headquartered in Birmingham, Alabama), Bank of America (headquartered in Charlotte, North Carolina), First Horizon (headquartered in Memphis, Tennessee), US Bancorp (headquartered in Milwaukee, Wisconsin), SunTrust (headquartered in Atlanta, Georgia), and Fifth Third (headquartered in Cincinnati, Ohio). According to FDIC deposit information, the collective market share of deposits in the Nashville MSA of Regions Financial (including the acquired Union Planters National Bank, First American National Bank, and AmSouth Bank), Bank of America and SunTrust (including the acquired National Bank of Commerce) declined from 67.3% to 45.5% since June 30, 1997. Pinnacle, on the other hand, after only eight years of operations, now holds the No. 4 market share position in the Nashville MSA immediately behind the three vulnerable out-of-state banks.

The Knoxville MSA banking market is also very competitive, with 43 financial institutions with over $11.1 billion in deposits in the market as of June 30, 2008. According to FDIC data, bank and thrift deposits in the Knoxville MSA grew from approximately $10.1 billion at June 30, 1996 to more than $11.1 billion at June 30, 2008. As of June 30, 2008, approximately 66.8% of this deposit base was controlled by large, multi-state banks headquartered outside of Knoxville, which included the following four banks, Regions Financial (headquartered in Birmingham, Alabama), First Horizon (headquartered in Memphis, Tennessee), Branch Banking and Trust (headquartered in Winston-Salem, North Carolina), and SunTrust (headquartered in Atlanta, Georgia). According to FDIC deposit information, the collective market share of deposits in the Knoxville MSA of Regions Financial (including the acquired Union Planters

National Bank, First American National Bank, and AmSouth Bank), First Horizon and SunTrust (including the acquired National Bank of Commerce) declined from 66.3% to 54.6% since June 30, 1997.

Consequently, while large, multi-state institutions are well established in both of our market areas, the general trends indicate that a majority of the community banks in our market areas have been able to increase their deposit market share in recent years at the expense of the larger, multi-state banks. Furthermore, continued consolidation of our industry, particularly with respect to the larger regional banks that have presence in our market, should create additional opportunities for us as we capitalize on customer dissatisfaction that usually occurs following a merger of these larger multi-state banks.

The Nashville MSA has also experienced several new denovo banks over the last few years. These new banks will increase the competitiveness of our local market as they work to build market share within Nashville and the surrounding counties. This competition may limit or reduce our profitability, reduce our growth and adversely affect our results of operations and financial condition. We expect that these new banks will approach our customers about moving their banking relationships as well as approach our associates about joining their organizations. However, we do not anticipate losing any customers or associates to these organizations as we will continue to focus on providing high quality customer service and maintaining a high level of engagement with our associate base.

We believe that the most important criteria to our bank s targeted clients when selecting a bank is their desire to receive exceptional and personal customer service while being able to enjoy convenient access to a broad array of sophisticated financial products. Additionally, when presented with a choice, we believe that many of our bank s targeted clients would prefer to deal with a locally-owned institution headquartered in Tennessee, like Pinnacle National, as opposed to a large, multi-state bank, where many important decisions regarding a client s financial affairs are made elsewhere.

Employees

As of Feb. 13, 2009, we employed 729 associates, including 700 full-time associates. We believe these associates are Pinnacle s most important asset and are the reason the firm continues to outpace growth rates of similar institutions. We consider our relationship with all associates to be excellent. This is supported by the fact that for the sixth consecutive year, Pinnacle was named by the Nashville Business Journal as the Best Place to Work in Nashville among Middle Tennessee s large companies with more than 100 employees. The selection is based on a survey of associates.

We are also one of a relatively small number of financial firms in the country that provide equity-based compensation for all associates via a broad-based equity incentive plan. We believe this broad-based equity incentive plan directly aligns our employee base with our shareholders, and that our associates have become even more engaged in the creation of shareholder value over the intermediate- and long-terms. Information concerning these plans is included in the Notes to the Consolidated Financial Statements.

Additionally, all of our non-commission based employees participate in the same annual cash incentive plan as our senior officers whereby they receive a certain percentage of their annual base salary should the firm meet certain soundness and earnings targets for the year. Information concerning this plan is included in Management s Discussion and Analysis of Financial Condition and Results of Operations.

Lending Services

We offer a full range of lending products, including commercial, real estate and consumer loans to individuals and small-to medium-sized businesses and professional entities. We compete for these loans with competitors who are also well established in the Nashville and Knoxville MSAs.

Pinnacle National s loan approval policies provide for various levels of officer lending authority. When the amount of total loans to a single borrower exceeds that individual officer s lending authority, officers with a higher lending limit, Pinnacle National s board of directors or the executive committee of the board determine whether to approve the loan request.

Pinnacle National s lending activities are subject to a variety of lending limits imposed by federal law. Differing limits apply based on the type of loan or the nature of the borrower, including the borrower s relationship to Pinnacle National. In general, however, at December 31, 2008, we were able to loan any one borrower a maximum amount equal to approximately $63.7 million plus an additional $42.5 million, or a total of approximately $106.2 million, for loans that meet certain additional federal collateral guidelines. These legal limits will increase or decrease as our bank subsidiary s capital increases or decreases as a result of its earnings or losses, the injection of additional capital or other reasons. In addition to these regulatory limits, Pinnacle National currently imposes upon itself an internal lending limit of $22 million, which is less than the prescribed legal lending limit.

The principal economic risk associated with each category of loans that Pinnacle National expects to make is the creditworthiness of the borrower. General economic factors affecting a commercial or consumer borrower s ability to repay include interest, inflation and unemployment rates, as well as other factors affecting a borrower s assets, clients, suppliers and employees. Many of Pinnacle National s commercial loans are made to small- to medium-sized businesses that are sometimes less able to withstand competitive, economic and financial pressures than larger borrowers. We also have a meaningful investment in residential construction and land acquisition and development loans. The weakness in the economy has impacted this industry significantly. During periods of economic weakness, like those currently being experienced, these businesses may be more adversely affected than larger enterprises, and may cause increased levels of nonaccrual or other problem loans, loan charge-offs and higher provision for loan losses.

Pinnacle National s commercial clients borrow for a variety of purposes. The terms of these loans will vary by purpose and by type of any underlying collateral and include equipment loans and working capital loans. Commercial loans may be unsecured or secured by accounts receivable or by other business assets. Pinnacle National also makes a variety of commercial real estate loans, residential real estate loans and construction and development loans. Pinnacle National also makes a variety of loans to individuals for personal, family, investment and household purposes, including secured and unsecured installment and term loans, residential first mortgage loans, home equity loans and home equity lines of credit. We do not have any concentrations of subprime loans.

Investment Securities

In addition to loans, Pinnacle National has investments primarily in obligations of the United States government, obligations guaranteed as to principal and interest by the United States government and other securities. No investment in any of those instruments exceeds any applicable limitation imposed by law or regulation. The executive committee of the board of directors reviews the investment portfolio on an ongoing basis in order to ensure that the investments conform to Pinnacle National s asset liability management policy as set by the board of directors.

Asset and Liability Management

Our Asset Liability Management Committee (ALCO), composed of senior managers of Pinnacle National, manages Pinnacle National s assets and liabilities and strives to provide a stable, optimized net interest income and margin, adequate liquidity and ultimately a suitable after-tax return on assets and return on equity. ALCO conducts these management functions within the framework of written policies that Pinnacle National s board of directors has adopted. ALCO works to maintain an acceptable position between rate sensitive assets and rate sensitive liabilities. The executive committee of the board of directors oversees the ALCO function on an ongoing basis.

Deposit Services

Pinnacle National seeks to establish a broad base of core deposits, including savings, checking, interest-bearing checking, money market and certificate of deposit accounts. To attract deposits, Pinnacle National has employed a marketing plan in its overall service area based on relationship banking and features a broad product line and competitive rates and services. The primary sources of deposits are residents and businesses located in the Nashville and Knoxville MSAs. Pinnacle National generally obtains these deposits through personal solicitation by its officers and directors and generally does not employ general media advertising for deposit generation. We also utilize non-core deposits as a significant funding source for our growth. These non-core deposit sources primarily include brokered certificates of deposits and public funds.

Investment, Trust and Insurance Services

Pinnacle National contracts with Raymond James Financial Service, Inc. (RJFS), a registered broker-dealer and investment adviser, to offer and sell various securities and other financial products to the public from Pinnacle National s locations through Pinnacle National employees that are also RJFS employees. RJFS is a subsidiary of Raymond James Financial, Inc.

Pinnacle National offers, through RJFS, non-FDIC insured investment products in order to assist Pinnacle National s clients in achieving their financial objectives consistent with their risk tolerances. Pinnacle National s suite of investment products include:

Mutual Funds;	Fixed Annuities;
Variable Annuities;	Stocks;
Money Market Instruments;	Financial Planning;
Treasury Securities;	Asset Management Accounts; and
Bonds;	Listed Options.

All of the financial products listed above are offered by RJFS from Pinnacle National s main office and its other offices. Additionally, we believe that the brokerage and investment advisory program offered by RJFS complements Pinnacle National s general banking business, and further supports its business philosophy and strategy of delivering to our clients those products and services that meet their financial needs. In addition to the compliance monitoring provided by RJFS, Pinnacle National has developed its own compliance-monitoring program to further ensure that Pinnacle National personnel deliver these products in a manner consistent with the various regulations governing such activities.

Pinnacle National receives a percentage of commission credits and fees generated by the program. Pinnacle National remains responsible for various expenses associated with the program, including promotional expenses, furnishings and equipment expenses and general personnel costs.

Pinnacle National also maintains a trust department which provides fiduciary and investment management services for individual and commercial clients. Account types include personal trust, endowments, foundations, individual retirement accounts, pensions and custody. Pinnacle Financial has also established Pinnacle Advisory Services, Inc., a registered investment advisor, to provide investment advisory services to its clients. Additionally, Miller Loughry Beach Insurance Services, Inc., a wholly-owned subsidiary of Pinnacle National provides insurance products, particularly in the property and casualty area, to its clients.

Other Banking Services

Given client demand for increased convenience in accessing banking and investment services, Pinnacle National also offers a broad array of convenience-centered products and services, including 24 hour telephone and Internet banking, debit cards, direct deposit and cash management services for small- to medium-sized businesses. Additionally, Pinnacle National is associated with a nationwide network of automated teller machines of other financial institutions that our clients are able to use throughout Tennessee and other regions. In many cases, Pinnacle National, in contrast to its regional competitors, reimburses its clients for any fees that may be charged to the client for utilizing the nationwide ATM network, providing greater convenience as compared to these competitors.

Pinnacle National also offers its targeted commercial clients remote deposit services, which allow electronic deposits to be made from the client s place of business.

Available Information

We file reports with the Securities and Exchange Commission (SEC), including annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K. The public may read and copy any materials we file with the SEC at the SEC s Public Reference Room at 100 F Street, N.E., Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. We are an electronic filer, and the SEC maintains an Internet site at *www.sec.gov* that contains the reports, proxy and information statements, and other information we have filed electronically. Our website address is *www.pnfp.com*. Please note that our website address is provided as an inactive textual reference only. We make available free of charge through our website, the annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. The information provided on our website is not part of this report, and is therefore not incorporated by reference unless such information is otherwise specifically referenced elsewhere in this report.

We have posted our Corporate Governance Guidelines, our Corporate Code of Conduct for directors, officers and employees, and the charters of our Audit Committee, Human Resources and Compensation Committee, and

Nominating and Corporate Governance Committee of our board of directors on the Corporate Governance section of our website at *www.pnfp.com*. Our corporate governance materials are available free of charge upon request to our Corporate Secretary, Pinnacle Financial Partners, Inc., 211 Commerce Street, Suite 300, Nashville, Tennessee 37201.

SUPERVISION AND REGULATION

Both Pinnacle Financial and Pinnacle National are subject to extensive state and federal banking laws and regulations that impose restrictions on and provide for general regulatory oversight of Pinnacle Financial s and Pinnacle National s operations. These laws and regulations are generally intended to protect depositors and borrowers, not shareholders. The following discussion describes the material elements of the regulatory framework which currently apply. However, Congress and the executive branch are likely to consider significant new regulatory reform initiatives in the near future, which could result in material changes to the current oversight structure.

Pinnacle Financial

We are a bank holding company under the federal Bank Holding Company Act of 1956. As a result, we are subject to the supervision, examination, and reporting requirements of the Bank Holding Company Act and the regulations of the Federal Reserve.

Acquisition of Banks. The Bank Holding Company Act requires every bank holding company to obtain the Federal Reserve s prior approval before:

- Acquiring direct or indirect ownership or control of any voting shares of any bank if, after the acquisition, the bank holding company will directly or indirectly own or control more than 5% of the bank s voting shares;
- Acquiring all or substantially all of the assets of any bank; or
- Merging or consolidating with any other bank holding company.

Additionally, the Bank Holding Company Act provides that the Federal Reserve may not approve any of these transactions if it would substantially lessen competition or otherwise function as a restraint of trade, or result in or tend to create a monopoly, unless the anticompetitive effects of the proposed transaction are clearly outweighed by the public interest in meeting the convenience and needs of the communities to be served. The Federal Reserve is also required to consider the financial and managerial resources and future prospects of the bank holding companies and banks concerned and the convenience and needs of the communities to be served. The Federal Reserve s consideration of financial resources generally focuses on capital adequacy, which is discussed below.

Under the Bank Holding Company Act, if adequately capitalized and adequately managed, we or any other bank holding company located in Tennessee may purchase a bank located outside of Tennessee. Conversely, an adequately capitalized and adequately managed bank holding company located outside of Tennessee may purchase a bank located inside Tennessee. In each case, however, state law restrictions may be placed on the acquisition of a bank that has only been in existence for a limited amount of time or will result in specified concentrations of deposits. For example, Tennessee law currently prohibits a bank holding company from acquiring control of a Tennessee-based financial institution until the target financial institution has been in operation for three years.

Change in Bank Control. Subject to various exceptions, the Bank Holding Company Act and the Federal Change in Bank Control Act, together with related regulations, require Federal Reserve approval prior to any person or company acquiring control of a bank holding company. Control is conclusively presumed to exist if an individual or company acquires 25% or more of any class of voting securities of the bank holding company. Control is rebuttably presumed to exist if a person or company acquires 10% or more, but less than 25%, of any class of voting securities and either:

- The bank holding company has registered securities under Section 12 of the Securities Exchange Act of 1934; or
- No other person owns a greater percentage of that class of voting securities immediately after the transaction.

Our common stock is registered under the Securities Exchange Act of 1934. The regulations provide a procedure for challenge of the rebuttable control presumption.

Permitted Activities. The Gramm-Leach-Bliley Act of 1999 amended the Bank Holding Company Act and expanded the activities in which bank holding companies and affiliates of banks are permitted to engage. The Gramm-Leach-Bliley Act eliminates many federal and state law barriers to affiliations among banks and securities firms, insurance companies, and other financial service providers. Generally, if we qualify and elect to become a financial holding company, which is described below, we may engage in activities that are:

- Financial in nature;
- Incidental to a financial activity; or
- Complementary to a financial activity and do not pose a substantial risk to the safety or soundness of depository institutions or the financial system generally.

The Gramm-Leach-Bliley Act expressly lists the following activities as financial in nature:

- Lending, trust and other banking activities;
- Insuring, guaranteeing, or indemnifying against loss or harm, or providing and issuing annuities, and acting as principal, agent, or broker for these purposes, in any state;
- Providing financial, investment, or advisory services;
- Issuing or selling instruments representing interests in pools of assets permissible for a bank to hold directly;
- Underwriting, dealing in or making a market in securities;
- Activities that the Federal Reserve has determined to be so closely related to banking or managing or controlling banks as to be a proper incident to banking or managing or controlling banks;
- Activities permitted outside of the United States that the Federal Reserve has determined to be usual in connection with banking or other financial operations abroad;
- Merchant banking through securities or insurance affiliates; and
- Insurance company portfolio investments.

The Gramm-Leach-Bliley Act also authorizes the Federal Reserve, in consultation with the Secretary of the Treasury, to determine activities in addition to those listed above that are financial in nature or incidental to such financial activity. In determining whether a particular activity is financial in nature or incidental or complementary to a financial activity, the Federal Reserve must consider (1) the purpose of the Bank Holding Company and Gramm-Leach-Bliley Acts, (2) changes or reasonably expected changes in the marketplace in which financial holding companies compete and in the technology for delivering financial services, and (3) whether the activity is necessary or appropriate to allow financial holding companies to effectively compete with other financial service providers and to efficiently deliver information and services.

To qualify to become a financial holding company, any of our depository institution subsidiaries must be well capitalized and well managed and must have a Community Reinvestment Act rating of at least satisfactory. Additionally, we must file an election with the Federal Reserve to become a financial holding company and provide the Federal Reserve with 30 days written notice prior to engaging in a permitted financial activity. Although we do not have any immediate plans to file an election with the Federal Reserve to become a financial holding company, one of the primary reasons we selected the holding company structure was to have increased flexibility. Accordingly, if deemed appropriate in the future, we may seek to become a financial holding company.

Under the Bank Holding Company Act, a bank holding company, which has not qualified or elected to become a financial holding company, is generally prohibited from engaging in or acquiring direct or indirect control of more than 5% of the voting shares of any company engaged in nonbanking activities unless, prior to the enactment of the Gramm-Leach-Bliley Act, the Federal Reserve found those activities to be so closely related to banking as to be a proper incident to the business of banking. Activities that the Federal Reserve has found to be so closely related to banking as to be a proper incident to the business of banking include:

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Factoring accounts receivable;

Acquiring or servicing loans;

Leasing personal property;

Conducting discount securities brokerage activities;

Performing selected data processing services;

Acting as agent or broker in selling credit life insurance and other types of insurance in connection with credit transactions; and

Performing selected insurance underwriting activities.

Despite prior approval, the Federal Reserve may order a bank holding company or its subsidiaries to terminate any of these activities or to terminate its ownership or control of any subsidiary when it has reasonable cause to believe that the bank holding company s continued ownership, activity or control constitutes a serious risk to the financial safety, soundness, or stability of any of its bank subsidiaries.

Support of Subsidiary Institutions. Under Federal Reserve policy, we are expected to act as a source of financial strength for our bank subsidiary, Pinnacle National, and to commit resources to support Pinnacle National. This support may be required at times when, without this Federal Reserve policy, we might not be inclined to provide it. In the unlikely event of our bankruptcy, any commitment by us to a federal bank regulatory agency to maintain the capital of Pinnacle National would be assumed by the bankruptcy trustee and entitled to a priority of payment.

Participation in the Capital Purchase Program of the Troubled Asset Relief Program. On October 3, 2008, the Emergency Economic Stabilization Act (ESSA) became law. Under the Troubled Asset Relief Program (TARP) authorized by ESSA, the U.S. Department of the Treasury established a capital purchase program (CPP) providing for the purchase of senior preferred shares of qualifying U.S. controlled banks, savings associations and certain bank and savings and loan holding companies. On December 12, 2008, Pinnacle Financial sold 95,000 shares of Series A preferred stock and warrants to acquire 534,910 shares of common stock to the U.S. Treasury pursuant to the CPP for aggregate consideration of $95 million. As a result of Pinnacle Financial s participation in the CPP, Pinnacle Financial has agreed to certain limitations on executive compensation. For as long as the U.S. Treasury owns any debt or equity securities of Pinnacle Financial issued in connection with the TARP capital purchase program, Pinnacle Financial will be required to take all necessary action to ensure that its benefit plans with respect to its senior executive officers comply in all respects with Section 111(b) of the Emergency Economic Stabilization Act of 2008, and the regulations issued and in effect thereunder as of the closing date of the sale of the preferred shares to the United States Treasury. This means that, among other things, while the U.S. Treasury owns debt or equity securities issued by Pinnacle Financial in connection with the TARP capital purchase program, Pinnacle Financial must:

Ensure that the incentive compensation programs for its senior executive officers do not encourage unnecessary and excessive risks that threaten the value of Pinnacle Financial;

Implement a required clawback of any bonus or incentive compensation paid to Pinnacle Financial s senior executive officers based on statements of earnings, gains, or other criteria that are later proven to be materially inaccurate;

Not make any golden parachute payment (as defined in the Internal Revenue Code) to any of Pinnacle Financial s senior executive officers; and

Agree not to deduct for tax purposes executive compensation in excess of $500,000 in any one fiscal year for each of Pinnacle Financial s senior executive officers.

On February 17, 2009 President Obama signed into law The American Recovery and Reinvestment Act of 2009 (ARRA), more commonly known as the economic stimulus or economic recovery package. ARRA includes a wide variety of programs intended to stimulate the economy and provide for extensive infrastructure, energy, health, and education needs. In addition, ARRA imposes certain new executive compensation and corporate expenditure limits on all current and future TARP recipients, including Pinnacle Financial, that are in addition to those previously announced by the U.S. Treasury, until the institution has repaid the U.S. Treasury, which is now permitted under ARRA without penalty and without the need to raise new capital, subject to the U.S. Treasury s consultation with the recipient s appropriate regulatory agency.

Pinnacle National

We own one bank - Pinnacle National. Pinnacle National is a national bank chartered under the federal National Bank Act. As a result, it is subject to the supervision, examination and reporting requirements of the National Bank Act and the regulations of the Office of the Comptroller of the Currency (the OCC). The OCC regularly examines Pinnacle National s operations and has the authority to approve or disapprove mergers, the establishment of branches and similar corporate actions. The OCC also has the power to prevent the continuance or development of unsafe or unsound banking practices or other violations of law. Additionally, Pinnacle National s deposits are insured by the FDIC to the maximum extent provided by law. Pinnacle National also is subject to numerous state and federal statutes and regulations that will affect its business, activities and operations.

Branching. While the OCC has authority to approve branch applications, national banks are required by the National Bank Act to adhere to branching laws applicable to state chartered banks in the states in which they are located. With prior regulatory approval, Tennessee law permits banks based in the state to either establish new or acquire existing branch offices throughout Tennessee. Pinnacle National and any other national or state-chartered bank generally may branch across state lines by merging with banks in other states if allowed by the applicable states laws. Tennessee law, with limited exceptions, currently permits branching across state lines either through interstate merger, branch acquisition, or branch establishment. The laws of Alabama, North Carolina and Virginia would allow Pinnacle to acquire or establish branches in those states, and banks in those states to similarly branch in Tennessee.

FDIC Insurance. The FDIC has adopted a risk-based assessment system for insured depository institutions that takes into account the risks attributable to different categories and concentrations of assets and liabilities. In early 2006, Congress passed the Federal Deposit Insurance Reform Act of 2005, which made certain changes to the Federal deposit insurance program. These changes included merging the Bank Insurance Fund and the Savings Association Insurance Fund, increasing retirement account coverage to $250,000 and providing for inflationary adjustments to general coverage beginning in 2010, providing the FDIC with authority to set the fund s reserve ratio within a specified range, and requiring dividends to banks if the reserve ratio exceeds certain levels. The new statute grants banks an assessment credit based on their share of the assessment base on December 31, 1996, and the amount of the credit can be used to reduce assessments in any year subject to certain limitations. Because it was not organized until 2000, Pinnacle National was not eligible to receive this one-time assessment credit; however, approximately $297,000 in credits were available from the Cavalry acquisition, all of which were used to reduce our insurance assessment in 2007.

ESSA provides for a temporary increase in the basic limit on federal deposit insurance coverage from $100,000 to $250,000 per depositor. This legislation provides that the basic deposit insurance limit will return to $100,000 on December 31, 2009. In addition, on October 14, 2008, the FDIC instituted a Temporary Liquidity Guarantee Program that provided for FDIC guarantees of unsecured debt of depository institutions and certain holding companies and for temporary unlimited FDIC coverage of non-interest bearing deposit transaction accounts. Institutions were automatically covered, without cost, under these programs for 30 days (later extended until December 5, 2008); however, after the specified deadline (December 5, 2008), institutions were required to opt-out of these programs if they did not wish to participate and incur fees thereunder. Pinnacle Financial has elected to participate in the transaction account guarantee program, which expires on December 31, 2009, and the temporary debt guarantee program. Under the transaction account guarantee program, an institution can provide full coverage on non-interest bearing transaction accounts for an annual assessment of 10 basis points of any deposit amounts exceeding the $250,000 deposit insurance limit, in addition to the normal risk-based assessment. Under the terms of the temporary debt guarantee program, Pinnacle Financial is eligible to issue prior to June 30, 2009 up to $18,000,000 of senior unsecured debt guaranteed by the FDIC until the earlier of the maturity of such debt or June 30, 2012. Such guaranteed debt would be subject to an annual assessment amount ranging from 50 to 100 basis points depending on its maturity date.

The FDIC may terminate its insurance of deposits if it finds that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC.

Capital Adequacy

Both Pinnacle Financial and Pinnacle National are required to comply with the capital adequacy standards established by the Federal Reserve, in our case, and the OCC, in the case of Pinnacle National. The Federal Reserve has established a risk-based and a leverage measure of capital adequacy for bank holding companies. Pinnacle National is also subject to risk-based and leverage capital requirements adopted by the OCC, which are substantially similar to those adopted by the Federal Reserve for bank holding companies.

The risk-based capital standards are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and bank holding companies, to account for off-balance-sheet exposure, and to minimize disincentives for holding liquid assets. Assets and off-balance-sheet items, such as letters of credit and unfunded loan commitments, are assigned to broad risk categories, each with appropriate risk weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance-sheet items.

The minimum guideline for the ratio of total capital to risk-weighted assets is 8%. Total capital consists of two components, Tier 1 capital and Tier 2 capital. Tier 1 capital generally consists of common stock, minority interests in the equity accounts of consolidated subsidiaries, noncumulative perpetual preferred stock, and a limited amount of cumulative perpetual preferred stock, less goodwill and other specified intangible assets. The preferred stock that Pinnacle Financial sold to the U.S. Treasury in connection with the TARP capital purchase program qualifies as Tier 1 capital. Tier 1 capital must equal at least 4% of risk-weighted assets. Tier 2 capital generally consists of subordinated debt, other preferred stock, and a limited amount of loan loss reserves. The total amount of Tier 2 capital is limited to 100% of Tier 1 capital.

In addition, the Federal Reserve has established minimum leverage ratio guidelines for bank holding companies. These guidelines provide for a minimum ratio of Tier 1 capital to average assets, less goodwill and other specified intangible assets, of 3% for bank holding companies that meet specified criteria, including having the highest regulatory rating and implementing the Federal Reserve s risk-based capital measure for market risk. All other bank holding companies generally are required to maintain a leverage ratio of at least 4%. The guidelines also provide that bank holding companies experiencing high internal growth, as is our case, or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels. Furthermore, the Federal Reserve has indicated that it will consider a bank holding company s Tier 1 capital leverage ratio, after deducting all intangibles, and other indicators of capital strength in evaluating proposals for expansion or new activities.

Information concerning our, and Pinnacle National s, regulatory ratios at December 31, 2008 is included in the Notes to the Consolidated Financial Statements.

If our growth rate continues as anticipated, our assets will grow faster than our capital and our capital ratios will decline. Capital ratios could also decline as a result of asset quality deterioration. In order to maintain capital at Pinnacle National at appropriate levels, we may be required to incur borrowings or issue additional trust preferred or equity securities, the proceeds of which would be contributed to Pinnacle National.

Failure to meet capital guidelines could subject a bank or bank holding company to a variety of enforcement remedies, including issuance of a capital directive, the termination of deposit insurance by the FDIC, a prohibition on accepting brokered deposits, and other restrictions on its business. As described above, significant additional restrictions can be imposed on FDIC-insured depository institutions that fail to meet applicable capital requirements.

Prompt Corrective Action

The Federal Deposit Insurance Corporation Improvement Act of 1991 establishes a system of prompt corrective action to resolve the problems of undercapitalized financial institutions. Under this system, the federal banking regulators have established five capital categories (well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized) into one of which all institutions are placed. Federal banking regulators are required to take various mandatory supervisory actions and are authorized to take other discretionary actions with respect to institutions in the three undercapitalized categories. The severity of the action depends upon the capital category in which the institution is placed. Generally, subject to a narrow exception, the banking regulator must appoint a receiver or conservator for an institution that is critically undercapitalized. The federal banking agencies have specified by regulation the relevant capital level for each category.

An institution that is categorized as undercapitalized, significantly undercapitalized, or critically undercapitalized is required to submit an acceptable capital restoration plan to its appropriate federal banking agency. A bank holding company must guarantee that a subsidiary depository institution meets its capital restoration plan, subject to various limitations. The controlling holding company s obligation to fund a capital restoration plan is limited to the lesser of 5% of an undercapitalized subsidiary s assets or the amount required to meet regulatory capital requirements. An undercapitalized institution is also generally prohibited from increasing its average total assets, making acquisitions, establishing any branches or engaging in any new line of business, except under an accepted capital restoration plan or with FDIC approval. The regulations also establish procedures for downgrading an institution and a lower capital category based on supervisory factors other than capital. As of December 31, 2008, we believe Pinnacle National and our other banking subsidiaries in existence at that date would be considered well capitalized by their primary regulators.

Payment of Dividends

We are a legal entity separate and distinct from Pinnacle National. Over time, the principal source of our cash flow, including cash flow to pay dividends to our holders of trust preferred securities, holders of the Series A preferred stock we issued to the United States Treasury in connection with the CPP and to our common stock shareholders, will be dividends that Pinnacle National pays to us as its sole shareholder. Under Tennessee law, we are not permitted to pay dividends if, after giving effect to such payment, we would not be able to pay our debts as they become due in the usual course of business or our total assets would be less than the sum of our total liabilities plus any amounts needed to satisfy any preferential rights if we were dissolving. In addition, in deciding whether or not to declare a dividend of any particular size, our board of directors must consider our current and prospective capital, liquidity, and other needs.

In addition to the limitations on our ability to pay dividends under Tennessee law, our ability to pay dividends on our common stock is also limited by our participation in the CPP and by certain statutory or regulatory limitations. Prior to December 12, 2011, unless we have redeemed the Series A preferred stock issued to the U.S. Treasury in the CPP or the U.S. Treasury has transferred the Series A preferred stock to a third party, the consent of the U.S. Treasury must be received before we can declare or pay any dividend or make any distribution on our common stock. Furthermore, if we are not current in the payment of quarterly dividends on the Series A preferred stock, we can not pay dividends on our common stock.

Statutory and regulatory limitations also apply to Pinnacle National s payment of dividends to us. Pinnacle National is required by federal law to obtain the prior approval of the OCC for payments of dividends if the total of all dividends declared by its board of directors in any year will exceed (1) the total of Pinnacle National s net profits for that year, plus (2) Pinnacle National s retained net profits of the preceding two years, less any required transfers to surplus. As of December 31, 2008, Pinnacle National could pay dividends to us of $53.9 million without seeking prior regulatory approval. Generally, federal regulatory policy encourages holding company debt to be serviced by subsidiary bank dividends or additional equity issuances instead of utilizing additional debt for such purpose. As a result, during 2008, Pinnacle National paid dividends to Pinnacle Financial of $5.0 million so that Pinnacle Financial could service its subordinated debt obligations.

The payment of dividends by Pinnacle National and us may also be affected by other factors, such as the requirement to maintain adequate capital above regulatory guidelines. If, in the opinion of the OCC, Pinnacle National was engaged in or about to engage in an unsafe or unsound practice, the OCC could require, after notice and a hearing, that Pinnacle National stop or refrain from engaging in the practice. The federal banking agencies have indicated that paying dividends that deplete a depository institution s capital base to an inadequate level would be an unsafe and unsound banking practice. Under the Federal Deposit Insurance Corporation Improvement Act of 1991, a depository institution may not pay any dividend if payment would cause it to become undercapitalized or if it already is undercapitalized. Moreover, the federal agencies have issued policy statements that provide that bank holding companies and insured banks should generally only pay dividends out of current operating earnings. See Prompt Corrective Action above.

Restrictions on Transactions with Affiliates

Both Pinnacle Financial and Pinnacle National are subject to the provisions of Section 23A of the Federal Reserve Act. Section 23A places limits on the amount of:

- A bank s loans or extensions of credit to affiliates;
- A bank s investment in affiliates;
- Assets a bank may purchase from affiliates, except for real and personal property exempted by the Federal Reserve;
- The amount of loans or extensions of credit to third parties collateralized by the securities or obligations of affiliates; and
- A bank s guarantee, acceptance or letter of credit issued on behalf of an affiliate.

The total amount of the above transactions is limited in amount, as to any one affiliate, to 10% of a bank s capital and surplus and, as to all affiliates combined, to 20% of a bank s capital and surplus. In addition to the limitation on the amount of these transactions, each of the above transactions must also meet specified collateral requirements. Pinnacle National must also comply with other provisions designed to avoid the taking of low-quality assets.

Pinnacle Financial and Pinnacle National are also subject to the provisions of Section 23B of the Federal Reserve Act which, among other things, prohibits an institution from engaging in the above transactions with affiliates unless the transactions are on terms substantially the same, or at least as favorable to the institution or its subsidiaries, as those prevailing at the time for comparable transactions with nonaffiliated companies.

Pinnacle National is also subject to restrictions on extensions of credit to its executive officers, directors, principal shareholders and their related interests. These extensions of credit (1) must be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third parties, and (2) must not involve more than the normal risk of repayment or present other unfavorable features.

Community Reinvestment

The Community Reinvestment Act requires that, in connection with examinations of financial institutions within their respective jurisdictions, the Federal Reserve, the OCC or the FDIC shall evaluate the record of each financial institution in meeting the credit needs of its local community, including low- and moderate-income neighborhoods. These facts are also considered in evaluating mergers, acquisitions, and applications to open a branch or facility. Failure to adequately meet these criteria could impose additional requirements and limitations on Pinnacle National. Additionally, banks are required to publicly disclose the terms of various Community Reinvestment Act-related agreements. Pinnacle National has received a satisfactory CRA rating from the OCC.

Privacy

Under the Gramm-Leach-Bliley Act, financial institutions are required to disclose their policies for collecting and protecting confidential information. Customers generally may prevent financial institutions from sharing personal financial information with nonaffiliated third parties except for third parties that market the institutions own products and services. Additionally, financial institutions generally may not disclose consumer account numbers to any nonaffiliated third party for use in telemarketing, direct mail marketing or other marketing through electronic mail to consumers. Pinnacle National has established a privacy policy to ensure compliance with federal requirements.

Other Consumer Laws and Regulations

Interest and other charges collected or contracted for by Pinnacle National are subject to state usury laws and federal laws concerning interest rates. For example, under the Soldiers and Sailors Civil Relief Act of 1940, a lender is generally prohibited from charging an annual interest rate in excess of 6% on any obligations for which the borrower is a person on active duty with the United States military. Pinnacle National s loan operations are also subject to federal laws applicable to credit transactions, such as the:

- Federal Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers;
- Home Mortgage Disclosure Act of 1975, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
- Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed or other prohibited factors in extending credit;
- Fair Credit Reporting Act of 1978, governing the use and provision of information to credit reporting agencies;
- Fair Debt Collection Act, governing the manner in which consumer debts may be collected by collection agencies;
- Bank Secrecy Act, governing how banks and other firms report certain currency transactions and maintain appropriate safeguards against money laundering activities;
- Soldiers and Sailors Civil Relief Act of 1940, governing the repayment terms of, and property rights underlying, secured obligations of persons in military service; and

Rules and regulations of the various federal agencies charged with the responsibility of implementing the federal laws.

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Pinnacle National s deposit operations are subject to the:

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

- Electronic Funds Transfer Act and Regulation E issued by the Federal Reserve to implement that act, which govern automatic deposits to and withdrawals from deposit accounts and customers rights and liabilities arising from the use of automated teller machines and other electronic banking services.

Anti-Terrorism Legislation

On October 26, 2001, the President of the United States signed the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT) Act of 2001. Under the USA PATRIOT Act, financial institutions are subject to prohibitions against specified financial transactions and account relationships as well as enhanced due diligence and know your customer standards in their dealings with foreign financial institutions and foreign customers.

In addition, the USA PATRIOT Act authorizes the Secretary of the Treasury to adopt rules increasing the cooperation and information sharing between financial institutions, regulators, and law enforcement authorities regarding individuals, entities and organizations engaged in, or reasonably suspected based on credible evidence of engaging in, terrorist acts or money laundering activities. Any financial institution complying with these rules will not be deemed to have violated the privacy provisions of the Gramm-Leach-Bliley Act, as discussed above. Pinnacle National currently has policies and procedures in place designed to comply with the USA PATRIOT Act.

Proposed Legislation and Regulatory Action

New regulations and statutes are regularly proposed that contain wide-ranging proposals for altering the structures, regulations and competitive relationships of the nation s financial institutions. We cannot predict whether or in what form any proposed regulation or statute will be adopted or the extent to which our business may be affected by any new regulation or statute. With the recent enactments of EESA and ARRA, the nature and extent of future legislative and regulatory changes affecting financial institutions is very unpredictable at this time.

Effect of Governmental Monetary Policies

Our earnings are affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. The Federal Reserve s monetary policies have had, and are likely to continue to have, an important impact on the operating results of commercial banks through the Federal Reserve s statutory power to implement national monetary policy in order, among other things, to curb inflation or combat a recession. The Federal Reserve, through its monetary and fiscal policies, affects the levels of bank loans, investments and deposits through its control over the issuance of United States government securities, its regulation of the discount rate applicable to member banks and its influence over reserve requirements to which member banks are subject. We cannot predict the nature or impact of future changes in monetary and fiscal policies.

ITEM 1A. RISK FACTORS

Investing in our common stock involves various risks which are particular to our company, our industry and our market area. Several risk factors regarding investing in our common stock are discussed below. This listing should not be considered as all-inclusive. If any of the following risks were to occur, we may not be able to conduct our business as currently planned and our financial condition or operating results could be negatively impacted. These matters could cause the trading price of our common stock to decline in future periods.

We are geographically concentrated in the Nashville, Tennessee MSA, and changes in local economic conditions impact our profitability.

We currently operate primarily in the Nashville, Tennessee MSA, and most all of our loan, deposit and other customers live or have operations in the Nashville MSA. Accordingly, our success significantly depends upon the growth in population, income levels, deposits and housing starts in the Nashville MSA, along with the continued attraction of business ventures to the area. Our profitability is impacted by the changes in general economic conditions in this market. Additionally, unfavorable local or national economic conditions could reduce our growth rate, affect the ability of our customers to repay their loans to us and generally affect our financial condition and results of operations.

We are less able than a larger institution to spread the risks of unfavorable local economic conditions across a large number of diversified economies. Moreover, we cannot give any assurance that we will benefit from any market growth or favorable economic conditions in our primary market areas if they do occur.

We may not be able to continue to expand into the Knoxville MSA in the time frame and at the levels that we currently expect and our projected expansion may continue to reduce our net income in 2009.

In order to continue our expansion into the Knoxville MSA we will be required to hire a significant number of new associates and build out a branch network. We can not assure you that we will be able to hire the number of experienced associates that we need to successfully execute our strategy in the Knoxville MSA, nor can we assure you that the associates we hire will be able to successfully execute our growth strategy in that market. Because we seek to hire experienced associates, the compensation cost associated with these individuals may be higher than that of other financial institutions of similar size in the market. If we are unable to grow our loan portfolio at planned rates, the increased compensation expense of these experienced associates may negatively impact our results of operations. Because there will be a period of time before we are able to fully deploy our resources in the Knoxville MSA, our start up costs, including the cost of our associates and our branch expansion, will negatively impact our results of operations. In addition, if we are not able to expand our branch footprint in the Knoxville MSA in the time period that we have targeted, our results of operations may be negatively impacted. Execution of our growth plans in the Knoxville MSA also depends on continued growth in the Knoxville economy, and unfavorable local or national economic conditions could reduce our growth rate, affect the ability of our customers to repay their obligations to us and generally negatively affect our financial condition and results of operations.

Recent negative developments in the financial services industry and U.S. and global credit markets may adversely impact our operations and results.

Negative developments in the latter half of 2007 and throughout 2008 in the capital markets have resulted in uncertainty in the financial markets in general with the expectation of the general economic downturn continuing into 2009. Loan portfolio performances have deteriorated at many institutions resulting from, amongst other factors, a weak economy and a decline in the value of the collateral supporting their loans. The competition for our deposits has increased significantly due to liquidity concerns at many of these same institutions. Stock prices of bank holding companies, like ours, have been negatively affected by the current condition of the financial markets, as has our ability, if needed, to raise capital or borrow in the debt markets compared to recent years. As a result, there is a potential for new federal or state laws and regulations regarding lending and funding practices and liquidity standards, and financial institution regulatory agencies are expected to be very aggressive in responding to concerns and trends identified in examinations, including the expected issuance of many formal enforcement actions. Negative developments in the financial services industry and the impact of new legislation in response to those developments could negatively impact our operations by restricting our business operations, including our ability to originate or sell loans, and adversely impact our financial performance. In addition, industry, legislative or regulatory developments may cause us to materially change our existing strategic direction, capital strategies, compensation or operating plans.

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Our continued growth may require the need for additional capital and further regulatory approvals which, if not obtained, could adversely impact our profitability and implementation of our current business plan.

To continue to grow, we will need to provide sufficient capital to Pinnacle National through earnings generation, additional equity or trust preferred offerings or borrowed funds or any combination of these sources of funds. For certain amounts or types of indebtedness, we may be required to obtain certain regulatory approvals beforehand. We recently received a $95 million preferred stock investment from the U.S. Treasury under the TARP capital purchase program. The terms of this investment provide incentives for us to replace this capital with other forms of Tier 1 capital from third parties as soon as practicable; however, our ability to raise additional capital, if needed, will depend on conditions in the capital markets at that time, which are outside our control, and on our financial performance. Accordingly, we cannot assure our ability to raise additional capital if needed on terms acceptable to us. If we cannot raise additional capital when needed, our ability to further expand and grow our operations could be materially impaired. Additionally, our current plan involves increasing our branch network, which will require capital expenditures. Our expansion efforts will likely also require certain regulatory approvals. Should we not be able to obtain such approvals or otherwise not be able to grow our asset base, our ability to attain our long-term profitability goals will be more difficult.

We have a concentration of credit exposure to borrowers in certain industries and we also target small to medium-sized businesses.

At December 31, 2008, we had significant credit exposures to borrowers in the trucking industry; commercial and residential building lessors; new home builders and to land subdividers. All of these industries are experiencing adversity in the current recession and, as a result, the borrowers in these industries could become unable to perform their obligations under their existing loan agreements, which could cause our earnings to be negatively impacted, causing the value of our common stock to decline. Furthermore, any of our large credit exposures that deteriorate unexpectedly as a result of the recession could cause us to have to make significant additional loan loss provisions, negatively impacting our earnings.

Additionally, a substantial focus of our marketing and business strategy is to serve small to medium-sized businesses in the Nashville and Knoxville MSAs. As a result, a relatively high percentage of our loan portfolio consists of commercial loans primarily to small to medium-sized business. At December 31, 2008, our commercial and industrial loans accounted for almost 29% of our total loans. During periods of economic weakness, small to medium-sized businesses may be impacted more severely and more quickly than larger businesses. Consequently, the ability of such businesses to repay their loans may deteriorate, and in some cases this determination may occur quickly, which would adversely impact our results of operations and financial condition.

Our acquisitions have significantly increased our real estate construction and development loans, which have a greater credit risk than residential mortgage loans.

Following the acquisitions of Cavalry and Mid-America, construction and development lending is a more significant portion of Pinnacle Financial s loan portfolio than it was prior to these acquisitions. The percentage of construction and land development loans in our bank subsidiaries portfolios were approximately 19.6% of total loans at December 31, 2008 compared to 21.2% at December 31, 2007, 16.9% at December 31, 2006 and 10.5% at December 31, 2005. This type of lending is generally considered to have more complex credit risks than traditional single-family residential lending because the principal is concentrated in a limited number of loans with repayment dependent on the successful operation of the related real estate project. Consequently, these loans are more sensitive to the current adverse conditions in the real estate market and the general economy. These loans are generally less predictable and more difficult to evaluate and monitor and collateral may be difficult to dispose of in a market decline. Furthermore, to the extent repayment is dependent upon the sale of newly constructed homes or of lots, such sales are likely to be at lower prices or at a slower rate than as expected when the loan was made which may result in such loans being placed on non-accrual status and subject to higher loss estimates even if the borrower keeps interest payments current. Additionally, Pinnacle National may experience significant construction loan losses because independent appraisers or project engineers inaccurately estimate the cost and value of construction loan projects. Also, in the event of a continued general economic downturn in the construction industry, Pinnacle Financial s results of operations may be adversely impacted and its net book value may be reduced.

If our allowance for loan losses is not sufficient to cover actual loan losses, our earnings will decrease.
If loan customers with significant loan balances fail to repay their loans according to the terms of these loans, our earnings and capital levels will suffer. We make various assumptions and judgments about the probable losses in our loan portfolio, including the creditworthiness of our borrowers and the value of any collateral securing the repayment of our loans. We maintain an allowance for loan losses in an attempt to cover our estimate of the probable losses in our loan portfolio. In determining the size of this allowance, we rely on an analysis of our loan portfolio based on volume and types of loans, internal loan classifications, trends in classifications, volume and trends in delinquencies, nonaccruals and charge-offs, national and local economic conditions, industry and peer bank loan quality indications, and other pertinent factors and information. Because we are a relatively young organization, our allowance estimation may be less reflective of our historical loss experience than a more mature organization. If our

assumptions are inaccurate, our current allowance may not be sufficient to cover potential loan losses, and additional provisions may be necessary which would decrease our earnings.

In addition, federal and state regulators periodically review our loan portfolio and may require us to increase our allowance for loan losses or recognize loan charge-offs. Their conclusions about the quality of our loan portfolio may be different than ours. Any increase in our allowance for loan losses or loan charge-offs as required by these regulatory agencies could have a negative effect on our operating results.

Noncore funding represents a large component of our funding base.

In addition to the traditional core deposits, such as demand deposit accounts, interest checking, money market savings and certificates of deposits, we utilize several noncore funding sources, such as brokered certificates of deposit, Federal Home Loan Bank of Cincinnati advances, Federal funds purchased and other sources. We utilize these noncore funding sources to fund the ongoing operations and growth of Pinnacle Financial. The availability of these noncore funding sources are subject to broad economic conditions and, as such, the pricing on these sources may fluctuate significantly and/or be restricted at any point in time, thus impacting our net interest income, our immediate liquidity and/or our access to additional liquidity.

Brokered certificates of deposit have received scrutiny from regulators in recent months. We impose upon ourselves limitations as to the absolute level of brokered deposits we may have on our balance sheet at any point in time. The pricing of these deposits are subject to the broader wholesale funding market and may fluctuate significantly in a very short period of time. Additionally, the availability of these deposits is impacted by overall market conditions as investors determine whether to invest in the less risky certificates of deposit or in the more risky debt and equity markets. As money flows between these various investment instruments, market conditions will impact the pricing and availability of brokered funds.

In recent months, the financial media has disclosed that the nation s Federal Home Loan Bank (FHLB) system may be under stress due to deterioration in the financial markets, particularly in relation to valuation of mortgage securities. Several FHLB institutions have announced impairment charges of these and other assets and as such their capital positions have deteriorated to the point that they may suspend dividend payments to their members. We are a member of the FHLB-Cincinnati which continues to pay dividends. However, should financial conditions continue to weaken, the FHLB system (including FHLB-Cincinnati) in the future may have to, not only suspend dividend payments, but also curtail advances to member institutions like Pinnacle Financial. Should the FHLB system deteriorate to the point of not being able to fund future advances to banks, including Pinnacle National, this would place increased pressure on other wholesale funding sources.

We impose certain internal limits as to the absolute level of noncore funding we will incur on our balance sheet at any point in time. Should we exceed those limitations, we may need to modify our growth plans, liquidate certain assets, participate loans to correspondents or execute other actions to allow for us to return to an acceptable level of noncore funding within a reasonable amount of time.

If the federal funds rate remains at current extremely low levels, our net interest margin, and consequently our net earnings, may continue to be negatively impacted.

Because of significant competitive deposit pricing pressures in our market and the negative impact of these pressures on our cost of funds, coupled with the fact that a significant portion of our loan portfolio has variable rate pricing that moves in concert with changes to the Federal Reserve s federal funds rate (which is at an extremely low rate as a result of the current recession), we have experienced net interest margin compression throughout 2008. Because of these competitive pressures, we are unable to lower the rate that we pay on interest-bearing liabilities to the same extent and as quickly as the yields we charge on interest-earning assets. As a result, our net interest margin, and consequently our profitability, has been negatively impacted. If the Federal Reserve s federal funds rate remains at extremely low levels, our higher funding costs may negatively impact our net interest margin and results of operations.

Fluctuations in interest rates could reduce our profitability.

The absolute level of interest rates as well as changes in interest rates may affect our level of interest income, the primary component of our gross revenue, as well as the level of our interest expense. Interest rate fluctuations are caused by many factors which, for the most part, are not under our direct control. For example, national monetary policy plays a significant role in the determination of interest rates. Additionally, competitor pricing and the resulting negotiations that occur with our customers also impact the rates we collect on loans and the rates we pay on deposits.

As interest rates change, we expect that we will periodically experience gaps in the interest rate sensitivities of our assets and liabilities, meaning that either our interest-bearing liabilities will be more sensitive to changes in market interest rates than our interest-earning assets, or vice versa. In either event, if market interest rates should move contrary to our position, this gap may work against us, and our earnings may be negatively affected.

Changes in the level of interest rates also may negatively affect our ability to originate real estate loans, the value of our assets and our ability to realize gains from the sale of our assets, all of which ultimately affect our earnings. A decline in the market value of our assets may limit our ability to borrow additional funds. As a result, we could be required to sell some of our loans and investments under adverse market conditions, upon terms that are not favorable to us, in order to maintain our liquidity. If those sales are made at prices lower than the amortized costs of the investments, we will incur losses.

National or state legislation or regulation may increase our expenses and reduce earnings.

Changes in tax law, federal legislation, regulation or policies, such as bankruptcy laws, deposit insurance, and capital requirements, among others, can result in significant increases in our expenses and/or charge-offs, which may adversely affect our earnings. Changes in state or federal tax laws or regulations can have a similar impact.

Loss of our senior executive officers or other key employees could impair our relationship with our customers and adversely affect our business.

We have assembled a senior management team which has a substantial background and experience in banking and financial services in the Nashville market. Loss of these key personnel could negatively impact our earnings because of their skills, customer relationships and/or the potential difficulty of promptly replacing them.

Competition with other banking institutions could adversely affect our profitability.

A number of banking institutions in the Nashville market have higher lending limits, more banking offices, and a larger market share of loans or deposits. In addition, our asset management division competes with numerous brokerage firms and mutual fund companies which are also much larger. In some respects, this may place these competitors in a competitive advantage, although many of our customers have selected us because of service quality concerns at the larger enterprises. This competition may limit or reduce our profitability, reduce our growth and adversely affect our results of operations and financial condition.

The Series A preferred stock impacts net income available to our common shareholders and our earnings per share.

As long as shares of our Series A preferred stock are outstanding, no dividends may be paid on our common stock unless all dividends on the Series A preferred stock have been paid in full. Additionally, for so long as the Treasury owns shares of the Series A preferred stock, we are not permitted to pay cash dividends on our common stock without the Treasury s consent. The dividends declared on shares of our Series A preferred stock will reduce the net income available to common shareholders and our earnings per common share. Additionally, warrants to purchase our common stock issued to the Treasury, in conjunction with the issuance of the Series A Preferred Stock, may be dilutive to our earnings per share. The shares of our Series A preferred stock will also receive preferential treatment in the event of our liquidation, dissolution or winding up.

Moreover, holders of our common stock are entitled to receive dividends only when, as and if declared by our board of directors. To date, we have not paid any cash dividends on our common stock and we do not believe that we will consider paying dividends until Pinnacle National has reached a level of profitability appropriate to fund such dividends and support asset growth.

Holders of the Series A preferred stock have rights that are senior to those of our common shareholders.

The Series A preferred stock that we have issued to the Treasury is senior to our shares of common stock and holders of the Series A preferred stock have certain rights and preferences that are senior to holders of our common stock. The Series A preferred stock will rank senior to our common stock and all other equity securities of ours designated as ranking junior to the Series A preferred stock. So long as any shares of the Series A preferred stock remain outstanding, unless all accrued and unpaid dividends for all prior dividend periods have been paid or are contemporaneously declared and paid in full, no dividend whatsoever shall be paid or declared on our common stock or other junior stock, other than a dividend payable solely in common stock. We and our subsidiaries also may not purchase, redeem or otherwise acquire for consideration any shares of our common stock or other junior stock unless we have paid in full all accrued dividends on the Series A preferred stock for all prior dividend periods, other than in certain circumstances described more fully below. Furthermore, the Series A preferred stock is entitled to a liquidation preference over shares of our common stock in the event of our liquidation, dissolution or winding up.

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Holders of the Series A preferred stock may, under certain circumstances, have the right to elect two directors to our board of directors.

In the event that we fail to pay dividends on the Series A preferred stock for an aggregate of six quarterly dividend periods or more (whether or not consecutive), the authorized number of directors then constituting our board of directors will be increased by two. Holders of the Series A preferred stock, together with the holders of any outstanding parity stock with like voting rights, referred to as voting parity stock, voting as a single class, will be entitled to elect the two additional members of our board of directors, referred to as the preferred stock directors, at the next annual meeting (or at a special meeting called for the purpose of electing the preferred stock directors prior to the next annual meeting) and at each subsequent annual meeting until all accrued and unpaid dividends for all past dividend periods have been paid in full.

Holders of the Series A preferred stock have limited voting rights.

Except as otherwise required by law and in connection with the election of directors to our board of directors in the event that we fail to pay dividends on the Series A preferred stock for an aggregate of at least six quarterly dividend periods (whether or not consecutive), holders of the Series A preferred stock have limited voting rights. So long as shares of the Series A preferred stock are outstanding, in addition to any other vote or consent of shareholders required by law or our amended and restated charter, the vote or consent of holders owning at least 66 2/3% of the shares of Series A preferred stock outstanding is required for (1) any authorization or issuance of shares ranking senior to the Series A preferred stock; (2) any amendment to the rights of the Series A preferred stock so as to adversely affect the rights, preferences, privileges or voting power of the Series A preferred stock; or (3) consummation of any merger, share exchange or similar transaction unless the shares of Series A preferred stock remain outstanding, or if we are not the surviving entity in such transaction, are converted into or exchanged for preference securities of the surviving entity and the shares of Series A preferred stock remaining outstanding or such preference securities have such rights, preferences, privileges and voting power as are not materially less favorable to the holders than the rights, preferences, privileges and voting power of the shares of Series A preferred stock.

We may issue additional common stock or other equity securities in the future which could dilute the ownership interest of existing shareholders.

In order to maintain our capital at desired or regulatory-required levels or to replace existing capital such as our Series A preferred stock, we may be required to issue additional shares of common stock, or securities convertible into, exchangeable for or representing rights to acquire shares of common stock. We may sell these shares at prices below the current market price of shares, and the sale of these shares may significantly dilute shareholder ownership. We could also issue additional shares in connection with acquisitions of other financial institutions.

Even though our common stock is currently traded on the Nasdaq Stock Market s Global Select Market, it has less liquidity than many other stocks quoted on a national securities exchange.

The trading volume in our common stock on the Nasdaq Global Select Market has been relatively low when compared with larger companies listed on the Nasdaq Global Select Market or other stock exchanges. Although we have experienced increased liquidity in our stock, we cannot say with any certainty that a more active and liquid trading market for our common stock will continue to develop. Because of this, it may be more difficult for shareholders to sell a substantial number of shares for the same price at which shareholders could sell a smaller number of shares.

We cannot predict the effect, if any, that future sales of our common stock in the market, or the availability of shares of common stock for sale in the market, will have on the market price of our common stock. We can give no assurance that sales of substantial amounts of common stock in the market, or the potential for large amounts of sales in the market, would not cause the price of our common stock to decline or impair our future ability to raise capital through sales of our common stock.

The market price of our common stock has fluctuated significantly, and may fluctuate in the future. These fluctuations may be unrelated to our performance. General market or industry price declines or overall market volatility in the future could adversely affect the price of our common stock, and the current market price may not be indicative of future market prices.

If a change in control is delayed or prevented, the market price of our common stock could be negatively affected.

Provisions in our corporate documents, as well as certain federal and state regulations, may make it difficult and expensive to pursue a tender offer, change in control or takeover attempt that our board of directors opposes. As a result, our shareholders may not have an opportunity to participate in such a transaction, and the trading price of our stock may not rise to the level of other institutions that are more vulnerable to hostile takeovers. Anti-takeover provisions contained in our charter also will make it more difficult for an outside shareholder to remove our current board of directors or management.

Holders of Pinnacle Financial s bank indebtedness and junior subordinated debentures have rights that are senior to those of Pinnacle Financial s common shareholders.

Pinnacle Financial has supported its continued growth through the issuance of trust preferred securities from special purpose trusts and accompanying junior subordinated debentures. At December 31, 2008, Pinnacle Financial had outstanding trust preferred securities and accompanying junior subordinated debentures totaling $82.5 million. Payments of the principal and interest on the trust preferred securities of these trusts are conditionally guaranteed by Pinnacle Financial. Further, the accompanying junior subordinated debentures Pinnacle Financial issued to the trusts are senior to Pinnacle Financial s shares of common stock. As a result, Pinnacle Financial must make payments on the junior subordinated debentures before any dividends can be paid on its common stock and, in the event of Pinnacle Financial s bankruptcy, dissolution or liquidation, the holders of the junior subordinated debentures must be satisfied before any distributions can be made on Pinnacle Financial s common stock. Pinnacle Financial has the right to defer distributions on its junior subordinated debentures (and the related trust preferred securities) for up to five years, during which time no dividends may be paid on its common stock.

Our business is dependent on technology, and an inability to invest in technological improvements may adversely affect our results of operations and financial condition.

The financial services industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services. In addition to better serving customers, the effective use of technology increases efficiency and enables financial institutions to reduce costs. We have made significant investments in data processing, management information systems and internet banking accessibility. Our future success will depend in part upon our ability to create additional efficiencies in our operations through the use of technology, particularly in light of our past and projected growth strategy. Many of our competitors have substantially greater resources to invest in technological improvements. We cannot make assurances that our technological improvements will increase our operational efficiency or that we will be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers.

Our internal control over financial reporting may have weaknesses or inadequacies that may be material.

Section 404 of the Sarbanes-Oxley Act of 2002 requires us to perform an evaluation of our internal control over financial reporting and our auditor to attest to such evaluation on an annual basis. Management concluded that our internal control over financial reporting was effective at December 31, 2008. Management s report on internal control over financial reporting is included on page 56 of this Form 10-K and the report of our independent registered public accounting firm on internal control over financial reporting is included on page 58 of this Form 10-K. While our management did not identify any material weaknesses in our internal control over financial reporting at December 31, 2008, and concluded that our internal control over financial reporting was effective, we cannot make any assurances that material weaknesses in our internal control over financial reporting will not be identified in the future. If any material weaknesses are identified in the future, we may be required to make material changes in our internal control over financial reporting which could negatively impact our results of operations. In addition, upon such occurrence, our management may not be able to conclude that our internal control over financial reporting is effective or our independent registered public accounting firm may not be able to attest that our internal control over financial reporting was effective. If we cannot conclude that our internal control over financial reporting is effective or if our independent registered public accounting firm is not able to attest that our internal control over financial reporting is effective, we may be subject to regulatory scrutiny, and a loss of public confidence in our internal control over financial reporting which may cause the value of our common stock to decrease.

We are subject to various statutes and regulations that may limit our ability to take certain actions.

We operate in a highly regulated industry and are subject to examination, supervision, and comprehensive regulation by various regulatory agencies. Our compliance with these regulations is costly and restricts certain of our activities, including payment of dividends, mergers and acquisitions, investments, loans and interest rates charged, interest rates paid on deposits and locations of offices. We are also subject to capitalization guidelines established by our regulators, which require us to maintain adequate capital to support our growth.

The laws and regulations applicable to the banking industry could change at any time, and we cannot predict the effects of these changes on our business and profitability. Because government regulation greatly affects the business and financial results of all commercial banks and bank holding companies, our cost of compliance could adversely affect our ability to operate profitably.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

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ITEM 2. PROPERTIES

The Company s executive offices are located at 211 Commerce Street, Suite 300, Nashville, Tennessee. The Company operates 33 banking locations throughout our market areas, of which for 9 locations the Company leases the land, the building or both. The Company has locations in the Tennessee municipalities of Nashville, Knoxville, Murfreesboro, Dickson, Ashland City, Mt. Juliet, Lebanon, Franklin, Brentwood, Hendersonville, Goodlettesville, Smyrna and Shelbyville.

ITEM 3. LEGAL PROCEEDINGS

As of the date hereof, there are no material pending legal proceedings to which Pinnacle Financial or any of its subsidiaries is a party or of which any of its or its subsidiaries properties are subject; nor are there material proceedings known to Pinnacle Financial or any of its subsidiaries to be contemplated by any governmental authority; nor are there material proceedings known to Pinnacle Financial or any of its subsidiaries, pending or contemplated, in which any director, officer or affiliate or any principal security holder of Pinnacle Financial or any of its subsidiaries or any associate of any of the foregoing, is a party adverse to Pinnacle Financial or any of its subsidiaries or has a material interest adverse to Pinnacle Financial or any of its subsidiaries.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

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PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Pinnacle Financial s common stock is traded on the Nasdaq Global Select Market under the symbol PNFP and has traded on that market since July 3, 2006. Prior to that date, Pinnacle Financial s common stock traded on the Nasdaq National Market and the Nasdaq SmallCap Market. The following table shows the high and low sales price information for Pinnacle Financial s common stock for each quarter in 2008 and 2007 as reported on the Nasdaq Global Select Market.

	Price Per Share	
	High	Low
2008:		
First quarter	$ 26.75	$ 20.82
Second quarter	29.29	20.05
Third quarter	36.57	19.30
Fourth quarter	32.00	22.01
2007:		
First quarter	$ 33.85	$ 29.40
Second quarter	31.48	28.27
Third quarter	31.31	21.62
Fourth quarter	30.93	24.85

As of January 31, 2009, Pinnacle Financial had approximately 10,000 shareholders of record.

Pinnacle Financial has not paid any cash dividends since inception, and it does not anticipate that it will consider paying dividends until Pinnacle National has achieved a level of profitability appropriate to fund such dividends and support asset growth. See ITEM 1. Business Supervision and Regulation Payment of Dividends and ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations for additional information on dividend restrictions applicable to Pinnacle Financial.

Pinnacle Financial did not repurchase any shares of its common stock during the quarter ended December 31, 2008.

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ITEM 6. SELECTED FINANCIAL DATA

	2008	2007(1)	2006(2)	2005	20
	(in thousands, except per share data, ratios and percentages)				
nent of Financial Condition Data:					
ssets	$ 4,754,075	$ 3,794,170	$ 2,142,187	$1,016,772	$ 727
net of unearned income	3,354,907	2,749,641	1,497,735	648,024	472
ance for loan losses	36,484	28,470	16,118	7,858	5
ecurities	849,781	522,685	346,494	279,080	208
vill and core deposit intangibles	261,032	260,900	125,673	-	
ts and securities sold under agreements to repurchase	3,717,544	3,081,390	1,763,427	875,985	602
ces from FHLB and other borrowings	273,609	141,666	53,726	41,500	53
linated debt	97,476	82,476	51,548	30,929	10
olders equity	627,298	466,610	256,017	63,436	57
e Statement Data:					
t income	$ 206,082	$ 150,931	$ 109,696	$ 46,308	$ 27
t expense	91,867	75,219	48,743	17,270	7
erest income	114,215	75,712	60,953	29,038	20
on for loan losses	11,214	4,720	3,732	2,152	2
erest income after provision for loan losses	103,001	70,992	57,221	26,886	17
erest income	34,718	22,521	15,786	5,394	4
erest expense	94,478	60,480	46,624	21,032	14
e before income taxes	43,241	33,033	26,383	11,248	7
e tax expense	12,367	9,992	8,456	3,193	2
come	30,874	23,041	17,927	8,055	5
ed dividends and accretion on common stock warrants	309	-	-	-	
come available to common stockholders	$ 30,565	$ 23,041	$ 17,927	$ 8,055	$ 5
nare Data:					
gs per share available to common stockholders basic	$ 1.34	$ 1.43	$ 1.28	$ 0.96	$
ted average shares outstanding basic	22,793,699	16,100,076	13,954,077	8,408,663	7,750
gs per share available to common stockholders diluted	$ 1.27	$ 1.34	$ 1.18	$ 0.85	$
ted average shares outstanding diluted	24,053,972	17,255,543	15,156,837	9,464,500	8,698
value per share	$ 26.40	$ 20.96	$ 16.57	$ 7.53	$
on shares outstanding at end of period	23,762,124	22,264,817	15,446,074	8,426,551	8,389
mance Ratios and Other Data:					
on average assets	0.74%	0.96%	1.01%	0.93%	
on average stockholders equity	6.13%	8.34%	8.66%	13.23%	1
erest margin (3)	3.17%	3.55%	3.90%	3.60%	
erest spread (4)	2.78%	2.88%	3.20%	3.16%	
erest income to average assets	0.84%	0.94%	0.89%	0.62%	
erest expense to average assets	2.30%	2.53%	2.61%	2.42%	
ncy ratio (5)	63.43%	61.57%	60.76%	61.08%	5
ge loan to average deposit ratio	97.70%	94.88%	88.73%	81.3%	
ge interest-earning assets to average interest-bearing liabilities	115.27%	119.46%	122.10%	120.0%	1
ge equity to average total assets ratio	12.15%	11.56%	11.64%	7.00%	

Quality Ratios:					
ance for loan losses to nonaccrual loans	335.95%	144.69%	227.98%	1708.26%	100
ance for loan losses to total loans	1.09%	1.04%	1.08%	1.21%	
rforming assets to total assets	0.61%	0.56%	0.37%	0.05%	
crual loans to total loans	0.32%	0.72%	0.47%	0.07%	
an charge-offs (recoveries) to average loans	0.11%	0.06%	0.05%	(0.01)%	
l Ratios (Pinnacle Financial):					
ge (6)	10.5%	11.6%	9.5%	9.9%	
risk-based capital	12.1%	9.5%	10.9%	11.7%	
isk-based capital	13.5%	10.4%	11.8%	12.6%	

(1) Information for 2007 fiscal year includes the operations of Mid-America, which Pinnacle Financial merged with on November 30, 2007 and reflects approximately 6.7 million shares of Pinnacle Financial common stock issued in connection with the merger.

(2) Information for 2006 fiscal year includes the operations of Cavalry, which Pinnacle Financial merged with on March 15, 2006 and reflects approximately 6.9 million shares of Pinnacle Financial common stock issued in connection with the merger.

(3) Net interest margin is the result of net interest income for the period divided by average interest earning assets.
(4) Net interest spread is the result of the difference between the interest yield earned on interest earning assets less the interest paid on interest bearing liabilities.
(5) Efficiency ratio is the result of noninterest expense divided by the sum of net interest income and noninterest income.
(6) Leverage ratio is computed by dividing Tier 1 capital by average total assets for the fourth quarter of each year.

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

The following is a discussion of our financial condition at December 31, 2008 and 2007 and our results of operations for each of the three-years ended December 31, 2008. The purpose of this discussion is to focus on information about our financial condition and results of operations which is not otherwise apparent from the consolidated financial statements. The following discussion and analysis should be read along with our consolidated financial statements and the related notes included elsewhere herein.

Overview

General. Our rapid organic growth together with our merger with Mid-America Bancshares, Inc. (Mid-America), a two-bank holding company in Nashville, Tennessee, on November 30, 2007 and our continued expansion in the Knoxville, Tennessee market has had a material impact on Pinnacle Financial s financial condition and results of operations in 2008 as compared to 2007. This rapid growth along with the Mid-America merger and the Knoxville market expansion are discussed more fully below. Our fully diluted net income per share for the years ended December 31, 2008 and 2007 was $1.27 and $1.34, respectively. December 31, 2008, loans totaled $3.355 billion, as compared to $2.750 billion at December 31, 2007, while total deposits increased to $3.533 billion at December 31, 2008 from $2.925 billion at December 31, 2007.

Acquisition Mid-America. On November 30, 2007, we consummated a merger with Mid-America. Pursuant to the merger agreement, Mid-America shareholders received a fixed exchange ratio of 0.4655 shares of our common stock and $1.50 in cash for each share of Mid-America common stock, or approximately 6.7 million Pinnacle Financial shares and $21.6 million in cash. We financed the cash portion of the merger consideration with the proceeds of a $30 million trust preferred securities offering by an affiliated trust. The accompanying consolidated financial statements include the activities of the former Mid-America since November 30, 2007.

During the years ended December 31, 2008 and 2007, we incurred merger integration expense related to the merger with Mid-America of $7,116,000 and $622,000, respectively. These expenses were directly related to the merger, and consisted primarily of retention costs, severance costs and costs to integrate processing systems and are reflected in the accompanying consolidated statements of income as merger related expenses.

Acquisition Cavalry Bancorp, Inc. On March 15, 2006, we consummated our merger with Cavalry Bancorp, Inc. (Cavalry). Pursuant to the merger agreement, we acquired all Cavalry common stock via a tax-free exchange whereby Cavalry shareholders received a fixed exchange ratio of 0.95 shares of our common stock for each share of Cavalry common stock, or approximately 6.9 million Pinnacle Financial shares. The financial information herein includes the activities of the former Cavalry since March 15, 2006.

Acquisition Beach & Gentry Insurance LLC. On July 2, 2008, we announced the merger of Murfreesboro, Tenn. based Beach & Gentry Insurance LLC (Beach & Gentry). Beach & Gentry merged with Miller & Loughry Insurance Services Inc. The combined company took the name Miller Loughry Beach Insurance Services, Inc. and has consolidated offices in Pinnacle Financial s offices in Murfreesboro. We anticipate that this merger will result in an increase to our insurance sales commissions in future periods.

Knoxville expansion. During April of 2007, we announced a de novo expansion of our firm to the Knoxville MSA. At that time, we had hired several new associates from other financial institutions in that market and had negotiated a lease agreement for our main office facility with future plans to construct four additional offices over the next few years. In June of 2007, we opened our first full service branch facility in Knoxville and we anticipate opening a second office during the third quarter of 2009. At December 31, 2008, our Knoxville facility had recorded $318 million in loan balances and $226 million in deposit balances. At December 31, 2008, we employed 32 associates in the Knoxville MSA.

Results of Operations. Our net interest income increased to $114.2 million for 2008 compared to $75.7 million for 2007 compared to $61.0 million for 2006. The net interest margin (the ratio of net interest income to average earning assets) for 2008 was 3.17% compared to 3.55% for 2007 and 3.90% for the same period in 2006.

Our provision for loan losses was $11.2 million for 2008 compared to $4.7 million in 2007 and $3.7 million in 2006. The provision for loan losses increased primarily due to increases in loan volumes and charge-offs in each year when compared to the previous year. During 2008, our organic loan growth amounted to $605 million compared to organic loan growth of $349 million in 2007 and $300 million in 2006. Our net charge-offs were $3.2 million during 2008 compared $1.1 million in 2007 and $574,000 in 2006. The increased loan volumes and charge-offs in 2008 in comparison to 2007 and 2006 as well as an increase in the ratio of allowance for loan losses to total loans contributed to higher provision expense in 2008 compared to the previous periods.

Noninterest income for 2008 compared to 2007 increased by $12.2 million, or 54.2%. This increase is largely attributable to the fee businesses associated with the Mid-America acquisition, including deposit service charges, investment services, insurance sales and mortgage loan originations. Additionally, during 2008, we recorded approximately $1.0 million in gains on the sale of bank premises. Noninterest income for 2007 compared to 2006 increased by $6.73 million, or 42.7%, which was primarily due to the impact of the Cavalry and Mid-America acquisitions, increases in service charges on deposits, investment sales commissions, insurance commissions, trust and other fees.

Our continued growth in 2008 resulted in increased noninterest expense compared to 2007 due to the addition of Mid-America for a full year, our expansion into the Knoxville MSA, increases in salaries and employee benefits, equipment and occupancy expenses and other operating expenses. The number of full-time equivalent employees increased from 404.0 at December 31, 2006 to 702.0 at December 31, 2007 to 719.0 at December 31, 2008. As a result, we experienced increases in compensation and employee benefit expense. We expect to add additional employees throughout 2009 which will also cause our compensation and employee benefit expense to increase in 2009. Additionally, our branch expansion efforts during the last few years and the addition of new associates in 2009 will also increase noninterest expense. Our efficiency ratio (the ratio of noninterest expense to the sum of net interest income and noninterest income) was 63.4% in 2008 compared to 61.6% in 2007 and 60.8% in 2006. These calculations include the impact of approximately $7,116,000 in Mid-America merger-related charges in 2008 and $622,000 in 2007 and $1,636,000 in Cavalry merger related charges in 2006.

The effective income tax expense rate for 2008 was approximately 28.6% compared to an effective income tax expense rate for 2007 of approximately 30.2% and 32.1% for 2006. The decrease in the effective rate for the three year period was due to increased investment in bank qualified municipal securities, state tax credits, and increased tax savings from our captive insurance subsidiary, PNFP Insurance, Inc.

Net income available for common shareholders for 2008 was $30.6 million compared to $23.0 million in 2007, an increase of 32.7%. Net income available for common shareholders for 2007 was 28.5% higher than net income for 2006 of $17.9 million. Fully-diluted net income per common share available to common stockholders was $1.27 for 2008 compared to $1.34 for 2007 and $1.18 for 2006.

Excluding the after-tax (rate of 39.23%) impact of merger related charges in all three years, net income available for common shareholders for 2008 was $34.9 million compared to $23.4 million, an increase of 49.0%. Net income available for common shareholders for 2007 was 23.8% higher than the $18.9 million of net income available for common shareholders in 2006. As a result, adjusted diluted net income per common share available to common stockholders was $1.45 for 2008 compared to $1.36 for 2007, an increase of 6.6%. Also, adjusted diluted net income per common share available to common stockholders for 2007 was 8.8% higher than the $1.25 adjusted diluted net income per common share for 2006. For a reconciliation of these non-GAAP financial measures to their most directly comparable GAAP financial measure, see Reconciliation of Non-GAAP financial measures on page 32.

Financial Condition. Loans increased $605 million between December 31, 2008 and December 31, 2007, a growth rate of 22.0 percent. We believe our organic loan growth is attributable to hiring the best financial services associates in our markets. We hire experienced relationship managers that have significant client followings such that when they come to our firm, they are able to bring many of their existing clients with them. Loans increased $1.252 billion during 2007 of which $863 million was attributable to the Mid-America acquisition. Thus, the net increase in our loan portfolio attributable to organic growth during 2007 was $389 million, or 31.0%.

Deposits increased $608 million between December 31, 2008 and December 31, 2007, a growth rate of 20.8 percent. We grew deposits to $2.925 billion at December 31, 2007 compared to $1.622 billion at December 31, 2006, an increase of $1.303 billion, of which $954 million was attributable to the Mid-America acquisition. Excluding the Mid-America acquisition, we increased our deposits by $349 million.

Capital and Liquidity. At December 31, 2008 and 2007, our capital ratios, including our bank s capital ratios, met regulatory minimum capital requirements. Additionally, our bank would be considered to be well-capitalized pursuant to banking regulations at these dates. As we grow, Pinnacle National will require additional capital from us over that which can be earned through operations. We anticipate that we will continue to use various capital raising techniques in order to support the growth of Pinnacle National.

During 2008, we increased our capital accounts through our participation in the U.S. Department of Treasury s Capital Purchase Program (the CPP). As a result of our participation in the CPP, we issued 95,000 shares of preferred stock for $95 million. Additionally, we issued 534,910 common stock warrants to the U.S. Treasury as a condition to our participation in the CPP. The warrants have an exercise price of $26.64 each, are immediately exercisable and expire 10 years from the date of issuance. Based on a Black Scholes options pricing model, the common stock warrants have been assigned a fair value of $11.86 per warrant, or

$6.7 million in the aggregate, as of December 12, 2008. As a result, $6.7 million has been recorded as the discount on the preferred stock obtained above and will be accreted as a reduction in net income available for common stockholders over the next five years at approximately $1.1 million to $1.3 million per year. The resulting $88.3 million has been assigned to the Series A preferred stock and will be accreted up to the redemption amount of $95 million over the next five years.

Additionally, during 2008, we sold one million shares of our common stock for $21.5 million which also increased our capital accounts. In the past, we have been successful in procuring additional capital from the capital markets (via public and private offerings of trust preferred securities and common stock). This additional capital was required to support our growth. As of December 31, 2008, we believe we have access to sufficient capital to support our current growth plans. However, expansion by acquisition of other banks or by branching into a new geographic market could result in issuance of additional capital, including additional common shares.

Critical Accounting Estimates

The accounting principles we follow and our methods of applying these principles conform with U.S. generally accepted accounting principles and with general practices within the banking industry. In connection with the application of those principles, we have made judgments and estimates which, in the case of the determination of our allowance for loan losses and the assessment of impairment of the intangibles resulting from the Mid-America and Cavalry mergers have been critical to the determination of our financial position and results of operations.

Allowance for Loan Losses (allowance). Our management assesses the adequacy of the allowance prior to the end of each calendar quarter. This assessment includes procedures to estimate the allowance and test the adequacy and appropriateness of the resulting balance. The level of the allowance is based upon management s evaluation of the loan portfolios, past loan loss experience, current asset quality trends, known and inherent risks in the portfolio, adverse situations that may affect the borrower s ability to repay (including the timing of future payment), the estimated value of any underlying collateral, composition of the loan portfolio, economic conditions, industry and peer bank loan quality indications and other pertinent factors. This evaluation is inherently subjective as it requires material estimates including the amounts and timing of future cash flows expected to be received on impaired loans that may be susceptible to significant change. Loan losses are charged off when management believes that the full collectability of the loan is unlikely. A loan may be partially charged-off after a confirming event has occurred which serves to validate that full repayment pursuant to the terms of the loan is unlikely. Allocation of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management s judgment, is deemed to be uncollectible.

Larger balance commercial and commercial real estate loans are impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. Collection of all amounts due according to the contractual terms means that both the interest and principal payments of a loan will be collected as scheduled in the loan agreement.

An impairment allowance is recognized if the fair value of the loan is less than the recorded investment in the loan (recorded investment in the loan is the principal balance plus any accrued interest, net of deferred loan fees or costs and unamortized premium or discount). The impairment is recognized through the allowance. Loans that are impaired are recorded at the present value of expected future cash flows discounted at the loan s effective interest rate, or if the loan is collateral dependent, impairment measurement is based on the fair value of the collateral, less estimated disposal costs. Income is recognized on impaired loans on a cash basis.

The level of allowance maintained is believed by management to be adequate to absorb probable losses inherent in the portfolio at the balance sheet date. The allowance is increased by provisions charged to expense and decreased by charge-offs, net of recoveries of amounts previously charged-off.

In assessing the adequacy of the allowance, we also consider the results of our ongoing independent loan review process. We undertake this process both to ascertain whether there are loans in the portfolio whose credit quality has weakened over time and to assist in our overall evaluation of the risk characteristics of the entire loan portfolio. Our loan review process includes the judgment of management, the input from our independent loan reviewer, and reviews that may have been conducted by bank regulatory agencies as part of their usual examination process. We incorporate loan review results in the determination of whether or not it is probable that we will be able to collect all amounts due according to the contractual terms of a loan.

As part of management s quarterly assessment of the allowance, management divides the loan portfolio into four segments: commercial, commercial real estate, consumer and consumer real estate. Each segment is then analyzed such that an allocation of the allowance is estimated for each loan segment.

The allowance allocation for commercial and commercial real estate loans begins with a process of estimating the probable losses inherent for these types of loans. The estimates for these loans are established by category and based on our internal system of credit risk ratings and historical loss data for industry and various peer bank groups. The estimated loan loss allocation rate for our internal system of credit risk grades for commercial and commercial real estate loans is based on management s experience with similarly graded loans, discussions with banking regulators and our internal loan review processes. During the year ended December 31, 2008, we also performed a migration analysis of all loans that were charged-off during the previous two years. A migration analysis assists in evaluating loan loss allocation rates for the various risk grades assigned to loans in our portfolio. We incorporated the migration analysis along with other factors to determine the loss allocation rates for the commercial and commercial real estate portfolios. Subsequently, we weighted the allocation methodologies for the commercial and commercial real estate portfolios and determine a weighted average allocation for these portfolios.

The allowance allocation for consumer and consumer real estate loans which includes installment, home equity, consumer mortgages, automobiles and others is established for each of the categories by estimating probable losses inherent in that particular category of consumer and consumer real estate loans. The estimated loan loss allocation rate for each category is based on management s experience, consideration of our actual loss rates, industry loss rates and loss rates of various peer bank groups. Consumer and consumer real estate loans are evaluated as a group by category (i.e. retail real estate, installment, etc.) rather than on an individual loan basis because these loans are smaller and homogeneous. We weight the allocation methodologies for the consumer and consumer real estate portfolios and determine a weighted average allocation for these portfolios.

The estimated loan loss allocation for all four loan portfolio segments is then adjusted for management s estimate of probable losses for several environmental factors. The allocation for environmental factors is particularly subjective and does not lend itself to exact mathematical calculation. This amount represents estimated probable inherent credit losses which exist, but have not yet been identified, as of the balance sheet date, and are based upon quarterly trend assessments in delinquent and nonaccrual loans, unanticipated charge-offs, credit concentration changes, prevailing economic conditions, changes in lending personnel experience, changes in lending policies or procedures and other influencing factors. These environmental factors are considered for each of the four loan segments and the allowance allocation, as determined by the processes noted above for each component, is increased or decreased based on the incremental assessment of these various environmental factors.

The assessment also includes an unallocated component. We believe that the unallocated amount is warranted for inherent factors that cannot be practically assigned to individual loan categories. An example is the imprecision in the overall measurement process, in particular the volatility of the national and global economy.

We then test the resulting allowance by comparing the balance in the allowance to historical trends and industry and peer information. Our management then evaluates the result of the procedures performed, including the result of our testing, and concludes on the appropriateness of the balance of the allowance in its entirety. The audit committee of our board of directors reviews and approves the assessment prior to the filing of quarterly and annual financial information.

Impairment of Intangible Assets We recorded the assets and liabilities of Mid-America as of November 30, 2007 and Cavalry as of March 15, 2006, at estimated fair value. We engaged a third party to assist us in valuing certain financial assets and liabilities.

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

Goodwill and intangible assets that have indefinite useful lives are evaluated for impairment annually, and are evaluated for impairment more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset s fair value. The goodwill impairment analysis is a two-step test. The first step, used to identify potential impairment, involves comparing each reporting unit s estimated fair value to its carrying value, including goodwill. If the estimated fair value of a reporting unit exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value exceeds estimated fair value, there is an indication of potential impairment and the second step is performed to measure the amount of impairment.

If required, the second step involves calculating an implied fair value of goodwill for each reporting unit for which the first step indicated impairment. The implied fair value of goodwill is determined in a manner similar to the amount of goodwill calculated in a business combination, by measuring the excess of the estimated fair value of the reporting unit, as determined in the first step, over the aggregate estimated fair values of the individual assets, liabilities and identifiable intangibles as if the reporting unit was being acquired in a business combination. If the implied fair value of goodwill exceeds the carrying value of goodwill assigned to the reporting unit, there is no impairment. If the carrying value of goodwill assigned to a reporting unit exceeds the implied fair value of the goodwill, an impairment charge is recorded for the excess. An impairment loss cannot exceed the carrying value of goodwill assigned to a reporting unit, and the loss establishes a new basis in the goodwill. Subsequent reversal of goodwill impairment losses is not permitted.

Our stock price has historically traded above its book value and tangible book value and was trading above its book value and tangible book value as of December 31, 2008. In the event our stock price were to trade below its book value and tangible book value, we would perform our usual evaluation of the carrying value of goodwill as of the reporting date. Such a circumstance would be one factor in our evaluation that could result in an eventual goodwill impairment charge. Additionally, should our future earnings and cash flows decline and/or discount rates increase, an impairment charge to goodwill and other intangible assets may also be required.

We also engage a third party to test for impairment of our goodwill and intangible assets as of our annual assessment date, which is September 30. We reviewed their report as of September 30, 2008 and concluded that no indications of impairment were present. Should we determine in a future period that the goodwill recorded in connection with our acquisitions has been impaired, then a charge to our earnings will be recorded in the period such determination is made.

Results of Operations

Our results for fiscal years 2008, 2007 and 2006 were highlighted by the continued growth in loans and other earning assets and deposits, which resulted in increased revenues and expenses. The following is a summary of our results of operations (dollars in thousands):

	Years ended December 31,		*2008-2007 Percent Increase (Decrease)*	*Year ended December 31,*	*2007-2006 Percent Increase (Decrease)*
	2008	*2007*		*2006*	
Interest income	$206,082	$150,931	*36.5%*	$109,696	*37.6%*
Interest expense	91,867	75,219	*22.1%*	48,743	*54.3%*
Net interest income	114,215	75,712	*50.9%*	60,953	*24.2%*
Provision for loan losses	11,214	4,720	*137.6%*	3,732	*26.5%*
Net interest income after provision for loan losses	103,001	70,992	*45.1%*	57,221	*24.1%*
Noninterest income	34,718	22,521	*54.2%*	15,786	*42.7%*
Noninterest expense	94,478	60,480	*56.2%*	46,624	*29.7%*
Net income before income taxes	43,241	33,033	*30.9%*	26,383	*25.2%*
Income tax expense	12,367	9,992	*23.8%*	8,456	*18.2%*
Net income	30,874	23,041	*34.0%*	17,927	*28.5%*
	309	-	*NA*	-	*NA*

Preferred dividends and preferred stock discount accretion					
Net income available to common shareholders	$ 30,565	$ 23,041	*32.7%*	$ 17,927	*28.5%*
Basic income per common share available to common shareholders	*$ 1.34*	*$ 1.43*	*(6.3)%*	*$ 1.28*	*11.7%*
Diluted income per common share available to common shareholders	*$ 1.27*	*$ 1.34*	*(5.2)%*	*$ 1.18*	*13.6%*

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Our results for the years ended December 31, 2008 and 2007 included merger related expense. Excluding merger related expense from our net income resulted in diluted net income per common share available to common stockholders for the year ended December 31, 2008 of $1.45 and for the year ended December 31, 2007 of $1.36. A comparison of these amounts to prior years and a reconciliation of this non-GAAP financial measure follow (dollars in thousands):

Reconciliation of Non-GAAP financial measures:

	Year ended December 31, 2008	*Year ended December 31, 2007*	*2008-2007 Percent Increase (Decrease)*	*Year ended December 31, 2006*	*2007-2006 Percent Increase (Decrease)*
Net income available to common shareholders, as reported	$30,565	$23,041	*32.7%*	$17,927	*28.5%*
Merger related expense, net of tax	4,325	378	*1044.2%*	994	*(62.0)%*
Net income available to common shareholders excluding merger related expense	$34,890	$23,419	*49.0%*	$18,921	*23.8%*
Fully-diluted net income per common share available to common stockholders, as reported	*$ 1.27*	*$ 1.34*	*(5.2)%*	*$ 1.18*	*13.6%*
Fully-diluted net income per common share available to common stockholders, excluding merger related expense	*$ 1.45*	*$ 1.36*	*6.6%*	*$ 1.25*	*8.8%*

The presentation of this non-GAAP financial information is not intended to be considered in isolation or as a substitute for any measure prepared in accordance with GAAP. Because non-GAAP financial measures presented are not measurements determined in accordance with GAAP and are susceptible to varying calculations, these non-GAAP financial measures, as presented, may not be comparable to other similarly titled measures presented by other companies.

Pinnacle Financial believes that these non-GAAP financial measures excluding the impact of merger related expenses facilitate making period-to-period comparisons, and provide investors with additional information to evaluate our past financial results and ongoing operational performance.

Pinnacle Financial s management and board utilize this non-GAAP financial information to compare our operating performance versus the comparable periods in prior years and utilized non-GAAP diluted earnings per share for the 2008 and 2007 fiscal years (excluding the merger related expenses) in calculating whether or not we met the performance targets of our 2008 and 2007 Annual Cash Incentive Plans and our earnings per share targets in our restricted stock award agreements.

Net Interest Income. Net interest income represents the amount by which interest earned on various earning assets exceeds interest paid on deposits and other interest bearing liabilities and is the most significant component of our earnings. For the year ended December 31, 2008, we recorded net interest income of $114,215,000, which resulted in a net interest margin of 3.17% for the year. For the year ended December 31, 2007, we recorded net interest income of

$75,712,000, which resulted in a net interest margin of 3.55%. For the year ended December 31, 2006, we recorded net interest income of $60,953,000, which resulted in a net interest margin of 3.90%.

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The following table sets forth the amount of our average balances, interest income or interest expense for each category of interest-earning assets and interest-bearing liabilities and the average interest rate for total interest-earning assets and total interest-bearing liabilities, net interest spread and net interest margin for each of the years in the three-year period ended December 31, 2008 (dollars in thousands):

	2008			**2007**			**2006**		
	Average Balances	Interest	Rates/ Yields	Average Balances	Interest	Rates/ Yields	Average Balances	Interest	Rates/ Yields
Interest-earning assets:									
Loans (1)	$ 3,028,932	$ 175,128	5.78%	$ 1,723,361	$ 129,889	7.54%	$ 1,226,803	$ 92,006	7.50%
Securities:									
Taxable	448,229	23,432	5.23%	280,668	13,962	4.97%	254,906	12,615	4.95%
Tax-exempt (2)	135,011	5,399	5.27%	82,001	3,066	4.93%	54,270	2,016	4.90%
Federal funds sold and other	54,878	2,123	4.13%	72,344	4,014	5.57%	53,562	3,059	6.87%
Total interest-earning assets	3,667,050	206,082	5.67%	2,158,374	150,931	7.04%	1,589,541	109,696	6.95%
Nonearning assets									
Intangible assets	260,294			135,893			100,107		
Other nonearning assets	176,546			93,782			89,568		
Total assets	$ 4,103,890			$ 2,388,049			$ 1,779,216		
Interest-bearing liabilities:									
Interest-bearing deposits:									
Interest checking	$ 368,995	5,191	1.41%	$ 261,163	8,309	3.18%	$ 171,637	4,074	2.37%
Savings and money market	705,988	11,954	1.69%	535,468	17,618	3.29%	435,082	13,532	3.11%
Certificates of deposit	1,620,621	59,853	3.69%	727,724	35,745	4.91%	516,394	22,426	4.34%
Total deposits	2,695,604	76,998	2.86%	1,524,355	61,672	4.05%	1,123,113	40,032	3.56%
Securities sold under agreements to repurchase	196,601	2,667	1.36%	181,621	7,371	4.06%	101,144	4,329	4.28%
Federal Home Loan Bank advances and other borrowings	200,699	6,870	3.42%	44,072	2,211	5.02%	39,728	1,878	4.68%
Subordinated debt	88,223	5,332	6.04%	56,759	3,965	6.98%	37,372	2,504	6.70%
Total interest-bearing liabilities	3,181,127	91,867	2.89%	1,806,807	75,219	4.16%	1,301,357	48,743	3.75%
Noninterest-bearing deposits	404,718	-	-	291,983	-	-	259,585	-	-
Total deposits and interest-bearing liabilities	3,585,845	91,867	2.56%	2,098,790	75,219	3.58%	1,560,942	48,743	3.12%

Other liabilities	19,351			13,108			11,105		
Stockholders equity	498,694			276,151			207,169		
	$ 4,103,890			$ 2,388,049			$ 1,779,216		
Net interest income		$ 114,215			$ 75,712			$ 60,953	
Net interest spread (3)			2.78%			2.88%			3.20%
Net interest margin			3.17%			3.55%			3.90%

(1) Average balances of nonperforming loans are included in the above amounts.

(2) Yields based on the carrying value of those tax exempt instruments are shown on a fully tax equivalent basis.

(3) The net interest spread calculation excludes the impact of demand deposits. Had the impact of demand deposits been included, the net interest spread for the year ended December 31, 2008 would have been 3.11% compared to a net interest spread for the years ended December 31, 2007 and 2006 of 3.46% and 3.83%, respectively.

As noted above, the net interest margin for 2008 was 3.17% compared to a net interest margin of 3.55% in 2007. The reduction in the net interest margin was significant as the net decreases in the yield on interest-earning assets was 137 basis points compared to the decrease in the rate paid on total deposits and interest-bearing liabilities of only 102 basis points. The net interest margin for 2006 was 3.90%. Other matters related to the changes in net interest income, net interest yields and rates, and net interest margin between 2008 and 2007 are presented below:

Our loan yields decreased by 176 basis points between 2008 and 2007 while they increased by 4 basis points between 2006 and 2007. A significant amount of our loan portfolio has variable rate pricing with a large portion of these loans tied to our prime lending rate. Approximately 41.6% of our loan portfolio at December 31, 2008 was subject to a daily floating rate; thus these loans will reprice quickly in concert with the Federal Reserve s changes to its Federal funds rate. Our weighted average prime rate was 7.94% in 2006 and 7.52% in 2007 compared to 5.21% in 2008. Other factors that impact our loan yields in any period are our evaluation of the credit worthiness, collateral and other factors related to the borrower when we agree to make a loan, the term of the loan and the ongoing relationship we have with a particular borrower. The absolute level of nonaccrual loans during the year will also negatively impact loan yields as these loans serve to reduce the overall loan yield.

We have been able to grow our funding base significantly. For asset/liability management purposes, we elected to allocate a greater proportion of such funds to our loan portfolio versus our securities and shorter-term investment portfolio during the three year period noted above. For 2008, average loan balances were 83% of total interest-earning assets compared to 80% in 2007 and 77% in 2006. Loans generally have higher yields than do securities and other shorter-term investments although the difference between loan and securities yields was much less in 2008 compared to previous periods primarily due to the more significant decreases in short term rates (i.e., prime rate) to which loans are more directly correlated in comparison to the more modest decreases in longer term rates to which investments are more directly correlated.

During 2008, overall deposit rates were less than in 2007. Changes in interest rates paid on such products as interest checking, savings and money market accounts, securities sold under agreements to repurchase and Federal funds purchased will generally increase or decrease in a manner that is consistent with changes in the short-term rate environment. There was a significant decrease in the short-term rate environment during 2008 when compared to 2007. As a result, the rates for those products experienced a large decrease between the two periods. However, competitive deposit pricing pressures in our market limited our ability to reduce our funding costs more aggressively and negatively impacted our net interest margin. We routinely monitor the pricing of deposit products by our primary competitors. We believe that our markets are very competitive banking markets with several new market entrants seeking deposit growth. As a result, even though the short-term rate environment may allow for rate decreases in our short-term funding base, these decreases will be limited by competitive pressures. During 2007, overall deposit rates were higher than in 2006 primarily due to competitive pressures.

During 2008, the average balances of noninterest bearing deposit balances, interest bearing transaction accounts, savings and money market accounts and securities sold under agreements to repurchase amounted to 47% of our total funding compared to 61% in 2007 and 62% in 2006. The decrease in these products as a percentage of total funding is attributable to the competitiveness of these products among the local banking franchises and the significant growth we have experienced as we have elected to fund lending opportunities thru noncore sources. These funding sources generally have lower rates than do other funding sources, such as certificates of deposit and other borrowings. Additionally, noninterest bearing deposits comprised only 10% of total funding in 2008, compared to 12% in 2007 and 17% in 2006. Maintaining our noninterest bearing deposit balances in relation to total funding is critical to maintaining and growing our net interest margin. Management places a great deal of emphasis on this particular product.

Also impacting the net interest margin during 2008 was a higher amount of floating rate subordinated indebtedness outstanding. The average balances of subordinated indebtedness increased from $37 million in 2006 to $57 million in 2007 to $88 million in 2008. The interest rate charged on this indebtedness is generally higher than other funding sources. In October 2007, we issued an additional $30 million in floating rate subordinated indebtedness to largely fund the cash component of the Mid-America purchase price. The rate we are required to pay on this indebtedness is 285 points over three-month LIBOR. In August 2008, Pinnacle National issued $15 million in additional subordinated indebtedness at a rate of 350 points over three-month LIBOR. Proceeds from this issuance are expected to be used for the anticipated growth of Pinnacle Financial. These spreads are higher than the spreads associated with our other forms of subordinated indebtedness which were issued in previous periods.

During 2008, the yield curve steepened which is advantageous for most banks, including us, as we use a significant amount of short-term funding to fund our balance sheet growth. This short-term funding comes in the form of checking accounts, savings accounts, money market accounts, short-term time deposits and securities sold under agreements to repurchase. Rates paid on these short-term deposits generally correlate to the Federal funds rate and short term treasury rates. During most of 2007, the Federal funds rate was higher than other longer term treasuries (i.e., an inverted yield curve). As a result, for most of 2007, depositors tended to maintain their funds in shorter-term deposit accounts where they could achieve a higher yield on their deposit balances and did not concern themselves with long-term products because there was not enough yield for them to justify the longer maturity. In a more traditional rate environment, depositors typically would either accept a lesser rate for more liquid deposit accounts or choose a higher rate for a longer-term time deposit.

During the fourth quarter of 2008, the Federal Reserve, in response to increasing economic instability, reduced the targeted Federal funds rate such that the targeted rate at year end 2008 was less than 0.25%. This reduction together with previous Federal Reserve rate reductions in 2008 has facilitated the continual compression of our net interest margins as we experience reduced yields on a significant portion of our earning asset base and have not been able to counter this impact via reduced funding costs quickly.

Generally, we expect over an extended period of time to reduce our funding costs following a Federal Reserve rate reduction but competitive pricing pressures may limit the speed and the size of any such reductions. Traditionally, we maintain an asset sensitive balance sheet, thus when rates are stable to increasing our net interest margins should expand.

We believe we should be able to increase net interest income through overall growth in earning assets in 2009 compared to previous periods. The additional revenues provided by increased loan volumes should be sufficient to overcome any immediate increases in funding costs, and thus we should be able to increase our current net interest income. Our net interest margins will likely decrease during the early stages of 2009 due to continuing competitive deposit pricing in our markets. We have taken steps to counter the impact of these rate decreases on our floating rate assets (including prime rate loans) by reducing deposit rates to an appropriate level where we believe we can sustain our funding base. We believe it will take more time for our competition in our market to begin to price in the full impact of these rate decreases, and for competitive reasons, we will not be able to counter the full impact of these rate decreases during the early stages of 2009 but anticipate that should the rate environment stabilize we will be able to increase our margins during late first quarter and second quarter of 2009.

Rate and Volume Analysis. Net interest income increased by $38,503,000 between the years ended December 31, 2008 and 2007 and by $14,759,000 between the years ended December 31, 2007 and 2006. The following is an analysis of the changes in our net interest income comparing the changes attributable to rates and those attributable to volumes (dollars in thousands):

	2008 Compared to 2007 Increase (decrease) due to			***2007 Compared to 2006 Increase (decrease) due to***		
	Rate	***Volume***	***Net***	***Rate***	***Volume***	***Net***
Interest-earning assets:						
Loans	$(30,331)	$75,570	$45,239	$ 491	$37,392	$37,883
Securities:						
Taxable	730	8,740	9,470	51	1,296	1,347
Tax-exempt	279	2,054	2,333	16	1,034	1,050
Federal funds sold	(1,042)	(849)	(1,891)	(696)	1,651	955
Total interest-earning assets	(30,364)	85,515	55,151	(138)	41,373	41,235
Interest-bearing liabilities:						
Interest-bearing deposits:						
Interest checking	(4,623)	1,505	(3,118)	1,390	2,845	4,235
Savings and money market	(8,567)	2,903	(5,664)	783	3,303	4,086
Certificates of deposit	(8,878)	32,986	24,108	2,943	10,376	13,319
Total deposits	(22,068)	37,394	15,326	5,116	16,524	21,640
Securities sold under agreements to repurchase	(4,904)	200	(4,704)	(223)	3,265	3,042
Federal Home Loan Bank advances and other borrowings	(705)	5,364	4,659	135	198	333
Subordinated debt	(534)	1,901	1,367	105	1,356	1,461
Total interest-bearing liabilities	(28,211)	44,859	16,648	5,134	21,342	26,476

Net interest income	$ (2,153)	$40,656	$38,503	$(5,272)	$20,031	$14,759

Changes in net interest income are attributed to either changes in average balances (volume change) or changes in average rates (rate change) for earning assets and sources of funds on which interest is received or paid. Volume change is calculated as change in volume times the previous rate while rate change is change in rate times the previous volume. The change attributed to rates and volumes (change in rate times change in volume) is considered above as a change in volume.

Provision for Loan Losses. The provision for loan losses represents a charge to earnings necessary to establish an allowance for loan losses that, in our management s evaluation, should be adequate to provide coverage for the inherent losses on outstanding loans. The provision for loan losses amounted to $11,214,000, $4,720,000 and $3,732,000 for the years ended December 31, 2008, 2007 and 2006, respectively.

Based upon our evaluation of the loan portfolio, which is discussed more fully on page 44, we believe the allowance for loan losses to be adequate to absorb our estimate of probable losses existing in the loan portfolio at December 31, 2008. The impact of the Mid-America merger as well as the significant organic loan growth, increase in nonperforming loans and net-charge offs and an overall increase in our allowance for loan losses in relation to loan balances during 2008 were the primary reasons for the increase in the provision expense in 2008 when compared to 2007 with similar reasons for the increased provision expense in 2007 when compared to 2006.

Based upon management s assessment of the loan portfolio, we adjust our allowance for loan losses to an amount deemed appropriate to adequately cover probable losses in the loan portfolio. While our policies and procedures used to estimate the allowance for loan losses, as well as the resultant provision for loan losses charged to operations, are considered adequate by our management and are reviewed from time to time by our regulators, they are necessarily approximate and imprecise. There are factors beyond our control, such as conditions in the local and national economy, the local real estate market or particular industry conditions which may negatively impact, materially, our asset quality and the adequacy of our allowance for loan losses and, thus, the resulting provision for loan losses.

Noninterest Income. Our noninterest income is composed of several components, some of which vary significantly between quarterly and annual periods. Service charges on deposit accounts and other noninterest income generally reflect our growth, while investment services and fees from the origination of mortgage loans will often reflect market conditions and fluctuate from period to period. The opportunities for recognition of gains on loans and loan participations sold and gains on sales of investment securities may also vary widely from quarter to quarter and year to year. The Mid-America and Cavalry mergers also had a significant impact on the changes in noninterest income between the periods noted below.

The following is the makeup of our noninterest income for the years ended December 31, 2008, 2007 and 2006 (dollars in thousands):

	Years ended December 31,		***2008-2007 Percent Increase (Decrease)***	***Year ended December 31,***	***2007-2006 Percent Increase (Decrease)***
	2008	***2007***		***2006***	
Noninterest income:					
Service charges on deposit accounts	$10,735	$ 7,941	*35.2%*	$ 4,645	*71.0%*
Investment services	4,924	3,456	*42.5%*	2,463	*40.3%*
Insurance sales commissions	3,520	2,487	*41.5%*	2,123	*17.1%*
Gains on sales of loans and loan participations, net:					
Fees from the origination and sale of mortgage loans, net of sales commissions	3,074	1,619	*89.9%*	1,448	*11.8%*
Gains on loans and loan participations sold, net	970	239	*305.9%*	420	*(43.1)%*
Gain on sale of premises	1,030	75	*1273.3%*	-	*NA*
Trust fees	2,178	1,908	*14.2%*	1,181	*61.6%*
Other noninterest income:					
ATM and other consumer fees	4,043	2,822	*43.3%*	1,796	*57.1%*
Letters of credit fees	325	293	*10.9%*	506	*(42.1)%*
Bank-owned life insurance	869	631	*37.7%*	470	*34.3%*
Equity in earnings of Collateral Plus, LLC	95	274	*(65.3)%*	120	*128.3%*
Swap fees on customer loan transactions, net	892	95	*838.9%*	-	*NA*
Visa related gains	203	-	*NA*	-	*NA*
Loan late fees	980	345	*184.1%*	175	*97.1%*
Gain on sale of investment securities, net	-	16	*(100.0)%*	-	*NA*

Other noninterest income	880	320	*175.00%*	439	*(10.0)%*
Total noninterest income	$34,718	$22,521	*54.2%*	$15,786	*42.7%*

Service charge income for 2008 increased over that of 2007 due to the addition of the Mid-America customers including an increased number of customers utilizing overdraft protection products and an increased per item insufficient fund charge. Service charge income for 2007 increased over that of 2006 due to increased volumes from our Rutherford County market and an increase in the number of Nashville deposit accounts subject to service charges. Also the increase in service charges in 2008 when compared to 2007 was impacted by a decreased earnings credit rate provided by Pinnacle National to its commercial deposit customers. This earnings credit rate serves to reduce the deposit service charges for our commercial customers and is based on the average balances of their checking accounts at Pinnacle National.

Also included in noninterest income are commissions and fees from our financial advisory unit, Pinnacle Asset Management, a division of Pinnacle National. At December 31, 2008, Pinnacle Asset Management was receiving commissions and fees in connection with approximately $686 million in brokerage assets held with Raymond James Financial Services, Inc. compared to $878 million at December 31, 2007. Additionally, at December 31, 2008, our trust department was receiving fees on approximately $588 million in assets compared to $464 million at December 31, 2007. We increased the number of licensed brokers in Pinnacle Asset Management and in our trust area in 2008, and we anticipate continuing to increase our capacity in these areas in 2009. In 2008, we earned $3.5 million in insurance commissions compared to $2.5 million in 2007 and $2.1 million in 2006. Following our merger with Cavalry in March of 2006, we began to offer trust services through Pinnacle National s trust division and insurance services through Miller and Loughry Insurance Services, Inc. During the first three months of 2008, Miller Loughry Beach received approximately $450,000 in fees from one of its insurance carriers due to favorable claims experience by that carrier.

Additionally, fees from the origination and sale of mortgage loans also provided for a significant portion of the increase in noninterest income. These mortgage fees are for loans originated in both the middle Tennessee and Knoxville markets that are subsequently sold to third-party investors. All of these loan sales transfer servicing rights to the buyer. Generally, mortgage origination fees increase in lower interest rate environments and decrease in rising interest rate environments. As a result, mortgage origination fees may fluctuate greatly in response to a changing rate environment. Also, impacting mortgage origination fees are the number of mortgage originators we have offering these products. These originators are largely commission-based employees. The gross fees from the origination and sale of mortgage loans have been offset by the commission expense associated with these originations. We have steadily increased the number of originators working for us over the years and plan to continue to increase our mortgage origination work force in 2009.

We also sell certain commercial loan participations to our correspondent banks. Such sales are primarily related to new lending transactions in excess of internal loan limits or industry concentration limits. At December 31, 2008 and pursuant to participation agreements with these correspondents, we had participated approximately $125 million of originated commercial loans to these other banks compared to $110 million at December 31, 2007. These participation agreements have various provisions regarding collateral position, pricing and other matters. Many of these agreements provide that we pay the correspondent less than the loan s contracted interest rate. Pursuant to SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities a replacement of Financial Accounting Standards Board (FASB) Statement No. 125,* in those transactions whereby the correspondent is receiving a lesser amount of interest than the amount owed by the customer, we record a net gain along with a corresponding asset representing the present value of our net retained cash flows. The resulting asset is amortized over the term of the loan. Conversely, should a loan be paid prior to maturity, any remaining unamortized asset is charged as a reduction to gains on loan participations sold. We recorded gains, net of amortization expense related to the aforementioned retained cash flow asset, of $276,000, $239,000 and $420,000 during each of the years in the three-year period ended December 31, 2008 related to the loan participation transactions. Additionally, Pinnacle Financial recognized a gain of $695,000 during 2008 related to the sale of four related impaired loans to a group of outside investors. We intend to maintain relationships with our correspondents in order to sell participations in future loans to these or other correspondents primarily due to limitations on loans to a single borrower or industry concentrations. In general, the Mid-America and Cavalry mergers and the sale of common and preferred stock in 2008 have resulted in an increase in capital which has resulted in increased lending limits for such items as loans to a single borrower and loans to a single industry such that our need to participate such loans in the future may be reduced. In any event, the timing of participations may cause the level of gains, if any, to vary significantly.

During the second quarter of 2008 and as a result of our merger with Mid-America, we sold a legacy Pinnacle branch and a legacy Mid-America branch for a combined net gain of $1.0 million. These branch divestures were related to facilities only and did not include any financial assets or deposit accounts.

Included in other noninterest income are miscellaneous consumer fees, such as ATM revenues, merchant card and other electronic banking revenues. We experienced a significant increase in these revenues in 2008 compared to 2007 due primarily to the merger with Mid-America and increased volumes from new customers.

Also included in other noninterest income is $892,000 and $95,000 for the years ended December 31, 2008 and 2007, respectively, in fees we receive when we originate an interest rate swap transaction for an individual commercial borrower and a counterparty interest rate swap transaction with a third party provider. This amount will fluctuate significantly based on both borrower demand for this product and the interest rate environment. We also increased the value of our bank-owned life insurance $869,000 during 2008 when compared to the $631,000 during 2007 and $470,000 during 2006. This was due primarily to the purchase of $18 million in new bank owned life insurance policies during the fourth quarter of 2007. In connection with the Cavalry merger, we became the owner and beneficiary of several life insurance policies on former Cavalry directors and executives. These policies were acquired by Cavalry in connection with a supplemental retirement plan for these former Cavalry directors and executives.

At the end of 2004, we formed a wholly-owned subsidiary, Pinnacle Credit Enhancement Holdings, Inc. (PCEH). PCEH owns a 24.5% interest in Collateral Plus, LLC, which is accounted for under the equity method. Collateral Plus, LLC serves as an intermediary between investors and borrowers in certain financial transactions whereby the borrowers require enhanced collateral in the form of guarantees or letters of credit issued by the investors for the benefit of banks and other financial institutions. Our equity

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in the earnings of Collateral Plus, LLC for the years ended December 31, 2008, 2007 and 2006 was $95,000, $274,000 and $120,000, respectively.

Noninterest Expense. Noninterest expense consists of salaries and employee benefits, equipment and occupancy expenses, and other operating expenses. The following is the makeup of our noninterest expense for the years ended December 31, 2008, 2007 and 2006 (dollars in thousands):

	Years ended December 31,		*2008-2007*	*Year ended December 31,*	*2007-2006*
	2008	*2007*	*Percent Increase (Decrease)*	*2006*	*Percent Increase (Decrease)*
Noninterest expense:					
Salaries and employee benefits:					
Salaries	$32,391	$24,204	*33.8%*	$18,017	*34.3%*
Commissions	2,696	1,778	*51.6%*	1,298	*37.0%*
Other compensation, primarily incentives	2,421	2,602	*(7.0)%*	4,209	*(38.2)%*
Equity compensation expenses	2,347	2,100	*11.8%*	1,475	*42.4%*
Employee benefits and other	9,541	5,462	*74.7%*	2,470	*121.1%*
Total salaries and employee benefits	49,396	36,146	*36.7%*	27,469	*31.6%*
Equipment and occupancy	16,600	10,261	*61.8%*	7,522	*36.4%*
Other real estate	1,403	160	*776.9%*	-	*NA*
Marketing and business development	1,916	1,677	*14.3%*	1,234	*35.9%*
Postage and supplies	2,953	1,995	*48.0%*	1,510	*32.1%*
Amortization of core deposit intangible	3,101	2,144	*44.6%*	1,783	*20.2%*
Other noninterest expense:					
Professional fees	1,120	1,690	*(33.7)%*	1,135	*48.9%*
Legal, including borrower-related charges	1,216	437	*178.3%*	310	*41.0%*
OCC exam fees	509	365	*39.5%*	257	*42.0%*
Directors fees	530	233	*127.5%*	257	*(9.3)%*
Insurance, including FDIC assessments	3,039	1,278	*137.8%*	687	*86.0%*
Charitable contributions	465	334	*39.2%*	186	*79.6%*
Other noninterest expense	5,114	3,138	*63.0%*	2,638	*18.95%*
Total other noninterest expense	11,993	7,475	*60.4%*	5,470	*36.7%*
Merger related expense	7,116	622	*1044.1%*	1,636	*(62.0)%*
Total noninterest expense	$94,478	$60,480	*56.2%*	$46,624	*29.7%*

Expenses have generally increased between the above periods due to our mergers with Mid-America and Cavalry, personnel additions occurring throughout each period, the continued development of our branch network and other expenses which increase in relation to our growth rate. We anticipate continued increases in our expenses in the future for such items as additional personnel, the opening of additional branches, audit expenses and other expenses which tend to increase in relation to our growth. Equity compensation expense is related to stock options and restricted shares awarded to our associates. The expense in each year is awards that we have issued, but for which the forfeiture restrictions have not yet lapsed.

At December 31, 2008, we employed 719.0 full time equivalent employees compared to 702.0 at December 31, 2007 and 404.0 at the end of 2006. We intend to continue to add employees to our work force for the foreseeable future, which will cause our salary and employee benefits costs to increase in future periods.

We believe that variable pay incentives are a valuable tool in motivating an employee base that is focused on providing our clients effective financial advice and increasing shareholder value. As a result, and unlike many other financial institutions, all of our non-commissioned employees are eligible to participate in an annual cash incentive plan. Under the plan, the targeted level of incentive payments requires the Company to achieve a certain soundness threshold and a targeted earnings per share. To the extent that actual earnings per share are above or below targeted earnings per share, the aggregate incentive payments are increased or decreased. Additionally, our Human Resources and Compensation Committee (the Committee) of the Board of Directors has the ability to change the parameters of the variable cash award at any time prior to final distribution of the awards in order to take into account current events and circumstances and maximize the benefit of the awards to our firm and to the associates.

Included in the salary and employee benefits amounts for the years ended December 31, 2008, 2007 and 2006, were $1,706,000, $2,373,000 and $4,104,000, respectively, related to variable cash awards. This expense will fluctuate from year to year and quarter to quarter based on the estimation of achievement of performance targets and the increase in the number of associates eligible to receive the award. In 2008 and 2007, the Committee approved the payment of cash incentive awards under the 2008 and 2007 plans at a percentage that was generally higher than would have been otherwise payable under the terms of the plans. For 2008, qualifying associates received approximately 25% of their targeted award. Also in 2008, certain officers, including five executive officers, who did not receive a cash incentive award for the 2007 fiscal year received special cash incentive payments following the integration of the Mid-American bank subsidiaries with Pinnacle National. In 2007, and at their request, five of our executive officers (President and Chief Executive Officer, Chairman of the Board, Chief Administrative Officer, Chief Financial Officer and Chief Credit Officer), did not receive any cash incentive payments under our 2007 cash incentive plan in order for the associate base to be paid an increased amount. As a result, qualifying associates received approximately 50% of their targeted award. For 2006, the actual award to be paid to qualifying associates equaled 120% of their targeted award as our actual earnings for 2006 exceeded our 2006 earnings target under the 2006 plan, adjusted for the impact of the merger related expenses incurred in connection with the Cavalry acquisition.

The incentive plan for 2009 is structured similarly to prior year plans in that the award is based on the achievement of certain performance objectives. Because of the relative experience of our associates, our compensation costs are, and we expect will continue to be, higher on a per associate basis than other financial institutions of a similar asset size; however, we believe the experience and engagement of our associates also allows us to employ fewer people than most financial institutions our size.

In connection with our merger with Mid-America, all former associates of Mid-America that were displaced by our merger were granted a retention bonus award provided they worked through a predetermined date. Also, those associates that continued as Pinnacle Financial associates following the merger were eligible for a retention bonus should they continue their employment through December 31, 2008. This retention bonus award was paid to the former associates of Mid-America in January, 2009 and amounted to approximately $4.7 million. This award was treated as a merger related expense in 2008. As a result of these associates agreeing to a retention bonus award, they did not participate in any of our other cash or equity incentive award plans in 2008, but will participate in all such plans in 2009.

Equipment and occupancy expenses in 2008 were greater than in 2007 by $6.3 million and in 2007 these expenses were greater than the 2006 amount by $2.7 million. These increases are primarily attributable to our market expansion to Knoxville, Tennessee, our new branch facility in the Donelson area of Nashville which opened in the first quarter of 2007, expenses associated with the eleven Mid-America branches which were acquired on November 30, 2007 which represented a full year of expense in 2008 and expenses associated with the Cavalry merger which occurred in March of 2006. We have also increased our leased main office space during the three years ended December 31, 2008 and will move into a new leased office space in late 2009 or early 2010 that will be our headquarters. These additions contributed to the increase in our equipment and occupancy expenses throughout the three year period and will contribute to increases in expenses in the future as we construct new facilities, including new facilities currently planned in both the Nashville and Knoxville MSAs.

Marketing and other business development and postage and supplies expenses are higher in 2008 compared to 2007 and 2006 due to increases in the number of customers and prospective customers; increases in the number of customer contact personnel and the corresponding increases in customer entertainment; and other business development expenses. The addition of customers from the Mid-America and Cavalry mergers had a direct impact on these increased charges.

Included in noninterest expense for 2008, 2007 and 2006 is $3.1 million, $2.1 million and $1.8 million, respectively, of amortization of intangibles related primarily to the Mid-America and Cavalry mergers. For Mid-America, this identified intangible is being amortized over ten years using an accelerated method which anticipates the life of the underlying deposits to which the intangible is attributable. For Cavalry, this identified intangible is being amortized over seven years using an accelerated method which anticipates the life of the underlying deposits to which the intangible is attributable. Amortization expense associated with these core deposit intangibles will approximate

$2.4 million to $2.9 million per year for the next five years with lesser amounts for the remaining years. Additionally, in connection with our acquisition of Beach and Gentry in July of 2008, we recorded a customer list intangible of $1,270,000 which is being amortized over 20 years on an accelerated basis. Amortization of this intangible amounted to $60,000 during 2008.

Additionally, for the years ended December 31, 2008 and 2007, we incurred $7,116,000 and $622,000, respectively, of merger related expenses directly associated with the Mid-America merger. The merger related expenses consisted of integration costs incurred in connection with the merger, including approximately $4.7 million of retention bonuses for Mid-America associates, $999,000 in conversion-related incentive payments and other personnel costs, $826,000 in information technology conversion costs and $559,000 in other integration charges. We do not anticipate any additional merger related expenses associated with the Mid-America transaction in 2009. For the year ended December 31, 2006, we incurred $1,636,000 of merger related expenses directly

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associated with the Cavalry merger. The merger related charges consisted of integration costs incurred in connection with the merger, including accelerated depreciation associated with software and other technology assets whose useful lives were shortened as a result of the Cavalry acquisition.

Other noninterest expenses increased 60.4% in 2008 over 2007 and 36.7% in 2007 over 2006. Most of these increases are attributable to increased legal fees, insurance and other expenses which are incidental variable costs related to deposit gathering and lending. Examples include expenses related to ATM networks, correspondent bank service charges, check losses, appraisal expenses, closing attorney expenses and other items which have increased significantly as a result of the Mid-America merger.

Recently, the Federal Deposit Insurance Corporation (FDIC) finalized its deposit insurance assessment rates for 2009. As a result of the requirement to increase the FDIC s Bank Insurance Fund to statutory levels over a prescribed period of time and increased pressure on the fund s reserves due to the increasing number of bank failures, FDIC insurance costs for 2009 will be significantly higher for all insured depository institutions. We anticipate our insurance costs to increase 100% in 2009 as our deposit assessment rate will increase from approximately 5 basis points of our deposits to approximately 10 basis points.

Our efficiency ratio (ratio of noninterest expense to the sum of net interest income and noninterest income) was 63.4% in 2008 compared to 61.6% in 2007 and to 60.8% in 2006, including the merger related expenses associated with the Mid-America and Cavalry mergers. The efficiency ratio measures the amount of expense that is incurred to generate a dollar of revenue.

Income Taxes. The effective income tax expense rate for the year ended December 31, 2008 was approximately 28.6%, compared to an effective income tax expense rate for years ended December 31, 2007 and 2006 of approximately 30.2% and 32.1%, respectively. The decrease in the effective rate for 2008 compared to 2007 and 2006 was due to increased investment in bank qualified municipal securities, state tax credits, and increased tax savings from our captive insurance subsidiary, PNFP Insurance, Inc.

Preferred stock dividends and preferred stock discount accretion Reducing net income available for common shareholders is $264,000 of preferred stock dividends and $45,000 of accretion on preferred stock discount. On December 12, 2008, we received $95.0 million from the sale of preferred stock to the U.S. Treasury as a result of our participation in the CPP. The Series A preferred stock we sold the U.S. Treasury pays cumulative dividends quarterly at a rate of 5 percent per annum for the first five years and 9 percent thereafter.

Additionally, we issued 534,910 common stock warrants to the U.S. Treasury as a condition to our participation in the CPP. The warrants have an exercise price of $26.64 each, are immediately exercisable and expire 10 years from the date of issuance. Based on a Black Scholes options pricing model, the warrants have been assigned a fair value of $11.86 per warrant, or $6.7 million in the aggregate, as of December 12, 2008. As a result, the $6.7 million has been recorded as the discount on the preferred stock obtained above and will be accreted as a reduction in net income available for common shareholders over the next five years at approximately $1.1 million to $1.3 million per year.

Financial Condition

Our consolidated balance sheet at December 31, 2008 reflects significant growth since December 31, 2006. Total assets grew from $2.14 billion at December 31, 2006 to $3.79 billion at December 31, 2007 to $4.75 billion at December 31, 2008. Total deposits grew $608 million during 2008 and $1.30 billion during 2007. Excluding the deposits acquired with the Mid-America acquisition on November 30, 2007 of $957 million, total deposits increased by $346 million in 2007. We invested substantially all of the additional deposits and other fundings in loans, which grew by $605 million during 2008 and $1.25 billion (of which $865 million was acquired with the Mid-America acquisition) during 2007, and securities, which increased by $327 million in 2008 and $176 million in 2007 (of which $148 million was acquired with the Mid-America acquisition).

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Loans. The composition of loans at December 31st for each of the past five years and the percentage (%) of each classification to total loans are summarized as follows (dollars in thousands):

	2008		*2007*		*2006*		*2005*		*2004*	
	Amount	***Percent***	***Amount***	***Percent***	***Amount***	***Percent***	***Amount***	***Percent***	***Amount***	***P***
ercial real estate Mortgage	$ 963,530	28.7%	$ 710,546	25.9%	$ 284,302	19.0%	$148,102	22.9%	$117,123	
mer real estate Mortgage	675,606	20.1%	539,768	19.6%	299,627	20.0%	169,953	26.2%	126,907	
uction and land development	658,799	19.6%	582,959	21.2%	253,097	16.9%	67,667	10.4%	23,419	
ercial and industrial	966,563	28.8%	794,419	28.9%	608,530	40.6%	239,129	36.9%	189,456	
mer and other loans	90,409	2.8%	121,949	4.4%	52,179	3.5%	23,173	3.6%	15,457	
oans	$3,354,907	100.0%	$2,749,641	100.0%	$1,497,735	100.0%	$648,024	100.0%	$472,362	1

During the year ended December 31, 2007, our loan balances increased by $1.25 billion, or 83.6%. Approximately $865 million of this increase was due to the Mid-America acquisition while $387 million was attributable to organic growth. Our organic growth rate equates to approximately 26% for the year ended December 31, 2007. The Mid-America loan portfolio had a significant impact on our loan portfolio volumes as well as mix of loans as Mid-America had a larger percentage of commercial real estate loans in comparison to our loans.

Although the allocation of our loan portfolio did not change significantly between 2008 and 2007, we did experience an increase of 35.6% in the commercial real estate classification. We continue to have loan demand for our commercial real estate and construction lending products, and we will continue to pursue sound, prudently underwritten real estate lending opportunities. Because these types of loans require that we maintain effective credit and construction monitoring systems, we have increased our resources in this area. We believe we can effectively manage this area of exposure due to our strategic focus of hiring experienced professionals who are well-trained in this type of lending and who have significant experience in our geographic market. After the integration of the Mid-America loan portfolio in early 2008, certain loan balances previously reported at December 31, 2007 have been reclassified to be consistent with the December 31, 2008 classification.

During the year ended December 31, 2006, and primarily due to the Cavalry merger, we increased the percentage of our outstanding loans in construction and land development loans significantly. These types of loans require that we maintain effective credit and construction monitoring systems. Also as a result of the Cavalry merger, we also increased our resources in this area so that we can attempt to effectively manage this area of exposure through utilization of experienced professionals who are well-trained in this type of lending and who have significant experience in our geographic market.

We periodically analyze our commercial loan portfolio to determine if a concentration of credit risk exists to any one or more industries. We use broadly accepted industry classification systems in order to classify borrowers into various industry classifications. As a result, we have a credit exposure (loans outstanding plus unfunded commitments) exceeding 25% of Pinnacle National s total risk-based capital to borrowers in the following industries at December 31, 2008 and December 31, 2007 (dollars in thousands):

	At December 31, 2008		
	Outstanding Principal	***Unfunded***	***Total Exposure at December 31,***

	Balances	*Commitments*	*Total exposure*	*2007*
Lessors of nonresidential buildings	$338,616	$68,182	$406,798	$ 249,959
Lessors of residential buildings	138,352	20,909	159,261	135,413
Land subdividers	237,667	82,034	319,701	283,327
New housing operative builders	201,741	59,884	261,625	269,744
Trucking industry	76,419	23,234	99,653	109,118
New single family housing construction	45,038	12,980	58,018	104,980

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The following table classifies our fixed and variable rate loans at December 31, 2008 according to contractual maturities of (1) one year or less, (2) after one year through five years, and (3) after five years. The table also classifies our variable rate loans pursuant to the contractual repricing dates of the underlying loans (dollars in thousands):

	Amounts at December 31, 2008				
	Fixed Rates	***Variable Rates***	***Totals***	***At December 31, 2008***	***At December 31, 2007***
Based on contractual maturity:					
Due within one year	$ 251,279	$1,121,591	$1,372,870	*40.9%*	*44.5%*
Due in one year to five years	835,839	469,983	1,305,821	*38.9%*	*39.9%*
Due after five years	141,232	534,983	676,216	*20.2%*	*15.6%*
Totals	$1,228,350	$2,126,557	$3,354,907	*100.0%*	*100.0%*
Based on contractual repricing dates:					
Daily floating rate	$ -	$1,401,972	$1,401,972	*41.8%*	*40.0%*
Due within one year	251,279	597,339	848,617	*25.3%*	*21.2%*
Due in one year to five years	835,839	112,748	948,587	*28.3%*	*32.4%*
Due after five years	141,232	14,498	155,731	*4.6%*	*6.4%*
Totals	$1,228,350	$2,126,557	$3,354,907	*100.0%*	*100.0%*

The above information does not consider the impact of scheduled principal payments. Daily floating rate loans are tied to Pinnacle National s prime lending rate or a national interest rate index with the underlying loan rates changing in relation to changes in these

indexes.
Non-Performing Assets. The specific economic and credit risks associated with our loan portfolio include, but are not limited to, a general downturn in the economy which could affect employment rates in our market areas, general real estate market deterioration, interest rate fluctuations, deteriorated or non-existent collateral, title defects, inaccurate appraisals, financial deterioration of borrowers, fraud, and any violation of laws and regulations.
We attempt to reduce these economic and credit risks by adherence to loan to value guidelines for collateralized loans, by investigating the creditworthiness of the borrower and by monitoring the borrower s financial position. Also, we establish and periodically review our lending policies and procedures. Banking regulations limit our exposure by prohibiting loan relationships that exceed 15% of Pinnacle National s statutory capital in the case of loans that are not fully secured by readily marketable or other permissible types of collateral which would approximate $63.7 million. Furthermore, we have an internal limit for aggregate credit exposure (loans outstanding plus unfunded commitments) to a single borrower of $22 million. Our loan policy requires that our Executive Committee to the board of directors approve any relationships that exceed this internal limit.
At December 31, 2008 we had $29.2 million in nonperforming assets compared to $21.4 at December 31, 2007, a 36.6% increase. A significant contributor to this increase is a weaker housing sector. Although we believe the dislocations in the Nashville and Knoxville housing sectors have not been as severe as many other areas of our country, we have noted weakness with respect to several specific clients who focus on residential construction and residential land development within our trade areas.
The Greater Nashville Association of Realtors (GNAR) reported that the average median residential home price for the quarter ended December 31, 2008 was $163,800, a decrease of 13.2% from the same quarter in 2007. GNAR also reported that the number of residential inventory at December 31, 2008 was 12,900 homes, a decrease of 4.7% from a year earlier. These statistics represent a generally weaker housing market than a year earlier in that median home prices have fallen indicating that home values have decreased and although fewer homes for sale could be considered a positive in this market, it also represents that fewer home owners are willing to consider selling their home and subsequently acquiring another home.
An extended recessionary period will likely cause our construction and land development loans to underperform and our nonperforming assets and loan losses to increase. We believe our nonperforming asset levels will remain elevated for at least the next several quarters as we work diligently to remediate these assets.
We have enhanced our credit administration resources dedicated to the residential construction and residential development portfolios by assigning senior executives and bankers to these portfolios. These individuals meet frequently to discuss the performance of the portfolio and specific relationships with emphasis on the underperforming assets. Their objective is to identify relationships that warrant continued support and remediate those relationships that will tend to cause our portfolio to underperform

over the long term. We have reappraised many nonperforming assets to ascertain appropriate valuations, and we continue to systematically review these valuations as new data is received.

We discontinue the accrual of interest income when (1) there is a significant deterioration in the financial condition of the borrower and full repayment of principal and interest is not expected or (2) the principal or interest is more than 90 days past due, unless the loan is both well-secured and in the process of collection. At December 31, 2008, we had $10.9 million in loans on nonaccrual compared to $19.7 million at December 31, 2007, of which $5.1 million and $10.2 million, respectively, were residential construction and land development loans. The decrease in nonperforming loans between December 31, 2008 and December 31, 2007 was primarily related to the foreclosure of certain nonperforming loans and the subsequent transfer of those balances to other real estate owned.

At December 31, 2008, we owned $18.3 million in real estate which we had acquired, usually through foreclosure, from borrowers compared to $1.7 million at December 31, 2007. Substantially all of these amounts relate to new home construction and residential development projects that are either completed or are in various stages of construction for which we believe we have adequate collateral. Approximately 98.1% of these assets are located within the Nashville MSA.

There were $1.5 million of other loans 90 days past due and still accruing interest at December 31, 2008 compared to $1.61 million at December 31, 2007. At December 31, 2008 and 2007, no loans were deemed to be restructured loans.

The following table is a summary of our nonperforming assets at December 31st for each of the years in the five year period ended December 31, 2008 (dollars in thousands):

	At December 31,				
	2008	***2007***	***2006***	***2005***	***2004***
Nonaccrual loans (1)	$ 10,860	$ 19,677	$ 7,070	$ 460	$ 561
Restructured loans	-	-	-	-	-
Other real estate owned	18,306	1,673	995	-	-
Total nonperforming assets	29,166	21,350	8,065	460	561
Accruing loans past due 90 days or more	1,508	1,613	737	-	146
Total nonperforming assets and accruing loans past due 90 days or more	$ 30,674	$ 22,963	$ 8,802	$ 460	$ 707
Total loans outstanding	$3,354,907	$2,749,641	$1,497,735	$648,024	$472,362
Ratio of nonperforming assets and accruing loans past due 90 days or more to total loans outstanding at end of period	0.91%	0.84%	0.59%	0.07%	0.15%
Ratio of nonperforming assets and accruing loans past due 90 days or more to total allowance for loan losses at end of period	84.08%	80.66%	54.61%	5.85%	12.51%

(1) Interest income that would have been recorded in 2008 related to nonaccrual loans was $1,574,000 compared to $485,000 for the year ended December 31, 2007 and $283,000 for the year ended December 31, 2006, none of which is included in interest income or net income for the applicable periods.

At February 12, 2009, the nonperforming assets had increased to approximately $31.5 million. We anticipate that we will experience increased levels of nonperforming assets during 2009.

Potential Problem Loans. Potential problem loans, which are not included in nonperforming loans, amounted to approximately $27.8 million, or 0.83% of total loans outstanding at December 31, 2008, compared to $15.3 million, or 0.56% of total loans outstanding at December 31, 2007. Potential problem loans represent those loans with a well-defined weakness and where information about possible credit problems of borrowers has caused management to have serious doubts about the borrower s ability to comply with present repayment terms. This definition is believed to be substantially consistent with the standards established by the OCC, Pinnacle National s primary regulator, for loans classified as substandard, excluding the impact of nonperforming loans. At February 12, 2009, the potential problem loans had decreased slightly to approximately $26.7 million.

In addition to potential problem loans, criticized loans are those loans with above-average weakness as identified by our internal loan review processes. These are loans are in varying stages of review by our officers with the review objective being to determine whether there is well-defined weakness, which would require a downgrade to a potential problem loan or a nonperforming loan, or whether the credit weakness is stable or improving which would warrant a continued criticized loan grade or an upgrade to a passing credit grade. Typically, all criticized loans are performing loans and are thus not impaired. At December 31, 2008, approximately $78.4 million, or 2.34% of total loans outstanding were criticized loans. At February 12, 2009, criticized loans had increased to approximately $105.1 million due primarily to one loan that was downgraded subsequent to December 31, 2008.

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Allowance for Loan Losses (allowance). We maintain the allowance at a level that our management deems appropriate to adequately cover the probable losses inherent in the loan portfolio. As of December 31, 2008 and December 31, 2007, our allowance for loan losses was $36.5 million and $28.5 million, respectively, which our management deemed to be adequate at each of the respective dates. The judgments and estimates associated with our allowance determination are described under Critical Accounting Estimates above.

The following table sets forth, based on management s best estimate, the allocation of the allowance to types of loans as well as the unallocated portion as of December 31 for each of the past five years and the percentage of loans in each category to total loans (dollars in thousands):

	2008		***2007***		***2006***		***2005***		***2004***	
	Amount	***Percent***	***Amount***	***Percent***	***Amount***	***Percent***	***Amount***	***Percent***	***Amount***	***Percent***
Commercial real estate Mortgage	$11,523	28.7%	$ 8,068	25.9%	$ 4,550	19.0%	$1,488	22.9%	$1,205	24.8%
Consumer real estate Mortgage	5,149	20.1%	1,890	19.6%	913	20.0%	1,286	26.2%	869	26.9%
Construction and land development	7,899	19.6%	4,897	21.2%	2,869	16.9%	690	10.5%	227	5.0%
Commercial and industrial	9,966	28.8%	11,660	28.9%	6,517	40.6%	2,305	36.9%	1,711	40.0%
Consumer and other loans	1,372	2.8%	1,400	4.4%	870	3.5%	552	3.5%	396	3.3%
Unallocated	575	NA	555	NA	399	NA	1,537	NA	1,242	NA
Total allowance for loan losses	$36,484	100.0%	$28,470	100.0%	$16,118	100.0%	$7,858	100.0%	$5,650	100.0%

In periods prior to 2006, the unallocated portion of the allowance consisted of dollar amounts specifically set aside for certain general factors influencing the allowance. These factors included ratio trends and other factors not specifically allocated to each category. Establishing the percentages for these factors was largely subjective but was supported by economic data, changes made in lending functions, and other support where appropriate. In 2006, the unallocated portion decreased significantly, due to application of a more comprehensive and refined methodology to assess the adequacy of our allowance for loan losses. The methodology was refined to embed many of the factors previously included in the unallocated portion of the allowance to the allocated amounts above for each category. This enhancement established a methodology whereby national and economic factors, concentrations in market segments, loan review and portfolio performance could be assigned to these specific categories.

The following is a summary of changes in the allowance for loan losses for each of the years in the five year period ended December 31, 2008 and the ratio of the allowance for loan losses to total loans as of the end of each period (dollars in thousands):

	For the year ended December 31,				
	2008	***2007***	***2006***	***2005***	***2004***
Balance at beginning of period	$28,470	$16,118	$ 7,858	$5,650	$ 3,719
Provision for loan losses	11,214	4,720	3,732	2,152	2,948
Allowance from Mid-America (2007) and Cavalry (2006) acquisitions	-	8,695	5,102	-	-
Charged-off loans:					
Commercial real estate Mortgage	(62)	(22)	-	-	-
Consumer real estate Mortgage	(1,144)	(364)	(46)	(38)	(834)

Construction and land development	(2,172)	(271)	-	-	-
Commercial and industrial	(773)	(326)	(436)	(61)	(50)
Consumer and other loans	(982)	(359)	(336)	(109)	(148)
Total charged-off loans	(5,133)	(1,342)	(818)	(208)	(1,032)
Recoveries of previously charged-off loans:					
Commercial real estate Mortgage	731	-	-	-	-
Consumer real estate Mortgage	3	125	-	231	-
Construction and land development	55	1	-	-	2
Commercial and industrial	844	51	166	3	-
Consumer and other loans	300	102	78	30	13
Total recoveries of previously charged-off loans	1,933	279	244	264	15
Net (charge-offs) recoveries	(3,200)	(1,063)	(574)	56	(1,017)
Balance at end of period	$36,484	$28,470	$16,118	$7,858	$ 5,650
Ratio of allowance for loan losses to total loans outstanding at end of period	1.09%	1.04%	1.08%	1.21%	1.20%
Ratio of net charge-offs (recoveries) to average loans outstanding for the period	0.11%	0.06%	0.05%	(0.01)%	0.27%

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As noted in our critical accounting policies, management assesses the adequacy of the allowance prior to the end of each calendar quarter. This assessment includes procedures to estimate the allowance and test the adequacy and appropriateness of the resulting balance. The level of the allowance is based upon management s evaluation of the loan portfolios, past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower s ability to repay (including the timing of future payments), the estimated value of any underlying collateral, composition of the loan portfolio, economic conditions, industry and peer bank loan quality indications and other pertinent factors. This evaluation is inherently subjective as it requires material estimates including the amounts and timing of future cash flows expected to be received on impaired loans that may be susceptible to significant change. The allowance increased by $8.0 million between December 31, 2008 and December 31, 2007 and the ratio of our allowance for loan losses to total loans outstanding increased to 1.09% at December 31, 2008 from 1.04% at December 31, 2007.

Investments. Our investment portfolio, consisting primarily of Federal agency bonds, state and municipal securities and mortgage-backed securities, amounted to $849.8 million and $522.7 million at December 31, 2008 and 2007, respectively. Our investment portfolio serves many purposes including serving as a stable source of income, collateral for public funds and as a potential liquidity source.

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The following table shows the carrying value of investment securities according to contractual maturity classifications of (1) one year or less, (2) after one year through five years, (3) after five years through ten years, and (4) after ten years. Actual maturities may differ from contractual maturities of mortgage-backed securities because the mortgages underlying the securities may be called or prepaid with or without penalty. Therefore, these securities are not included in the maturity categories but are listed below these categories as of December 31, 2008 and 2007 (dollars in thousands):

					At December 31,					
	U.S. Treasury securities		*U.S. government agency securities*		*State and Municipal securities*		*Corporate securities*		*Totals*	
	Amount	*Yield*	*Amount*	*Yield*	*Amount*	*Yield*	*Amount*	*Yield*	*Amount*	*Yield*
At December 31, 2008:										
Securities available-for-sale:										
Due in one year or less	$-	-%	$ 7,499	4.0%	$ 606	3.8%	$ 859	3.5%	$ 8,964	3.9%
Due in one year to five years	-	-%	6,611	4.4%	12,882	3.5%	-	-%	19,493	3.8%
Due in five years to ten years	-	-%	26,008	5.2%	56,143	3.9%	522	4.1%	82,673	4.3%
Due after ten years	-	-%	24,305	5.6%	65,194	4.3%	243	5.3%	89,742	4.7%
	$-	-%	$64,423	5.1%	$134,825	4.0%	$1,624	3.9%	200,872	4.4%
Mortgage-backed securities									638,357	5.6%
Total available-for-sale securities									$839,229	5.3%
Securities held-to-maturity:										
Due in one year or less	$-	-%	$ -	-%	$ 481	3.2%	$ -	-%	$ 481	3.2%
Due in one year to five years	-	-%	1,998	4.2%	6,497	3.5%	-	-%	8,495	3.8%
Due in five years to ten years	-	-%	-	4.8%	1,575	3.9%	-	-%	1,575	3.9%
Due after ten years	-	-%	-	-%	-	-%	-	-%	-	-%
	$-	-%	$ 1,998	4.3%	$ 8,553	3.5%	$ -	-%	10,551	3.8%
Mortgage-backed securities									-	-%
Total held-for-sale securities									$ 10,551	3.8%
At December 31, 2007:										
Securities available-for-sale:										
Due in one year or less	$-	-%	$16,612	4.3%	$ 12,463	5.2%	$ 490	3.4%	$ 29,565	4.7%
Due in one year to five years	-	-%	43,097	4.5%	27,089	5.3%	1,488	3.9%	71,674	4.8%
Due in five years to ten years	-	-%	6,774	5.1%	45,545	5.6%	-	5.2%	52,319	5.5%
Due after ten years	-	-%	3,180	4.9%	40,809	5.6%	400	5.4%	44,389	5.5%
	$-	-%	$69,663	4.5%	$125,906	5.5%	$2,378	5.2%	197,947	5.2%

Mortgage-backed securities									297,705	4.9%
Total available-for-sale securities									$495,652	5.0%
Securities held-to-maturity:										
Due in one year or less	$-	-%	$ -	-%	$ 1,578	5.0%	$ -	-%	$ 1,578	5.0%
Due in one year to five years	-	-%	15,750	4.2%	6,786	4.4%	-	-%	22,536	4.3%
Due in five years to ten years	-	-%	1,997	4.8%	922	5.0%	-	-%	2,919	4.8%
Due after ten years	-	-%	-	-%	-	-%	-	-%	-	-%
	$-	-%	$17,747	4.3%	$ 9,286	4.6%	$ -	-%	27,033	4.4%
Mortgage-backed securities									-	-%
Total held-for-sale securities									$ 27,033	4.4%

We computed yields using coupon interest, adding discount accretion or subtracting premium amortization, as appropriate, on a ratable basis over the life of each security. We computed the weighted average yield for each maturity range using the acquisition price of each security in that range.

Deposits and Other Borrowings. We had approximately $3.53 billion of deposits at December 31, 2008 compared to $2.93 billion at December 31, 2007. Our deposits consist of noninterest and interest-bearing demand accounts, savings accounts, money market accounts and time deposits. Additionally, we entered into agreements with certain customers to sell certain of our securities under agreements to repurchase the security the following day. These agreements (which are typically associated with comprehensive treasury management programs for our commercial clients and provide the client with short-term returns for their excess funds) amounted to $184.3 million at December 31, 2008 and $156.1 million at December 31, 2007. Additionally, at December 31, 2008, we had borrowed $183.3 million in advances from the Federal Home Loan Bank of Cincinnati compared to $92.8 million at December 31, 2007.

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Generally, banks classify their funding base as either core funding or non-core funding. Core funding consists of all deposits other than time deposits issued in denominations of $100,000 or greater. All other funding is deemed to be non-core. The following table represents the balances of our deposits and other fundings and the percentage of each type to the total at December 31, 2008 and December 31, 2007 (dollars in thousands):

	December 31, 2008	*Percent*	*December 31, 2007*	*Percent*
Core funding:				
Noninterest-bearing deposit accounts	$ 424,757	*10.4%*	$ 400,120	*12.1%*
Interest-bearing demand accounts	375,993	*9.2%*	410,661	*12.4%*
Savings and money market accounts	694,582	*17.0%*	742,354	*22.5%*
Time deposit accounts less than $100,000	570,443	*13.9%*	371,881	*11.2%*
Total core funding	2,065,775	*50.5%*	1,925,016	*58.2%*
Non-core funding:				
Time deposit accounts greater than $100,000				
Public funds	538,809	*13.2%*	104,902	*3.2%*
Brokered deposits	585,599	*14.3%*	163,188	*4.9%*
Other time deposits	343,062	*8.4%*	732,213	*22.2%*
Securities sold under agreements to repurchase	184,298	*4.5%*	156,071	*4.7%*
Federal Home Loan Bank advances and other borrowings	273,609	*6.7%*	141,666	*4.3%*
Subordinated debt Pinnacle National	15,000	*0.4%*	-	-
Subordinated debt Pinnacle Financial	82,476	*2.0%*	82,476	*2.5%*
Total non-core funding	2,022,853	*49.5%*	1,380,516	*41.8%*
Totals	$4,088,628	*100.0%*	$3,305,532	*100.0%*

Our funding policies limit the amount of non-core funding we can use to support our growth. As noted in the table above, our core funding decreased from 58.2% at December 31, 2007 to 50.5% at December 31, 2008. Although growing our core deposit base is a key strategic objective of our firm, we believe that our dependence on non-core funding will increase, but remain within our policies, as we continue to fund the rapid growth of our loan portfolio. The amount of time deposits as of December 31, 2008 amounted to $2.0 billion. The following table shows our time deposits in denominations of under $100,000 and those of denominations of $100,000 and greater by category based on time remaining until maturity of (1) three months or less, (2) over three but less than six months, (3) over six but less than twelve months and (4) over twelve months and the weighted average rate for each category (dollars in thousands):

	Balances	***Weighted Avg. Rate***
Denominations less than $100,000		
Three months or less	$ 264,267	2.87%
Over three but less than six months	96,944	3.04%
Over six but less than twelve months	151,157	3.49%
Over twelve months	58,075	3.89%

	570,443	3.17%
Denomination $100,000 and greater		
Three months or less	625,066	2.23%
Over three but less than six months	281,961	3.42%
Over six but less than twelve months	397,448	3.77%
Over twelve months	162,996	4.15%
	1,467,471	3.09%
Totals	$2,037,914	3.11%

Subordinated debt. On December 29, 2003, we established PNFP Statutory Trust I; on September 15, 2005 we established PNFP Statutory Trust II; on September 7, 2006 we established PNFP Statutory Trust III and on October 31, 2007 we established PNFP Statutory Trust IV (Trust I ; Trust II ; Trust III , Trust IV or collectively, the Trusts). All are wholly-owned Pinnacle Financial subsidiaries that are statutory business trusts. We are the sole sponsor of the Trusts and acquired each Trust s common securities for $310,000; $619,000; $619,000; and $928,000, respectively. The Trusts were created for the exclusive purpose of issuing 30-year capital trust preferred securities (Trust Preferred Securities) in the aggregate amount of $10,000,000 for Trust I; $20,000,000 for Trust II; $20,000,000 for Trust III; and $30,000,000 for Trust IV and using the proceeds to acquire junior subordinated debentures (Subordinated Debentures) issued by Pinnacle Financial. The sole assets of the Trusts are the

Subordinated Debentures. At December 31, 2008, our $2,476,000 investment in the Trusts is included in investments in unconsolidated subsidiaries in the accompanying consolidated balance sheets and our $82,476,000 obligation is reflected as subordinated debt.

The Trust I Preferred Securities bear a floating interest rate based on a spread over 3-month LIBOR (4.30% at December 31, 2008) which is set each quarter and matures on December 30, 2033. The Trust II Preferred Securities bear a fixed interest rate of 5.848% per annum through September 30, 2010 at which time the securities will bear a floating rate set each quarter based on a spread over 3-month LIBOR. The Trust II securities mature on September 30, 2035. The Trust III Preferred Securities bear a floating interest rate based on a spread over 3-month LIBOR (3.11% at December 31, 2008) which is set each quarter and mature on September 30, 2036. The Trust IV Preferred Securities bear a floating interest rate based on a spread over 3-month LIBOR (4.35% at December 31, 2008) which is set each quarter and mature on September 30, 2037.

Distributions are payable quarterly. The Trust Preferred Securities are subject to mandatory redemption upon repayment of the Subordinated Debentures at their stated maturity date or their earlier redemption in an amount equal to their liquidation amount plus accumulated and unpaid distributions to the date of redemption. We guarantee the payment of distributions and payments for redemption or liquidation of the Trust Preferred Securities to the extent of funds held by the Trusts. Pinnacle Financial s obligations under the Subordinated Debentures together with the guarantee and other back-up obligations, in the aggregate, constitute a full and unconditional guarantee by Pinnacle Financial of the obligations of the Trusts under the Trust Preferred Securities.

The Subordinated Debentures are unsecured; bear interest at a rate equal to the rates paid by the Trusts on the Trust Preferred Securities and mature on the same dates as those noted above for the Trust Preferred Securities. Interest is payable quarterly. We may defer the payment of interest at any time for a period not exceeding 20 consecutive quarters provided that the deferral period does not extend past the stated maturity. During any such deferral period, distributions on the Trust Preferred Securities will also be deferred and our ability to pay dividends on our common shares will be restricted.

Subject to approval by the Federal Reserve Bank of Atlanta and the limitations on repurchase resulting from Pinnacle Financial s participation in the CPP, the Trust Preferred Securities may be redeemed subject to the limitations imposed under the CPP prior to maturity at our option on or after September 17, 2008 for Trust I; on or after September 30, 2010 for Trust II; September 30, 2011 for Trust III and September 30, 2012 for Trust IV. The Trust Preferred Securities may also be redeemed at any time in whole (but not in part) in the event of unfavorable changes in laws or regulations that result in (1) the Trust becoming subject to federal income tax on income received on the Subordinated Debentures, (2) interest payable by the parent company on the Subordinated Debentures becoming non-deductible for federal tax purposes, (3) the requirement for the Trust to register under the Investment Company Act of 1940, as amended, or (4) loss of the ability to treat the Trust Preferred Securities as Tier I capital under the Federal Reserve capital adequacy guidelines.

The Trust Preferred Securities for the Trusts qualify as Tier I capital under current regulatory definitions subject to certain limitations. Debt issuance costs associated with Trust I of $120,000 consisting primarily of underwriting discounts and professional fees are included in other assets in the accompanying consolidated balance sheet. These debt issuance costs are being amortized over ten years using the straight-line method. There were no debt issuance costs associated with Trust II, Trust III or Trust IV.

On August 5, 2008, Pinnacle National entered into a $15 million subordinated term loan with a regional bank. The loan bears interest at three month LIBOR plus 3.5%, matures in 2015 and qualifies as 100% Tier 2 capital for regulatory capital purposes until 2010 and at a decreasing percentage each year thereafter. This additional bank level capital will be utilized to support our anticipated growth.

Holding Company Line of Credit. On February 28, 2008, we entered into a loan agreement for a $25 million line of credit with a regional bank. This line of credit has been used to support the growth of Pinnacle National. The balance owed pursuant to this line of credit at December 31, 2008 was $18 million and is included in other investments on the accompanying balance sheet. The $25 million line of credit has a one year term which matures on February 26, 2009, and contained customary affirmative and negative covenants regarding the operations of our business, a negative pledge on the common stock of Pinnacle National and is priced at 30-day LIBOR plus 125 basis points. We anticipate this line of credit will be renewed at substantially the same terms and conditions.

Capital Resources. At December 31, 2008 and 2007, our stockholders equity amounted to $627.3 million and $466.6 million, respectively. This increase was primarily attributable to receipt of $95.0 million from the sale of preferred stock to the U.S. Treasury as a result of our participation in the CPP and $38.4 million in comprehensive income, which was composed of $30.6 million in net income together with $7.8 million of net unrealized holding gains associated with our available-for-sale portfolio.

Additionally, during the third quarter of 2008, we received $21.5 million in proceeds from the sale of our common stock . The 2007 increase of $210.6 million was primarily attributable to $183.5 million of common stock issued in connection with the Mid-America acquisition and $24.3 million in comprehensive income, which was composed of $23.0 million in net income and $1.3 million of net unrealized holding gains associated with our available-for-sale portfolio.

During the third quarter of 2008, we sold one million shares of common stock via a private placement to mutual funds and certain other institutional accounts managed by T. Rowe Price Associates, Inc. at $21.50 per share. Proceeds from this sale of common stock are expected to be used for general corporate purposes, including supporting the continued, anticipated growth of Pinnacle National.

On December 12, 2008, we issued 95,000 shares of preferred stock to the U.S. Treasury for $95 million pursuant to the CPP. Additionally, we issued 534,910 common stock warrants to the U.S. Treasury as a condition to our participation in the CPP. The warrants have an exercise price of $26.64 each, are immediately exercisable and expire 10 years from the date of issuance. In addition to the accrued dividend costs and the accretion of the discount recorded on the preferred stock, which totaled $309,000 during the year ended December 31, 2008, we also accrued $237,000 in franchise tax expense which will be paid to the State of Tennessee as a result of the additional capital acquired through the CPP. Proceeds from this sale of preferred stock are expected to be used for general corporate purposes, including supporting the continued, anticipated growth of Pinnacle National.

The Series A preferred stock sold pursuant to the CPP is non-voting, other than having class voting rights on certain matters, and pays cumulative dividends quarterly at a rate of 5 percent per annum for the first five years and 9 percent thereafter. The preferred shares are only redeemable at our option under certain circumstances during the first three years and are redeemable thereafter without restriction. As a result of our participation in the CPP, our capital ratios have been further enhanced.

At December 31, 2008, our Tier 1 risk-based capital ratio was 12.1 percent, our total risk-based capital was 13.5 percent and our leverage ratio was 10.5 percent, compared to 9.6 percent, 10.5 percent and 8.7 percent at December 31, 2007, respectively.

Dividends. Pinnacle National is subject to restrictions on the payment of dividends to Pinnacle Financial under federal banking laws and the regulations of the Office of the Comptroller of the Currency. During the year ended December 31, 2008, Pinnacle National paid $5.0 million in dividends to Pinnacle Financial. Pinnacle Financial is subject to limits on payment of dividends to its shareholders by the rules, regulations and policies of Federal banking authorities, the laws of the State of Tennessee and as a result of its participation in the CPP (as more fully discussed above). Pinnacle Financial has not paid any dividends to date, nor does it anticipate paying dividends to its shareholders for the foreseeable future. Future dividend policy will depend on Pinnacle Financial s earnings, capital position, financial condition and other factors.

Market and Liquidity Risk Management

Our objective is to manage assets and liabilities to provide a satisfactory, consistent level of profitability within the framework of established liquidity, loan, investment, borrowing, and capital policies. Our Asset Liability Management Committee (ALCO) is charged with the responsibility of monitoring these policies, which are designed to ensure acceptable composition of asset/liability mix. Two critical areas of focus for ALCO are interest rate sensitivity and liquidity risk management.

Interest Rate Sensitivity. In the normal course of business, we are exposed to market risk arising from fluctuations in interest rates. ALCO measures and evaluates the interest rate risk so that we can meet customer demands for various types of loans and deposits. ALCO determines the most appropriate amounts of on-balance sheet and off-balance sheet items. Measurements which we use to help us manage interest rate sensitivity include an earnings simulation model and an economic value of equity model. These measurements are used in conjunction with competitive pricing analysis.

Earnings simulation model. We believe that interest rate risk is best measured by our earnings simulation modeling. Forecasted levels of earning assets, interest-bearing liabilities, and off-balance sheet financial instruments are combined with ALCO forecasts of interest rates for the next 12 months and are combined with other factors in order to produce various earnings simulations. To limit interest rate risk, we have guidelines for our earnings at risk which seek to limit the variance of net interest income to less than a 20 percent decline for a gradual 300 basis point change up or down in rates from management s flat interest rate forecast over the next twelve months; to less than a 10 percent decline for a gradual 200 basis point change up or down in rates from management s flat interest rate forecast over the next twelve months; and to less than a 5 percent decline for a gradual 100 basis point change up or down in rates from management s flat interest rate forecast over the next twelve months.

Economic value of equity. Our economic value of equity model measures the extent that estimated economic values of our assets, liabilities and off-balance sheet items will change as a result of interest rate changes. Economic values are determined by discounting expected cash flows from assets, liabilities and off-balance sheet items, which establishes a base case economic value of equity. To help limit interest rate risk, we have a guideline stating that for an instantaneous 300 basis point change in interest rates up or down, the economic value of equity should not decrease by more than 30 percent from the base case; for a 200 basis point instantaneous change in interest rates up or down, the economic value of equity should not decrease by more than 20 percent; and for a 100 basis point instantaneous change in interest rates up or down, the economic value of equity should not decrease by more than 10 percent.

At December 31, 2008, our model results indicated that we remain asset-sensitive. Asset sensitivity implies that our assets will reprice faster than our liabilities. As a result, an interest rate increase would be beneficial to us as our asset yields would increase at a more rapid rate than the costs of our liabilities. This asset sensitivity is primarily attributable to the absolute low level of rates in the current economic cycle. Our deposit rates are difficult to lower as we have achieved, for many deposit products, embedded floors, which basically means that we either are near a zero interest level or competitive pressures do not allow for any meaningful decreases. Due to rate conditions, during 2008, we periodically operated outside of our guidelines for interest rate sensitivity and economic value of equity on a few of the rates down interest rate scenarios.

Each of the above analyses may not, on its own, be an accurate indicator of how our net interest income will be affected by changes in interest rates. Income associated with interest-earning assets and costs associated with interest-bearing liabilities may not be affected uniformly by changes in interest rates. In addition, the magnitude and duration of changes in interest rates may have a significant impact on net interest income. For example, although certain assets and liabilities may have similar maturities or periods of repricing, they may react in different degrees to changes in market interest rates. Interest rates on certain types of assets and liabilities fluctuate in advance of changes in general market rates, while interest rates on other types may lag behind changes in general market rates. In addition, certain assets, such as adjustable rate mortgage loans, have features (generally referred to as interest rate caps and floors) which limit changes in interest rates. Prepayment and early withdrawal levels also could deviate significantly from those assumed in calculating the maturity of certain instruments. The ability of many borrowers to service their debts also may decrease during periods of rising interest rates. ALCO reviews each of the above interest rate sensitivity analyses along with several different interest rate scenarios as part of its responsibility to provide a satisfactory, consistent level of profitability within the framework of established liquidity, loan, investment, borrowing, and capital policies.

We may also use derivative financial instruments to improve the balance between interest-sensitive assets and interest-sensitive liabilities and as one tool to manage our interest rate sensitivity while continuing to meet the credit and deposit needs of our customers. Beginning in 2007, we entered into interest rate swaps (swaps) to facilitate customer transactions and meet their financing needs. These swaps qualify as derivatives, but are not designated as hedging instruments. At December 31, 2008 and 2007, we had not entered into any derivative contracts to assist managing our interest rate sensitivity.

Liquidity Risk Management. The purpose of liquidity risk management is to ensure that there are sufficient cash flows to satisfy loan demand, deposit withdrawals, and our other needs. Traditional sources of liquidity for a bank include asset maturities and growth in core deposits. A bank may achieve its desired liquidity objectives from the management of its assets and liabilities and by internally generated funding through its operations. Funds invested in marketable instruments that can be readily sold and the continuous maturing of other earning assets are sources of liquidity from an asset perspective. The liability base provides sources of liquidity through attraction of increased deposits and borrowing funds from various other institutions.

Changes in interest rates also affect our liquidity position. We currently price deposits in response to market rates and our management intends to continue this policy. If deposits are not priced in response to market rates, a loss of deposits could occur which would negatively affect our liquidity position.

Scheduled loan payments are a relatively stable source of funds, but loan payoffs and deposit flows fluctuate significantly, being influenced by interest rates, general economic conditions and competition. Additionally, debt security investments are subject to prepayment and call provisions that could accelerate their payoff prior to stated maturity. We attempt to price our deposit products to meet our asset/liability objectives consistent with local market conditions. Our ALCO is responsible for monitoring our ongoing liquidity needs. Our regulators also monitor our liquidity and capital resources on a periodic basis.

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In addition, Pinnacle National is a member of the Federal Home Loan Bank of Cincinnati (FHLB). As a result, Pinnacle National receives advances from the FHLB, pursuant to the terms of various borrowing agreements, which assist it in the funding of its home mortgage and commercial real estate loan portfolios. Under the borrowing agreements with the Federal Home Loan Bank of Cincinnati, Pinnacle National has pledged certain qualifying residential mortgage loans and, pursuant to a blanket lien, all qualifying commercial mortgage loans as collateral. At December 31, 2008, Pinnacle National had received advances from the Federal Home Loan Bank of Cincinnati totaling $184.0 million at the following rates and maturities (dollars in thousands):

	Scheduled Maturities	*Weighted Average Interest Rates*
2009	$ 15,144	5.01%
2010	57,248	3.55%
2011	83	0.00%
2012	30,085	3.51%
2013	20,066	2.67%
Thereafter	61,340	2.93%
	$ 183,966	
Weighted average interest rate		*3.36%*

Pinnacle National also has accommodations with upstream correspondent banks for unsecured short-term advances. These accommodations have various covenants related to their term and availability, and in most cases must be repaid within less than a month. Although there were no amounts outstanding at December 31, 2008, for the year ended December 31, 2008, we averaged borrowings from correspondent banks of $25.8 million under such agreements.

At December 31, 2008, brokered certificates of deposit approximated $585.6 million which represented 14.3% of total fundings compared to $163.2 million and 4.9% at December 31, 2007. We issue these brokered certificates through several different brokerage houses based on competitive bid. Typically, these funds are for varying maturities up to two years and are issued at rates which are competitive to rates we would be required to pay to attract similar deposits from the local market as well as rates for Federal Home Loan Bank of Cincinnati advances of similar maturities. We consider these deposits to be a ready source of liquidity under current market conditions.

Our short-term borrowings (borrowings which mature within the next fiscal year) consist primarily of securities sold under agreements to repurchase (these agreements are typically associated with comprehensive treasury management programs for our clients and provide them with short-term returns on their excess funds), Federal Home Loan Bank of Cincinnati advances and Federal funds purchased. Information concerning our short-term borrowings as of and for each of the years in the three-year period ended December 31, 2008 is as follows (dollars in thousands):

	2008	*2007*	*2006*
Amounts outstanding at year-end:			
Securities sold under agreements to repurchase	$184,298	$156,071	$141,016
Federal funds purchased	71,643	39,862	-
Holding Company line of credit	18,000	9,000	-
Federal Home Loan Bank advances	15,000	92,804	25,000
Weighted average interest rates at year-end:			
Securities sold under agreements to repurchase	0.38%	2.81%	4.33%
Federal funds purchased	0.68%	3.75%	-
Holding Company line of credit	1.71%	6.25%	-
Federal Home Loan Bank advances	5.01%	4.26%	5.36%
Maximum amount of borrowings at any month-end:			
Securities sold under agreements to repurchase	$256,472	$216,321	$166,520
Federal funds purchased	81,545	39,862	9,985
Holding Company line of credit	18,000	9,000	-
Federal Home Loan Bank advances	92,804	92,804	25,000
Average balances for the year:			
Securities sold under agreements to repurchase	$196,601	$181,621	$101,144
Federal funds purchased	25,835	5,544	1,260
Holding Company line of credit	13,525	750	-
Federal Home Loan Bank advances	40,561	38,528	6,284
Weighted average interest rates for the year:			
Securities sold under agreements to repurchase	1.36%	4.06%	4.28%
Federal funds purchased	2.47%	5.15%	5.26%
Holding Company line of credit	4.19%	6.25%	-
Federal Home Loan Bank advances	4.31%	4.97%	4.70%

At December 31, 2008, we had no significant commitments for capital expenditures. However, we are in the process of developing our branch network and other office facilities in the Nashville MSA and the Knoxville MSA. As a result, we anticipate that we will enter into contracts to buy property or construct branch facilities and/or lease agreements to lease facilities in the Nashville MSA and Knoxville MSA, including entering into an agreement to relocate our downtown office facility in Nashville, Tennessee to a new facility projected to open in early 2010.

The following table presents additional information about our contractual obligations as of December 31, 2008, which by their terms have contractual maturity and termination dates subsequent to December 31, 2008 (dollars in thousands):

	Next 12 months	*13-36 months*	*37-60 months*	*More than 60 months*	*Totals*

Contractual obligations:					
Certificates of deposit	$1,816,844	$211,214	$ 9,703	$ 153	$2,037,914
Securities sold under agreements to repurchase	184,298	-	-	-	184,298
Federal Home Loan Bank advances	15,000	57,149	50,000	61,817	183,966
Line of credit	18,000	-	-	-	18,000
Federal funds purchased	71,643	-	-	-	71,643
Subordinated debt	-	-	-	97,476	97,476
Minimum operating lease commitments	2,055	5,163	5,433	25,915	38,566
Totals	$2,107,840	$273,526	$65,136	$185,361	$2,631,863

Our management believes that we have adequate liquidity to meet all known contractual obligations and unfunded commitments, including loan commitments and reasonable borrower, depositor, and creditor requirements over the next twelve months.

Off-Balance Sheet Arrangements. At December 31, 2008, we had outstanding standby letters of credit of $86 million and unfunded loan commitments outstanding of $1.01 billion. Because these commitments generally have fixed expiration dates and many will expire without being drawn upon, the total commitment level does not necessarily represent future cash requirements. If needed to fund these outstanding commitments, Pinnacle National has the ability to liquidate Federal funds sold or securities available-for-sale, or on a short-term basis to borrow and purchase Federal funds from other financial institutions. The following table presents additional information about our unfunded commitments as of December 31, 2008, which by their terms have contractual maturity dates subsequent to December 31, 2008 (dollars in thousands):

	Next 12 months	*13-36 months*	*37-60 months*	*More than 60 months*	*Totals*
Unfunded commitments:					
Lines of credit	$644,033	$129,592	$67,343	$169,385	$1,010,353
Letters of credit	78,272	6,453	1,250	-	85,975
Totals	$722,305	$136,045	$68,593	$169,385	$1,096,328

Impact of Inflation

The consolidated financial statements and related consolidated financial data presented herein have been prepared in accordance with U.S. generally accepted accounting principles and practices within the banking industry which require the measurement of financial position and operating results in terms of historical dollars without considering the changes in the relative purchasing power of money over time due to inflation. Unlike most industrial companies, virtually all the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates have a more significant impact on a financial institution s performance than the effects of general levels of inflation.

Recently Adopted Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements SFAS No. 157, which defines fair value, establishes a framework for measuring fair value in U.S. generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 applies only to fair-value measurements that are already required or permitted by other accounting standards and is expected to increase the consistency of those measurements. The definition of fair value focuses on the exit price, (i.e., the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date), not the entry price, (i.e., the price that would be paid to acquire the asset or received to assume the liability at the measurement date). The statement emphasizes that fair value is a market-based measurement; not an entity-specific measurement. Therefore, the fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. The effective date for SFAS No. 157 was for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Pinnacle Financial adopted SFAS No. 157 effective January 1, 2008.

In February of 2007, the FASB issued Statement of Financial Accounting Standard No. 159 (SFAS 159), The Fair Value Option for Financial Assets and Financial Liabilities , which gives entities the option to measure eligible financial assets, and financial liabilities at fair value on an instrument by instrument basis, that are otherwise not permitted to be accounted for at fair value under other accounting standards. The election to use the fair value option is available when an entity first recognizes a financial asset or financial liability. Subsequent changes in fair value must be recorded in earnings. This statement was effective as of January 1, 2008; however, it had no impact on the consolidated financial statements of Pinnacle Financial because it did not elect the fair value option for any financial instrument not presently being accounted for at fair value.

In June 2006, the Emerging Issues Task Force issued EITF No. 06-4, Accounting for Deferred Compensation and Postretirement Benefits Aspects of Endorsement Split-Dollar Life Insurance Arrangements. The EITF concluded that deferred compensation or postretirement benefit aspects of an endorsement split-dollar life insurance arrangement should be recognized as a liability by the employer and the obligation is not effectively settled by the purchase of a life insurance policy. The effective date is for fiscal years beginning after December 15, 2007. On January 1, 2008, we accounted for this EITF as a change in accounting principle and recorded a liability of $985,000 along with a corresponding adjustment of $598,700 to beginning retained earnings, net of tax.

In December 2007, the SEC issued SAB 110, Share-Based Payment. SAB 110 allows eligible public companies to continue to use a simplified method for estimating the expense of stock options if their own historical experience isn t sufficient to provide a reasonable basis. Under SAB 107, Share-Based Payment, the simplified method was scheduled to expire for all grants made after

December 31, 2007. The SAB describes disclosures that should be provided if a company is using the simplified method for all or a portion of its stock option grants beyond December 31, 2007. The provisions of this bulletin were effective on January 1, 2008. Pinnacle Financial continues to use the simplified method allowed by SAB 110 for determining the expected term component for share options granted during 2008.

In October 2008, the FASB issued FSP No. FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active. This FSP clarifies the application of SFAS No. 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. This FSP was effective for the Company upon issuance, including prior periods for which financial statements have not been issued; and, therefore was effective for the Company s financial statements as of and for the year ended December 31, 2008. Adoption of FSP No. FAS 157-3 did not have a significant impact on the Company s financial position or results of operations.

Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS 141R, Business Combinations. SFAS 141R clarifies the definitions of both a business combination and a business. All business combinations will be accounted for under the acquisition method (previously referred to as the purchase method). This standard defines the acquisition date as the only relevant date for recognition and measurement of the fair value of consideration paid. SFAS 141R requires the acquirer to expense all acquisition related costs. SFAS 141R will also require acquired loans to be recorded net of the allowance for loan losses on the date of acquisition. SFAS 141R defines the measurement period as the time after the acquisition date during which the acquirer may make adjustments to the provisional amounts recognized at the acquisition date. This period cannot exceed one year, and any subsequent adjustments made to provisional amounts are done retrospectively and restate prior period data. The provisions of this statement are effective for business combinations during fiscal years beginning after December 15, 2008. Pinnacle Financial has not determined the impact that SFAS 141R will have on its financial position and results of operations and believes that such determination will not be meaningful until Pinnacle Financial enters into a business combination.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in consolidated financial statements An Amendment of ARB No. 51. SFAS No. 160 requires noncontrolling interests to be treated as a separate component of equity, not as a liability or other item outside of equity. Disclosure requirements include net income and comprehensive income to be displayed for both the controlling and noncontrolling interests and a separate schedule that shows the effects of any transactions with the noncontrolling interests on the equity attributable to the controlling interest. The provisions of this statement are effective for fiscal years beginning after December 15, 2008. This statement should be applied prospectively except for the presentation and disclosure requirements which shall be applied retrospectively for all periods presented. Pinnacle Financial does not expect the impact of SFAS No. 160 on its financial position, results of operations or cash flows to be material.

In March 2008, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 161 (SFAS 161), Disclosures about Derivative Instruments and Hedging Activities . SFAS 161 requires companies with derivative instruments to disclose information that should enable financial-statement users to understand how and why a company uses derivative instruments, how derivative instruments and related hedged items are accounted for under FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities, and how derivative instruments and related hedged items affect a company s financial position, financial performance and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. We are currently evaluating the impact, if any, that SFAS 161 will have on our consolidated financial statements.

In April 2008, the FASB issued FASB Staff Position (FSP) No. 142-3, Determination of the Useful Life of Intangible Assets . FSP 142-3 amends the factors an entity should consider in developing renewal or extension assumptions used in determining the useful life of recognized intangible assets under FASB Statement No. 142, Goodwill and Other Intangible Assets . This new guidance applies prospectively to intangible assets that are acquired individually or with a group of other assets in business combinations and asset acquisitions. FSP 142-3 is effective for financial statements issued for fiscal years and interim periods beginning after December 15, 2008. Early adoption is prohibited. We are currently evaluating the impact, if any, that FSP 142-3 will have on our consolidated financial statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The response to this Item is included in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, on pages 50 through 54 and is incorporated herein by reference.

ITEM 8. FINANCIAL STATEMENTS

Pinnacle Financial Partners, Inc. and Subsidiaries
Consolidated Financial Statements
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MANAGEMENT REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Pinnacle Financial Partners, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting. Pinnacle Financial Partners, Inc. s internal control system was designed to provide reasonable assurance to the Company s management and board of directors regarding the preparation and fair presentation of published financial statements. All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Pinnacle Financial Partners, Inc. s management assessed the effectiveness of the Company s internal control over financial reporting as of December 31, 2008. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework.

Based on our assessment we believe that, as of December 31, 2008, the Company s internal control over financial reporting is effective based on those criteria.

Pinnacle Financial Partners, Inc. s independent registered public accounting firm has issued an audit report on Pinnacle Financial Partners Inc. s internal control over financial reporting. This report appears on page 58 of this Annual Report on Form 10-K.

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Pinnacle Financial Partners, Inc.:

We have audited the accompanying consolidated balance sheets of Pinnacle Financial Partners, Inc. and subsidiaries (the Company) as of December 31, 2008 and 2007, and the related consolidated statements of income, stockholders equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

As discussed in note 14 to the consolidated financial statements, the Company changed its method of accounting for split dollar life insurance arrangements as required by EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefits Aspects of Endorsement Split-Dollar Life Insurance Arrangements* in 2008.

As discussed in notes 1 and 11 to the consolidated financial statements, the Company changed its method of accounting for uncertainty in income taxes as required by FASB Interpretation No.48, *Accounting for Uncertainty in Income Taxes* in 2007.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company s internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 19, 2009 expressed, an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

(signed) KPMG LLP

Nashville, Tennessee
February 19, 2009

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Pinnacle Financial Partners, Inc.:

We have audited Pinnacle Financial Partners, Inc. s (the Company) internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company and subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of income, stockholders equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2008, and our report dated February 19, 2009 expressed an unqualified opinion on those consolidated financial statements.

(signed) KPMG LLP

Nashville, Tennessee
February 19, 2009

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PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	December 31, 2008	December 31, 2007
ASSETS		
Cash and noninterest-bearing due from banks	$ 68,388,961	$ 76,941,931
Interest-bearing due from banks	8,869,680	24,706,966
Federal funds sold	12,994,114	20,854,966
Cash and cash equivalents	90,252,755	122,503,863
Securities available-for-sale, at fair value	839,229,428	495,651,939
Securities held-to-maturity (fair value of $10,642,973 and $26,883,473 at December 31, 2008 and December 31, 2007, respectively)	10,551,256	27,033,356
Mortgage loans held-for-sale	25,476,788	11,251,652
Loans	3,354,907,269	2,749,640,689
Less allowance for loan losses	(36,484,073)	(28,470,207)
Loans, net	3,318,423,196	2,721,170,482
Premises and equipment, net	68,865,221	68,385,946
Other investments	33,616,450	22,636,029
Accrued interest receivable	17,565,141	18,383,004
Goodwill	244,160,624	243,573,636
Core deposit and other intangible assets	16,871,202	17,325,988
Other assets	89,062,703	46,254,566
Total assets	$4,754,074,764	$3,794,170,461
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits:		
Non-interest-bearing	$ 424,756,813	$ 400,120,147
Interest-bearing	375,992,912	410,661,187
Savings and money market accounts	694,582,319	742,354,465
Time	2,037,914,307	1,372,183,317
Total deposits	3,533,246,351	2,925,319,116
Securities sold under agreements to repurchase	184,297,793	156,070,830
Federal Home Loan Bank advances and other borrowings	201,966,181	101,804,133
Federal Funds purchased	71,643,000	39,862,000
Subordinated debt	97,476,000	82,476,000

Accrued interest payable	8,326,264	10,374,538
Other liabilities	29,820,779	11,653,550
Total liabilities	4,126,776,368	3,327,560,167
Stockholders equity:		
Preferred stock, no par value; 10,000,000 shares authorized; 95,000 shares issued and outstanding at December 31, 2008, and no shares issued and outstanding at December 31, 2007	88,348,647	-
Common stock, par value $1.00; 90,000,000 shares authorized; 23,762,124 issued and outstanding at December 31, 2008 and 22,264,817 issued and outstanding at December 31, 2007	23,762,124	22,264,817
Common stock warrants	6,696,804	-
Additional paid-in capital	417,040,974	390,977,308
Retained earnings	84,380,447	54,150,679
Accumulated other comprehensive income (loss), net of taxes	7,069,400	(782,510)
Total stockholders equity	627,298,396	466,610,294
Total liabilities and stockholders equity	$4,754,074,764	$3,794,170,461

See accompanying notes to consolidated financial statements.

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PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

	For the years ended December 31,		
	2008	**2007**	**2006**
Interest income:			
Loans, including fees	$ 175,128,097	$ 129,888,784	$ 92,005,602
Securities:			
Taxable	23,431,746	13,961,714	12,614,623
Tax-exempt	5,399,312	3,066,519	2,016,044
Federal funds sold and other	2,122,343	4,014,424	3,059,750
Total interest income	206,081,498	150,931,441	109,696,019
Interest expense:			
Deposits	76,998,042	61,671,734	40,032,020
Securities sold under agreements to repurchase	2,666,760	7,371,490	4,329,327
Federal Home Loan Bank advances and other borrowings	12,201,797	6,176,205	4,381,878
Total interest expense	91,866,599	75,219,429	48,743,225
Net interest income	114,214,899	75,712,012	60,952,794
Provision for loan losses	11,213,543	4,719,841	3,732,032
Net interest income after provision for loan losses	103,001,356	70,992,171	57,220,762
Noninterest income:			
Service charges on deposit accounts	10,735,080	7,941,029	4,645,685
Investment services	4,923,840	3,455,808	2,463,205
Insurance sales commissions	3,520,205	2,486,884	2,122,702
Gains on loan sales, net	4,044,441	1,858,077	1,868,184
Net gain on sale of premises	1,030,231	75,337	-
Trust fees	2,178,112	1,908,440	1,180,839
Gains on sales of investment securities, net	-	16,472	-
Other noninterest income	8,286,458	4,778,880	3,505,903
Total noninterest income	34,718,367	22,520,927	15,786,518
Noninterest expense:			
Salaries and employee benefits	49,396,022	36,145,588	27,469,275
Equipment and occupancy	16,600,272	10,260,915	7,521,602
Other real estate owned	1,403,022	160,367	-
Marketing and other business development	1,915,747	1,676,455	1,234,497
Postage and supplies	2,953,013	1,995,267	1,510,048
Amortization of intangibles	3,100,599	2,144,018	1,783,230

Merger related expense	7,116,770	621,883	1,635,831
Other noninterest expense	11,993,345	7,475,072	5,469,777
Total noninterest expense	94,478,790	60,479,565	46,624,260
Income before income taxes	43,240,933	33,033,533	26,383,020
Income tax expense	12,367,015	9,992,178	8,455,987
Net income	30,873,918	23,041,355	17,927,033
Preferred stock dividends	263,889	-	-
Accretion on preferred stock discount	45,451	-	-
Net income available to common stockholders	$ 30,564,578	$ 23,041,355	$ 17,927,033
Per share information:			
Basic net income per common share available to common stockholders	$ 1.34	$ 1.43	$ 1.28
Diluted net income per common share available to common stockholders	$ 1.27	$ 1.34	$ 1.18
Weighted average common shares outstanding:			
Basic	22,793,699	16,100,076	13,954,077
Diluted	24,053,972	17,255,543	15,156,837

See accompanying notes to consolidated financial statements.

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PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY
AND COMPREHENSIVE INCOME (LOSS)

For the each of the years in the three-year period ended December 31, 2008

	Preferred Stock Amount	Common Stock Shares	Common Stock Amount	Common Stock Warrants	Additional Paid-in Capital	Unearned Compensation	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Tot Stockho Equ
ces, ber 31,	**-**	**8,426,551**	**$ 8,426,551**	**-**	**$ 44,890,912**	**$ (169,689)**	**$ 13,182,291**	**$ (2,893,640)**	**$ 63,43**
er of ed nsation to nal paid-in upon on of SFAS	-	-	-	-	(169,689)	169,689	-	-	
se of yee ve on stock , common varrants ated tax s	-	141,168	141,168	-	1,284,724	-	-	-	1,42
ce of ed on shares nt to 2004 Incentive	-	22,057	22,057	-	(22,057)	-	-	-	
nsation e for ed shares	-	-	-	-	465,003	-	-	-	46
nsation e for stock .	-	-	-	-	1,009,958	-	-	-	1,00
r with y Bancorp,	-	6,856,298	6,856,298	-	164,231,274	-	-	-	171,08
o register on stock in	-	-	-	-	(187,609)	-	-	-	(18

tion with rger with y Bancorp,									
ehensive :									
ome	-	-	-	-	-	-	17,927,033	-	17,92
realized g gains on le-for-sale es, net of d tax e of 86	-	-	-	-	-	-	-	852,747	85
ehensive :									18,77
es, ber 31,	-	15,446,074	$ 15,446,074	-	$ 11,502,516	$ -	$ 31,109,324	$ (2,040,893)	$ 256,01
se of vee ve on stock , stock ation nd related efits	-	99,862	99,862	-	883,429	-	-	-	98
ce of ed on shares nt to 2004 Incentive	-	42,301	42,301	-	(42,301)	-	-	-	
nsation e for ed shares	-	-	-	-	396,378	-	-	-	39
nsation e for stock .	-	-	-	-	1,703,441	-	-	-	1,70
r with merica ares, Inc.	-	6,676,580	6,676,580	-	176,833,242	-	-	-	183,50
o register	-	-	-	-	(299,397)	-	-	-	(29
on stock in tion with rger with									

merica ares, Inc. ehensive :									
ome	-	-	-	-	-	-	23,041,355	-	23,04
realized g gains on le-for-sale es, net of d tax e of 56	-	-	-	-	-	-	-	1,258,383	1,25
ehensive :									24,29
es, ber 31,	-	22,264,817	$ 22,264,817	-	$ 390,977,308	$ -	$ 54,150,679	$ (782,510)	$ 466,61
ative effect ge in ting le due to on of EITF et of tax	-	-	-	-	-	-	(598,699)	-	(59
ds from common ess g expenses 242)	-	1,000,000	1,000,000	-	20,454,758	-	-	-	21,45
ce of shares of ed stock 4,910 on stock ts, net of es	$ 88,303,196	-	-	$ 6,696,804	(62,065)	-	-	-	94,93
on on ed stock nt	45,451	-	-	-	-	-	(45,451)	-	
se of ree on stock , stock ation common varrants ated tax	-	314,434	314,434	-	3,516,569	-	-	-	3,83

s ce of ed on shares nt to 2004 Incentive et of res	-	183,245	183,245	-	(183,245)	-	-	-	
ted shares ld for taxes	-	(372)	(372)	-	(9,780)	-	-	-	(1
nsation e for ed shares		-	-		425,050	-	-	-	42
nsation e for stock .		-	-		1,922,379	-	-	-	1,92
ehensive e: ome		-	-		-	-	30,873,918	-	30,87
realized gs gains on es le for sale, deferred ense of ,491		-	-		-	-	-	7,851,910	7,85
ehensive :									38,72
es, ber 31,	$ 88,348,647	23,762,124	$ 23,762,124	$ 6,696,804	$ 417,040,974	$ -	$ 84,380,447	$ 7,069,400	$ 627,29

See accompanying notes to consolidated financial statements.

PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the years ended December 31, 2008	2007	2006
Operating activities:			
Net income	$ 30,873,918	$ 23,041,355	$ 17,927,033
Adjustments to reconcile net income to net cash provided by operating activities:			
Net amortization/accretion of premium/discount on securities	726,538	492,280	629,634
Depreciation and amortization	7,285,781	3,810,374	1,382,401
Provision for loan losses	11,213,543	4,719,841	3,732,032
Net gains on sale of premises	(1,030,231)	(75,337)	-
Gains on sales of investment securities, net	-	(16,472)	-
Gain on loan sales, net	(4,044,441)	(1,858,077)	(1,868,184)
Stock-based compensation expense	2,347,429	2,099,819	1,474,961
Deferred tax (benefit) expense	(2,619,989)	3,977,708	(1,164,336)
Losses on other real estate and other investments	1,165,145	-	-
Excess tax benefit from stock compensation	(875,114)	(105,809)	(131,121)
Mortgage loans held for sale:			
Loans originated	(293,906,669)	(169,808,372)	(131,971,094)
Loans sold	283,449,870	169,599,685	134,301,622
Increase in other assets	(15,654,171)	(17,471,118)	(6,103,122)
Increase (decrease) in other liabilities	14,701,265	(2,011,851)	(6,303,665)
Net cash provided by operating activities	33,632,874	16,394,026	11,906,161
Investing activities:			
Activities in available for sale securities:			
Purchases	(531,736,803)	(78,978,057)	(62,760,686)
Sales	-	770,400	-
Maturities, prepayments and calls	200,164,277	51,518,109	35,568,504
Activities in held to maturity securities:			
Maturities, prepayments and calls	16,420,000	-	-
Increase in loans, net	(636,979,248)	(386,164,624)	(297,565,733)
Purchases of premises and equipment and software	(9,449,780)	(5,793,535)	(4,649,676)
Proceeds from the sale of premises and equipment	2,821,702	278,278	-
Cash and cash equivalents (used for) provided by acquisitions, net of acquisition costs	(3,800,000)	38,149,471	36,230,539
Increases in other investments	(9,712,133)	(4,905,032)	(6,107,658)
Net cash used in investing activities	(972,271,985)	(385,681,546)	(299,284,710)
Financing activities:			
Net increase in deposits	610,090,035	346,584,243	229,745,145

Net increase (decrease) in repurchase agreements	28,226,963	(5,481,091)	75,181,529
Net increase in Federal funds purchased	31,781,000	39,862,000	-
Federal Home Loan Bank:			
Issuances	120,531,743	80,000,000	56,000,000
Payments	(29,163,002)	(102,304,513)	(61,540,828)
Net increase in borrowings under lines of credit	9,000,000	9,000,000	-
Proceeds from issuance of subordinated debt	15,000,000	30,928,000	20,619,000
Exercise of common stock warrants	250,000	-	55,000
Exercise of common stock options and stock appreciation rights	3,403,457	877,482	1,239,771
Excess tax benefit from stock compensation	875,114	105,809	131,121
Proceeds from the sale of common stock and common stock warrants, net of expenses	21,454,758	-	-
Proceeds from issuances of preferred stock, net of expenses	94,937,935	-	-
Costs incurred in connection with registration of common stock issued in merger	-	(299,397)	(187,609)
Net cash provided by financing activities	906,388,003	399,272,533	321,243,129
Net increase (decrease) in cash and cash equivalents	(32,251,108)	29,985,013	33,864,580
Cash and cash equivalents, beginning of year	122,503,863	92,518,850	58,654,270
Cash and cash equivalents, end of year	$ 90,252,755	$ 122,503,863	$ 92,518,850

See accompanying notes to consolidated financial statements.

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PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

Nature of Business Pinnacle Financial Partners, Inc. (Pinnacle Financial) is a bank holding company whose primary business is conducted by its wholly-owned subsidiary, Pinnacle National Bank (Pinnacle National). Pinnacle National is a commercial bank headquartered in Nashville, Tennessee. Pinnacle National provides a full range of banking services in its primary market areas of the Nashville-Davidson-Rutherford-Franklin, Tennessee and Knoxville, Tennessee Metropolitan Statistical Areas.

In addition to Pinnacle National, Pinnacle Financial, for the time period following the merger with Mid-America Bancshares, Inc. (Mid-America) on November 30, 2007 through February 29, 2008, conducted banking operations through the two banks formerly owned by Mid-America: PrimeTrust Bank in Nashville, Tennessee and Bank of the South in Mt. Juliet, Tennessee. On February 29, 2008, Pinnacle National purchased all of the assets and assumed all of the liabilities of PrimeTrust Bank and simultaneously, through a series of transactions, sold the PrimeTrust Bank charter and rights to operate a branch in Tennessee to an unaffiliated out-of-state third party for $500,000. Pinnacle Financial also merged Bank of the South into Pinnacle National on that date. References to Pinnacle National from and after November 30, 2007 include PrimeTrust Bank and Bank of the South.

Basis of Presentation These consolidated financial statements include the accounts of Pinnacle Financial and its wholly-owned subsidiaries. PNFP Statutory Trust I, PNFP Statutory Trust II, PNFP Statutory Trust III, PNFP Statutory Trust IV and Collateral Plus, LLC, are affiliates of Pinnacle Financial and are included in these consolidated financial statements pursuant to the equity method of accounting. Significant intercompany transactions and accounts are eliminated in consolidation.

Use of Estimates The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the balance sheet date and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term include the determination of the allowance for loan losses.

Impairment Long-lived assets, including purchased intangible assets subject to amortization, such as Pinnacle Financial s core deposit intangible asset, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the excess of the carrying amount over the fair value of the asset. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell and are no longer depreciated.

Goodwill and intangible assets that have indefinite useful lives are tested annually for impairment and are tested for impairment more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset s fair value. The goodwill impairment analysis is a two-step test. The first step, used to identify potential impairment, involves comparing each reporting unit s estimated fair value to its carrying value, including goodwill. If the estimated fair value of a reporting unit exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value exceeds estimated fair value, there is an indication of potential impairment and the second step is