2014
Annual Report

NORTHUMBERLAND BANCORP

NORTHUMBERLAND BANCORP
AUDITED CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2014

2014 ANNUAL REPORT
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Northumberland Bancorp

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March 27, 2015

To our Shareholders:

I am happy to report that Northumberland Bancorp (the Company) continued to grow in 2014. Assets at year end increased to $478,443,000, The Northumberland National Bank (the Bank) experienced some positive factors during the year. Net loans including loans available for sale grew $13,316,000 in 2014. This allowed the loan to deposit ratio to increase to 64.4% at December 31, 2014 up from 61.1% at December 31, 2013.

Net income of the Company decreased to $3,661,000 in 2014 from $4,196,000 in 2013. The decrease can be attributed primarily to a decline in non-interest income. This decline was a result in a decline in the gain on sale of mortgages, a lower level of security gains, and income in 2013 resulting from the reversal of a valuation allowance for mortgage servicing rights. The estimated value of the bank's mortgage servicing rights is currently in excess of the basis assigned.

Non-interest expense increased $402,000. This increase is spread among various expense categories. One area of interest is the engagement of FIS Pronet Solutions, Inc. to provide enhanced cyber security and network management capabilities to position the bank for the increased information technology needs of the bank going forward.

Asset quality remained strong. Net loan losses to average total loans were .05% compared to the national peer group of .18%. Loans evaluated as special mention and substandard decreased slightly to $4,869,000 compared to $5,146,000 in 2013.

The Company continues to be well capitalized. Tier one capital to average assets of the Bank increased to 9.84% compared to 9.22% at December 31, 2013. Dividends per share during the year increased to $.74 per share from $.68 in 2013 or an increase of 8.82%. During the year, the Company purchased 1,675 shares of Company stock to add to its treasury. This purchase was additive to the book value of the Company's stock.

In 2014, the Bank completed the expansion of its Hummel's Wharf Office to house an expanded commercial loan department, its secondary mortgage department and NNB Financial Services. This expansion will allow us to better serve our customers and provide more room for the bank's branch operation. The Bank has experienced delays in the approval process of the relocation of the Bank's Weis Market Office at Susquehanna Valley Mall. The branch will be relocated to a location in downtown Selinsgrove, which will better serve that customer segment.

We thank you, our valued shareholders, directors, officers and employees, for your contributions to the company's success during the year as we continue to pursue our mission, "To provide outstanding community banking and financial services throughout the Central Susquehanna Valley".

J. Donald Steele, Jr.

J. Donald Steele, Jr.
Chairman and President

SNODGRASS

CERTIFIED PUBLIC ACCOUNTANTS
AND CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

Board of Directors and Stockholders
Northumberland Bancorp

Report on the Financial Statements

We have audited the accompanying consolidated balance sheet of Northumberland Bancorp and subsidiary as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity, and cash flows for the years then ended; and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Northumberland Bancorp and subsidiary as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

S.R. Snodgrass, P.C.

Wexford, Pennsylvania
March 27, 2015

NORTHUMBERLAND BANCORP
CONSOLIDATED BALANCE SHEET
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

(Amounts in thousands except share data)

	2014	2013
ASSETS		
Cash and due from banks	$ 2,486	$ 2,898
Interest-bearing deposits in other banks	11,252	5,427
Total cash and cash equivalents	13,738	8,325
Investment securities available for sale	160,139	176,438
Investment securities held to maturity (fair value of $3,643 and $4,695)	3,621	4,663
Total investment securities	163,760	181,101
Loans held for sale	1,249	1,585
Loans	278,454	264,754
Less allowance for loan losses	2,553	2,505
Net loans	275,901	262,249
Premises and equipment	8,957	8,415
Bank-owned life insurance	8,252	8,001
Accrued interest and other assets	6,586	6,506
TOTAL ASSETS	$ 478,443	$ 476,182
LIABILITIES		
Deposits:		
Noninterest-bearing demand	$ 60,312	$ 51,091
Interest-bearing demand	173,436	181,119
Savings	70,291	67,504
Time deposits	126,256	132,309
Total deposits	430,295	432,023
Accrued interest and other liabilities	2,511	391
TOTAL LIABILITIES	432,806	432,414
STOCKHOLDERS' EQUITY		
Common stock, par value $.10; 5,000,000 shares authorized, 1,502,500 shares issued	150	150
Capital surplus	3,832	3,832
Retained earnings	45,534	42,858
Accumulated other comprehensive loss	(1,612)	(886)
	47,904	45,954
Treasury stock, at cost (172,142 and 170,467 shares)	(2,189)	(2,134)
TOTAL NORTHUMBERLAND BANCORP STOCKHOLDERS' EQUITY	45,715	43,820
Noncontrolling interest	(78)	(52)
TOTAL STOCKHOLDERS' EQUITY	45,637	43,768
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 478,443	$ 476,182

See accompanying notes to the consolidated financial statements.

NORTHUMBERLAND BANCORP
CONSOLIDATED STATEMENT OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

(Amounts in thousands except share data)

	2014	2013
INTEREST AND DIVIDEND INCOME		
Interest and fees on loans:		
Taxable	$ 11,978	$ 12,155
Tax-exempt	153	73
Interest on interest-bearing deposits in other banks	17	18
Interest and dividends on investment securities:		
Taxable	1,444	1,527
Tax-exempt	1,427	1,607
Dividends	137	45
Total interest and dividend income	15,156	15,425
INTEREST EXPENSE		
Deposits	2,865	3,560
Total interest expense	2,865	3,560
NET INTEREST INCOME	12,291	11,865
Provision for loan losses	178	122
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	12,113	11,743
NONINTEREST INCOME		
Service charges on deposit accounts	856	802
Trust services income	628	712
Investment securities gains, net	224	376
Gain on sale of loans	768	1,108
Earnings on bank-owned life insurance	251	247
Other income	668	878
Total noninterest income	3,395	4,123
NONINTEREST EXPENSE		
Salaries and employee benefits	5,940	5,833
Occupancy expense, net	688	668
Equipment expense	761	706
Professional fees	479	401
Data processing	392	357
Shares tax	242	286
Federal deposit insurance expense	268	266
Other expense	2,138	1,989
Total noninterest expense	10,908	10,506
Income before income taxes	4,600	5,360
Income taxes	965	1,209
NET INCOME	3,635	4,151
Less: net loss attributable to noncontrolling interest	(26)	(45)
NET INCOME ATTRIBUTABLE TO NORTHUMBERLAND BANCORP	$ 3,661	$ 4,196
EARNINGS PER SHARE	$ 2.75	$ 3.15
WEIGHTED-AVERAGE SHARES OUTSTANDING	1,330,848	1,332,828

See accompanying notes to the consolidated financial statements.

NORTHUMBERLAND BANCORP
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

(Amount in thousands)

	2014	2013
Net income	$ 3,635	$ 4,151
Other comprehensive loss:		
Change in unrealized holding gains (losses) on investment securities available for sale	1,404	(3,442)
Tax effect	(480)	1,170
Reclassification adjustment for investment securities gains recognized in net income	(224)	(376)
Tax effect	76	128
Change in unrecognized pension costs	(2,276)	2,007
Tax effect	774	(682)
Other comprehensive loss, net of tax	(726)	(1,195)
Net comprehensive income before noncontrolling interest	2,909	2,956
Less: net loss attributable to noncontrolling interest	(26)	(45)
Comprehensive income	$ 2,935	$ 3,001

See accompanying notes to the consolidated financial statements.

NORTHUMBERLAND BANCORP
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

(Amounts in thousands except share data)

	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Noncontrolling Interest	Total
Balance, December 31, 2012	$ 150	$ 3,832	$ 39,567	$ 309	$ (2,096)	$ (7)	$ 41,755
Net income			4,196			(45)	4,151
Other comprehensive loss				(1,195)			(1,195)
Dividends declared ($.68 per share)			(905)				(905)
Purchase of treasury stock (1,150 shares)					(38)		(38)
Balance, December 31, 2013	150	3,832	42,858	(886)	(2,134)	(52)	43,768
Net income			3,661			(26)	3,635
Other comprehensive loss				(726)			(726)
Dividends declared ($.74 per share)			(985)				(985)
Purchase of treasury stock (1,675 shares)					(55)		(55)
Balance, December 31, 2014	$ 150	$ 3,832	$ 45,534	$ (1,612)	$ (2,189)	$ (78)	$ 45,637

See accompanying notes to the consolidated financial statements.

NORTHUMBERLAND BANCORP
CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(Amount in thousands)

	2014	2013
OPERATING ACTIVITIES		
Net income	$ 3,635	$ 4,151
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	178	122
Depreciation, amortization, and accretion, net	2,341	2,636
Proceeds from sale of loans held for sale	21,229	31,836
Gain on sale of loans	(768)	(1,108)
Originations of residential loans held for sale	(20,125)	(27,798)
Investment securities gains, net	(224)	(376)
Deferred income taxes	3	81
Earnings on bank-owned life insurance	(251)	(247)
Change in valuation allowance on mortgage servicing rights	-	(152)
Decrease in prepaid federal deposit insurance	-	687
Decrease in accrued interest receivable	88	95
Decrease in accrued interest payable	(22)	(44)
Other, net	(117)	(588)
Net cash provided by operating activities	5,967	9,295
INVESTING ACTIVITIES		
Investment securities available for sale:		
Proceeds from sales	27,999	35,819
Proceeds from maturities or redemptions	20,590	22,986
Purchases	(32,365)	(52,070)
Investment securities held to maturity:		
Proceeds from sales	401	258
Proceeds from maturities or redemptions	600	520
Purchases	-	(1,036)
Increase in loans, net	(14,452)	(24,205)
Purchases of premises and equipment	(1,091)	(390)
Purchases of regulatory stock	(545)	(583)
Redemptions of regulatory stock	706	82
Purchase of bank-owned life insurance	-	(1,608)
Proceeds from sale of real estate owned	371	235
Net cash provided by (used for) investing activities	2,214	(19,992)
FINANCING ACTIVITIES		
Net (decrease) increase in deposits	(1,728)	11,929
Cash dividends paid	(985)	(905)
Purchase of treasury stock	(55)	(38)
Net cash (used for) provided by financing activities	(2,768)	10,986
Increase in cash and cash equivalents	5,413	289
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	8,325	8,036
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 13,738	$ 8,325

See accompanying notes to the consolidated financial statements.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of significant accounting and reporting policies applied in the presentation of the accompanying consolidated financial statements follows:

Nature of Operations and Basis of Presentation

Northumberland Bancorp (the "Company") is a Pennsylvania corporation and is registered under the Bank Holding Company Act. The Company was organized as the holding company of its wholly owned subsidiary, The Northumberland National Bank (the "Bank"). The Bank is a nationally chartered commercial bank located in Northumberland, Pennsylvania. The Bank's service area includes portions of Northumberland, Snyder, Union, and Montour counties in Pennsylvania. The Company and the Bank derive substantially all of their income from banking and bank-related services, which include interest earnings on commercial, commercial mortgage, residential real estate, and consumer loan financing as well as interest earnings on investment securities and deposit and trust services to their customers. The Bank created a new subsidiary, NNB Financial Services, during 2012 for the purpose of selling financial and insurance products. The Company is supervised by the Federal Reserve Board, while the Bank is subject to regulation and supervision by the Office of the Comptroller of the Currency.

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, the Bank. Intercompany activity has been eliminated in consolidation.

The consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles and with general practice within the banking industry. In preparing the financial statements, management is required to make certain estimates and assumptions that affect the reported amounts of assets and liabilities as of the Consolidated Balance Sheet date and revenues and expenses for the period. Actual results could differ significantly from those estimates.

Investment Securities

Investment securities are classified at the time of purchase, based on management's intention and ability, as securities held to maturity or securities available for sale. Debt securities acquired with the intent and ability to hold to maturity are stated at cost adjusted for amortization of premium and accretion of discount that are computed using the level yield method and recognized as adjustments of interest income. Certain other debt securities have been classified as available for sale to serve principally as a source of liquidity. Unrealized holding gains and losses for available-for-sale securities are reported as a separate component of stockholders' equity, net of tax, until realized. Realized securities gains and losses are computed using the specific identification method. Interest and dividends on investment securities are recognized as income when earned.

Securities are periodically reviewed for other-than-temporary impairment based upon a number of factors including, but not limited to, the length of time and extent to which the market value has been less than cost, the financial condition of the underlying issuer, the ability of the issuer to meet contractual obligations, the likelihood of the security's ability to recover any decline in its market value, and whether or not the Company intends to sell the security or whether it's more likely than not that the Company would be required to sell the security before its anticipated recovery in market value. A decline in value that is considered to be other than temporary is recorded as a loss within noninterest income in the Consolidated Statement of Income.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Federal Home Loan Bank Stock

The Bank is a member of the Federal Home Loan Bank ("FHLB") of Pittsburgh and, as such, is required to maintain a minimum investment in stock of the FHLB that varies with the level of advances outstanding with the FHLB, as well as a minimum level of mortgages in the MPF Program. The stock is bought from and sold to the FHLB based upon its $100 par value. The stock does not have a readily determinable fair value and as such is classified as restricted stock, carried at cost, and evaluated for impairment as necessary. The stock's value is determined by the ultimate recoverability of the par value rather than by recognizing temporary declines. The determination of whether the par value will ultimately be recovered is influenced by criteria such as the following: (a) the significance of the decline in net assets of the FHLB as compared to the capital stock amount and the length of time this situation has persisted; (b) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance; (c) the impact of legislative and regulatory changes on the customer base of the FHLB; and (d) the liquidity position of the FHLB. Management evaluated the stock and concluded that the stock was not impaired for the periods presented herein.

Loans Held for Sale and Loans Serviced

Loans held for sale are carried at the lower of cost or fair value, as determined on an aggregate basis. Gains and losses on sales of loans held for sale are recognized on settlement dates and are determined by the difference between the sale proceeds and the carrying value of loans. All sales are made with limited recourse. Loans held for sale were $1,249,000 and $1,585,000 at December 31, 2014 and 2013, respectively. At December 31, 2014 and 2013, the amounts of loans serviced by the Company for the benefit of others were $108,190,000 and $96,400,000, respectively.

Loans

Loans originated with the intention to hold to maturity are reported at their principal amount, net of unearned income and the allowance for loan losses. Interest income on all loans is recognized on an accrual basis. Nonrefundable loan fees and certain direct costs are deferred and amortized over the life of the loans using the interest method. The amortization is reflected as an interest yield adjustment, and the deferred portion of the net fees and costs is reflected as part of the loan balance. Accrual of interest is discontinued when, in the opinion of management, reasonable doubt exists as to the collectability of additional interest. Loans are returned to accrual status when past-due interest is collected and the collection of principal is probable.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for Loan Losses

The allowance for loan losses represents the amount that management estimates is adequate to provide for probable losses inherent in its loan portfolio. The allowance method is used in providing for loan losses. Accordingly, all loan losses are charged to the allowance, and all recoveries are credited to it. The allowance for loan losses is established through a provision for loan losses charged to operations. The provision for loan losses is based on management's periodic evaluation of individual loans, economic factors, past loan loss experience, changes in the composition and volume of the portfolio, and other relevant factors. The estimates used in determining the adequacy of the allowance for loan losses, including the amounts and timing of future cash flows expected on impaired loans, are particularly susceptible to changes in the near term.

Impaired loans are commercial and commercial real estate loans for which it is probable the Company will not be able to collect all amounts due according to the contractual terms of the loan agreement. The Company individually evaluates such loans for impairment and does not aggregate loans by major risk classifications. The definition of "impaired loans" is not the same as the definition of "nonaccrual loans," although the two categories overlap. The Company may choose to place a loan on nonaccrual status due to payment delinquency or uncertain collectability, while not classifying the loan as impaired if the loan is not a commercial or commercial real estate loan. Factors considered by management in determining impairment include payment status and collateral value. The amount of impairment for these types of impaired loans is determined by the difference between the present value of the expected cash flows related to the loan, using the original interest rate, and its recorded value, or as a practical expedient in the case of collateralized loans, the difference between the fair value of the collateral and the recorded amount of the loans. When foreclosure is probable, impairment is measured based on the fair value of the collateral.

Mortgage loans on one-to-four family properties and all consumer loans are large groups of smaller-balance homogeneous loans and are measured for impairment collectively. Loans that experience insignificant payment delays, which are defined as 90 days or less, generally are not classified as impaired. Management determines the significance of payment delays on a case-by-case basis taking into consideration all circumstances surrounding the loan and the borrower including the length of the delay, the borrower's prior payment record, and the amount of shortfall in relation to the principal and interest owed.

Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful lives of the assets, which range from 3 to 20 years for furniture, fixtures, and equipment and 15 to 50 years for buildings and leasehold improvements. Expenditures for maintenance and repairs are charged against income as incurred. Costs of major additions and improvements are capitalized.

Mortgage Servicing Rights ("MSRs")

The Company has agreements for the express purpose of selling loans in the secondary market. The Company maintains servicing rights for certain loans. Originated MSRs are recorded by allocating total costs incurred between the loan and servicing rights based on their relative fair values. MSRs are amortized in proportion to the estimated servicing income over the estimated life of the servicing portfolio. Annually, the Company performs an impairment review of the MSRs and recognizes impairment through a valuation account. No impairment was recognized in 2014 or 2013. In 2013 the Company reversed the $152,000 valuation allowance that was established in 2012 because the fair value exceeded carrying value at December 31, 2013. MSRs are a component of other assets on the Consolidated Balance Sheet.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Real Estate Owned

Real estate owned acquired in settlement of foreclosed loans is carried as a component of other assets at fair value minus estimated cost to sell. Prior to foreclosure, the estimated collectible value of the collateral is evaluated to determine whether a partial charge-off of the loan balance is necessary. After transfer to real estate owned, any subsequent write-downs are charged against other operating expenses. Direct costs incurred in the foreclosure process and subsequent holding costs incurred on such properties are recorded as expenses of current operations.

Bank Owned Life Insurance

The Company invests in bank owned life insurance ("BOLI") as a source of funding for employee benefit expenses. BOLI involves the purchasing of life insurance by the Bank on a select group of employees. The Company is the owner and beneficiary of the policies. This life insurance investment is carried at the cash surrender value of the underlying policies. Income from the increase in cash surrender value of the policies or from death benefits realized is included in other income on the Consolidated Statements of Income.

Advertising Costs

Advertising costs are expensed as the costs are incurred. Advertising expenses amounted to $128,000 and $155,000 for 2014 and 2013, respectively.

Income Taxes

The Company and the Bank file a consolidated federal income tax return. Deferred tax assets or liabilities are computed based on the difference between the financial statement and income tax basis of assets and liabilities using the enacted marginal tax rates. Deferred income tax expenses or benefits are based on the changes in the deferred tax asset or liability from period to period.

Pension Plan

The Bank has a noncontributory defined benefit pension plan that covers all eligible employees. Benefits are based upon years of service, the employee's compensation, and age at retirement. The Bank's contribution is actuarially determined and is intended to meet the current and projected obligations of the plan.

Trust Assets and Income

Assets held by the Bank in a fiduciary or agency capacity for its customers are not included in the accompanying financial statements, since such items are not assets of the Bank. In accordance with banking industry practice, trust services income is recognized on the cash basis and is not materially different than if it was reported on the accrual basis.

Comprehensive Income

The Company is required to present comprehensive income and its components in a full set of general-purpose financial statements for all periods presented. Other comprehensive income (loss) is composed of net unrealized holding gains or losses on its available-for-sale investment and mortgage-backed securities portfolio, as well as changes in unrecognized pension cost.

(Amounts in thousands except share data)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Earnings Per Share

The Company currently maintains a simple capital structure; therefore, there are no dilutive effects on earnings per share. As such, earnings per share are calculated using the weighted-average number of shares outstanding for the periods.

Cash Flow Information

The Company has defined cash and cash equivalents as those amounts included in the Consolidated Balance Sheet captions "Cash and due from banks," and "Interest-bearing deposits in other banks," with original maturities of 90 days or less.

	2014	2013
Cash paid during the year for:		
Interest	$ 2,887	$ 3,604
Income taxes	901	1,512
Noncash investing transactions:		
Transfer of loans to real estate owned	350	168

Reclassification of Comparative Amounts

Certain comparative amounts for the prior year have been reclassified to conform to current-year classifications. Such reclassifications had no effect on stockholders' equity or net income.

NOTE 2 - INVESTMENT SECURITIES

The amortized cost and fair values of investment securities are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
2014 AVAILABLE FOR SALE				
Obligations of states and political subdivisions	$ 56,689	$ 918	$ (162)	$ 57,445
Mortgage-backed securities in government-sponsored entities	101,812	453	(536)	101,729
Corporate debt securities	750	6	(1)	755
Subtotal	159,251	1,377	(699)	159,929
Equity securities in financial institutions	158	52	-	210
Total	$ 159,409	$ 1,429	$ (699)	$ 160,139

(Amounts in thousands except share data)

NOTE 2 - INVESTMENT SECURITIES (Continued)

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
2013 AVAILABLE FOR SALE				
Obligations of states and political subdivisions	$ 56,909	$ 1,064	$ (732)	$ 57,241
Mortgage-backed securities in government-sponsored entities	119,078	398	(1,246)	118,230
Corporate debt securities	750	8	(2)	756
Subtotal	176,737	1,470	(1,980)	176,227
Equity securities in financial institutions	151	60	-	211
Total	$ 176,888	$ 1,530	$ (1,980)	$ 176,438

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
2014 HELD TO MATURITY				
Obligations of states and political subdivisions	$ 3,371	$ 24	$ (2)	$ 3,393
Corporate debt securities	250	-	-	250
Total	$ 3,621	$ 24	$ (2)	$ 3,643

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
2013 HELD TO MATURITY				
Obligations of states and political subdivisions	$ 4,413	$ 39	$ (7)	$ 4,445
Corporate debt securities	250	-	-	250
Total	$ 4,663	$ 39	$ (7)	$ 4,695

(Amounts in thousands except share data)

NOTE 2 - INVESTMENT SECURITIES (Continued)

The following tables show the Company's gross unrealized losses and fair value, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position, at December 31, 2014 and 2013.

	2014					
	Less than Twelve Months		Twelve Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Obligations of states and political subdivisions	$ 7,147	$ (38)	$ 6,792	$ (126)	$ 13,939	$ (164)
Mortgage-backed securities in government-sponsored entities	18,945	(81)	42,638	(455)	61,583	(536)
Corporate debt securities	-	-	249	(1)	249	(1)
Total	$ 26,092	$ (119)	$ 49,679	$ (582)	$ 75,771	$ (701)

	2013					
	Less than Twelve Months		Twelve Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Obligations of states and political subdivisions	$ 20,656	$ (624)	$ 2,461	$ (115)	$ 23,117	$ (739)
Mortgage-backed securities in government-sponsored entities	60,355	(1,051)	17,932	(195)	78,287	(1,246)
Corporate debt securities	497	(2)	-	-	497	(2)
Total	$ 81,508	$ (1,677)	$ 20,393	$ (310)	$ 101,901	$ (1,987)

The Company reviews its position quarterly and has asserted that at December 31, 2014 and 2013, the declines outlined in the above table represent temporary declines and the Company does not intend to sell and does not believe it will be required to sell these securities before recovery of their cost basis, which may be at maturity. There were 135 positions that were temporarily impaired at December 31, 2014. The Company has concluded that the unrealized losses disclosed above are not other than temporary but are the result of interest rate changes, sector credit ratings changes, or Company-specific ratings changes that are not expected to result in the noncollection of principal and interest during the period.

(Amounts in thousands except share data)

NOTE 2 - INVESTMENT SECURITIES (Continued)

The amortized cost and fair value of debt securities at December 31, 2014, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 3,395	$ 3,430	$ 1,367	$ 1,373
Due after one year through five years	30,506	31,194	2,254	2,270
Due after five years through ten years	63,901	64,107	-	-
Due after ten years	61,449	61,198	-	-
Total	$ 159,251	$ 159,929	$ 3,621	$ 3,643

Proceeds from the sales of available-for-sale securities during 2014 amounted to $27,999,000 resulting in gross gains and gross losses of $263,000 and $40,000 respectively. Proceeds from the sales of available-for-sale securities during 2013 amounted to $35,819,000 resulting in gross gains and gross losses of $566,000 and $193,000, respectively.

The Company sold two held-to-maturity securities for proceeds of $401,000 during 2014 and one held-to-maturity security for proceeds of $258,000 during 2013. The held-to-maturities securities portfolio is not considered tainted because there was evidence that there was significant deterioration in the issuer's creditworthiness. The sales resulted in gains of $1,000 and $3,000 in 2014 and 2013, respectively.

Investment securities with fair values of $77,292,000 and $81,572,000 at December 31, 2014 and 2013, respectively, were pledged to secure public deposits and other purposes as required by law.

NOTE 3 - LOANS

Major classifications of loans are summarized as follows:

	2014	2013
Commercial	$ 56,947	$ 57,494
Commercial real estate	42,485	42,553
Residential real estate	173,952	160,795
Consumer	5,070	3,912
	278,454	264,754
Less allowance for loan losses	2,553	2,505
Net loans	$ 275,901	$ 262,249

The Company grants residential, commercial, and consumer loans to customers throughout its trade area, which is concentrated in North Central Pennsylvania. Although the Company has a diversified loan portfolio at December 31, 2014 and 2013, a substantial portion of its debtors' ability to honor their loan agreements is dependent upon the economic stability of its immediate trade area.

(Amounts in thousands except share data)

NOTE 4 - ALLOWANCE FOR LOAN LOSSES

Changes in the allowance for loan losses by portfolio segment are as follows:

	2014					
	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Beginning balance	$ 560	$ 385	$ 1,280	$ 30	$ 250	$ 2,505
Charge-offs	-	-	(118)	(17)	-	(135)
Recoveries	-	2	-	3	-	5
Provision	59	(85)	165	29	10	178
Ending balance	$ 619	$ 302	$ 1,327	$ 45	$ 260	$ 2,553

	2013					
	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Beginning balance	$ 603	$ 491	$ 1,056	$ 29	$ 279	$ 2,458
Charge-offs	-	-	(114)	(16)	-	(130)
Recoveries	44	-	-	11	-	55
Provision	(87)	(106)	338	6	(29)	122
Ending balance	$ 560	$ 385	$ 1,280	$ 30	$ 250	$ 2,505

Management has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and losses inherent in the loan portfolio. For purposes of determining the allowance for loan losses, the Company has segmented certain loans in the portfolio by product type. Loans are segmented into the following pools: commercial, commercial real estate loans, residential real estate loans, and consumer loans. Historical loss percentages for each risk category are calculated and used as the basis for calculating allowance allocations. These historical loss percentages are calculated over a three-year period for all portfolio segments. Certain qualitative factors are then added to the historical allocation percentage to apply the adjusted factor to nonclassified loans. The following qualitative factors are analyzed for each portfolio segment:

- Levels of and trends in delinquencies
- Trends in volume and terms
- Trends in credit quality ratings
- Changes in management and lending staff
- Economic trends
- Concentrations of credit

(Amounts in thousands except share data)

NOTE 4 - ALLOWANCE FOR LOAN LOSSES (Continued)

These qualitative factors are reviewed each quarter and adjusted based upon relevant changes within the portfolio. During 2014, the qualitative factors for all portfolio segments decreased slightly by 4 to 8 basis points. The historical loss factor for commercial loans decreased 20 basis points in 2014, while historical factors related to other portfolio segments remained the same. During 2013, the qualitative factors for commercial loans decreased slightly and factors for residential real estate increased slightly. The factors for the other portfolio segments remained the same during 2013.

The total allowance reflects management's estimate of loan losses inherent in the loan portfolio at the Consolidated Balance Sheet date. The Company considers the allowance for loan losses of $2,553,000 and $2,505,000 adequate to cover loan losses inherent in the loan portfolio at December 31, 2014 and 2013. The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31, 2014 and 2013:

	2014					
	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses:						
Individually evaluated for impairment	$ 261	$ 4	$ 18	$ -	$ -	$ 283
Collectively evaluated for impairment	358	298	1,309	45	260	2,270
Total	$ 619	$ 302	$ 1,327	$ 45	$ 260	$ 2,553
Loans:						
Individually evaluated for impairment	$ 2,173	$ 104	$ 41	$ -	$ -	$ 2,318
Collectively evaluated for impairment	54,774	42,381	173,911	5,070	-	276,136
Total	$ 56,947	$ 42,485	$ 173,952	$ 5,070	$ -	$ 278,454

	2013					
	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses:						
Individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -
Collectively evaluated for impairment	560	385	1,280	30	250	2,505
Total	$ 560	$ 385	$ 1,280	$ 30	$ 250	$ 2,505
Loans:						
Individually evaluated for impairment	$ 1,678	$ 102	$ -	$ -	$ -	$ 1,780
Collectively evaluated for impairment	55,816	42,451	160,795	3,912	-	262,974
Total	$ 57,494	$ 42,553	$ 160,795	$ 3,912	$ -	$ 264,754

Credit Quality Information

The Company's internally assigned grades are as follows:

Pass loans are protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral. There are five sub-grades within the Pass category to further distinguish the loan.

Special Mention loans are loans for which a potential weakness or risk exists, which could cause a more serious problem if not corrected.

(Amounts in thousands except share data)

NOTE 4 - ALLOWANCE FOR LOAN LOSSES (Continued)

Credit Quality Information (Continued)

Substandard loans have a well-defined weakness based on objective evidence and are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful loans have all the weaknesses inherent in a Substandard asset. In addition, these weaknesses make collection or liquidation in full highly questionable and improbable, based on existing circumstances.

Loss loans are considered uncollectible, or of such value that continuance as an asset is not warranted.

The following tables represent credit exposures by internally assigned grades for the years ended December 31, 2014 and 2013. The grading analysis estimates the capability of the borrower to repay the contractual obligations of the loan agreements as scheduled or at all. The Company's internal credit risk grading system is based on experiences with similarly graded loans.

	2014				
	Obligations of States and Political Subdivisions	Other Commercial Loans	Loans for Investment Properties	Other Commercial Real Estate Loans	Total
Pass	$ 20,097	$ 32,237	$ 19,237	$ 22,992	$ 94,563
Special Mention	-	183	-	-	183
Substandard	-	4,430	72	184	4,686
Doubtful	-	-	-	-	-
Loss	-	-	-	-	-
Ending balance	$ 20,097	$ 36,850	$ 19,309	$ 23,176	$ 99,432

	2013				
	Obligations of States and Political Subdivisions	Other Commercial Loans	Loans for Investment Properties	Other Commercial Real Estate Loans	Total
Pass	$ 20,862	$ 32,042	$ 20,331	$ 21,666	$ 94,901
Special Mention	-	586	-	-	586
Substandard	-	4,004	125	431	4,560
Doubtful	-	-	-	-	-
Loss	-	-	-	-	-
Ending balance	$ 20,862	$ 36,632	$ 20,456	$ 22,097	$ 100,047

(Amounts in thousands except share data)

NOTE 4 - ALLOWANCE FOR LOAN LOSSES (Continued)

Credit Quality Information (Continued)

The following tables present performing and nonperforming residential real estate and consumer loans based on payment activity for the years ended December 31, 2014 and 2013. Payment activity is reviewed by management on a monthly basis to determine how loans are performing. Loans are considered to be nonperforming when they become 90 days past due or are placed on nonaccrual.

	2014			
	First Mortgages	Home Equity Loans	Consumer	Total
Performing	$ 152,968	$ 20,394	$ 5,070	$ 178,432
Nonperforming	546	44	-	590
Total	$ 153,514	$ 20,438	$ 5,070	$ 179,022

	2013			
	First Mortgages	Home Equity Loans	Consumer	Total
Performing	$ 137,837	$ 22,450	$ 3,912	$ 164,199
Nonperforming	487	21	-	508
Total	$ 138,324	$ 22,471	$ 3,912	$ 164,707

Following are tables which include an aging analysis of the recorded investment of past-due loans as of December 31, 2014 and 2013.

	2014					
	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater	Total Past Due	Current	Total
Commercial						
Obligations of states and political subdivisions	$ -	$ -	$ -	$ -	$ 20,097	$ 20,097
Other commercial loans	277	-	-	277	36,573	36,850
Commercial real estate						
Loans for investment property	46	-	85	131	19,178	19,309
Other commercial real estate loans	-	-	-	-	23,176	23,176
Residential mortgage loans						
First mortgages	1,863	471	546	2,880	150,634	153,514
Home equity loans	214	4	44	262	20,176	20,438
Consumer	19	9	-	28	5,042	5,070
Total	$ 2,419	$ 484	$ 675	$ 3,578	$ 274,876	$ 278,454

(Amounts in thousands except share data)

NOTE 4 - ALLOWANCE FOR LOAN LOSSES (Continued)

Credit Quality Information (Continued)

	2013					
	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater	Total Past Due	Current	Total
Commercial						
Obligations of states and political subdivisions	$ -	$ -	$ -	$ -	$ 20,862	$ 20,862
Other commercial loans	116	-	244	360	36,272	36,632
Commercial real estate						
Loans for investment property	37	-	102	139	20,317	20,456
Other commercial real estate loans	-	-	-	-	22,097	22,097
Residential mortgage loans						
First mortgages	1,712	201	449	2,362	135,962	138,324
Home equity loans	127	27	21	175	22,296	22,471
Consumer	50	14	-	64	3,848	3,912
Total	$ 2,042	$ 242	$ 816	$ 3,100	$ 261,654	$ 264,754

Impaired Loans

Management evaluates commercial loans and commercial real estate loans which are 90 days or more past due and considers them to be impaired. Loans rated Substandard or Doubtful are also evaluated for impairment. These loans are analyzed to determine whether it is probable that all amounts will not be collected according to the contractual terms of the loan agreement. If management determines that the value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees, or costs and unamortized premium or discount), impairment is recognized through an allowance estimate or a charge-off to the allowance.

(Amounts in thousands except share data)

NOTE 4 - ALLOWANCE FOR LOAN LOSSES (Continued)

Impaired Loans (Continued)

The following tables include the recorded investment and unpaid principal balances for impaired loans with the associated allowance amount, if applicable, as of and for the years ending December 31:

	2014				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial:					
Other commercial loans	$ -	$ -	$ -	$ -	$ -
Commercial real estate:					
Loans for investment properties	78	96	-	79	3
Residential real estate:					
First mortgages	-	-	-	-	-
With an allowance recorded:					
Commercial:					
Other commercial loans	2,173	2,300	261	2,126	25
Commercial real estate:					
Loans for investment properties	26	37	4	32	1
Residential mortgage loans:					
First mortgages	41	52	18	47	2
Total	$ 2,318	$ 2,485	$ 283	$ 2,284	$ 31

	2013				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial:					
Other commercial loans	$ 1,678	$ 1,744	$ -	$ 1,709	$ 7
Commercial real estate:					
Loans for investment properties	102	150	-	123	4
With an allowance recorded:					
Commercial:					
Other commercial loans	-	-	-	-	-
Commercial real estate:					
Loans for investment properties	-	-	-	-	-
Total	$ 1,780	$ 1,894	$ -	$ 1,832	$ 11

(Amounts in thousands except share data)

NOTE 4 - ALLOWANCE FOR LOAN LOSSES (Continued)

Nonaccrual Loans

Loans are considered for nonaccrual status upon 90 days delinquency. When a loan is placed in nonaccrual status, previously accrued but unpaid interest is deducted from interest income.

The following tables present loans that are on nonaccrual status and that are 90 days delinquent and still accruing interest by portfolio segment as of December 31:

	2014	
	Nonaccrual	Past Due 90 Days or More and Still Accruing
Commercial:		
Obligations of states and political subdivisions	$ -	$ -
Other commercial loans	2,173	-
Commercial real estate:		
Loans for investment properties	45	59
Other commercial real estate loans	-	-
Residential mortgage loans:		
First mortgages	41	505
Home equity loans	-	44
Consumer loans	-	-
	$ 2,259	$ 608

	2013	
	Nonaccrual	Past Due 90 Days or More and Still Accruing
Commercial:		
Obligations of states and political subdivisions	$ -	$ -
Other commercial loans	1,434	244
Commercial real estate:		
Loans for investment properties	37	65
Other commercial real estate loans	-	-
Residential mortgage loans:		
First mortgages	38	449
Home equity loans	14	7
Consumer loans	-	-
	$ 1,523	$ 765

Interest income on nonaccrual loans not recognized during 2014 and 2013 was $78,000 and $68,000, respectively.

During the years ended December 31, 2014 and 2013, the Company did not have any loan modifications classified as troubled debt restructurings. During the periods, the Company also did not have any loans classified as a troubled debt restructuring that subsequently defaulted.

(Amounts in thousands except share data)

NOTE 5 - PREMISES AND EQUIPMENT

Major classifications of premises and equipment are summarized as follows:

	2014	2013
Land and improvements	$ 1,458	$ 1,458
Buildings and improvements	8,882	7,977
Furniture, fixtures, and equipment	3,476	3,814
	13,816	13,249
Less accumulated depreciation	4,859	4,834
Total	$ 8,957	$ 8,415

Depreciation expense for the years ended December 31, 2014 and 2013, was $549,000 and $539,000, respectively.

NOTE 6 - DEPOSITS

Time deposits at December 31, 2014, mature $62,708,000, $21,527,000, $10,149,000, $8,929,000, $22,015,000, and $928,000 during 2015, 2016, 2017, 2018, 2019, and thereafter, respectively.

Time deposits include certificates of deposit in denominations that meet or exceed the FDIC insurance limit at the balance sheet date. The FDIC insurance limit for the years ended December 31, 2014 and 2013, was $250,000. Such deposits aggregated $22,888,000 and $20,123,000 at December 31, 2014 and 2013, respectively. Maturities on time deposits that meet or exceed the FDIC insurance limit at December 31, 2014, are as follows:

Within three months	$ 452
Three through six months	4,356
Six through twelve months	9,045
Over twelve months	9,035
Total	$ 22,888

(Amounts in thousands except share data)

NOTE 7 - INCOME TAXES

The provision for income taxes consists of:

	2014	2013
Current	$ 962	$ 1,128
Deferred	3	81
Total	$ 965	$ 1,209

The tax effects of deductible and taxable temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities, respectively, at December 31 are as follows:

	2014	2013
Deferred tax assets:		
Allowance for loan losses	$ 779	$ 753
Accrued pension obligation	1,077	304
Unrealized loss on investment securities	-	153
Other	116	73
Total gross deferred tax assets	1,972	1,283
Deferred tax liabilities:		
Premises and equipment	475	522
Investment accretion	2	1
Unrealized gain on investment securities	250	-
Prepaid pension costs	495	392
Loan origination fees and costs	82	83
Other	16	-
Total gross deferred tax liabilities	1,320	998
Net deferred tax assets	$ 652	$ 285

No valuation allowance was established at December 31, 2014 and 2013, in view of the Company's ability to carryback to taxes paid in previous years and certain tax strategies, coupled with the anticipated future taxable income as evidenced by the Company's earnings potential.

The following is a reconciliation of the federal statutory rate and the Company's effective income tax rate for the years ended December 31:

	2014		2013	
	Amount	% of Pretax Income	Amount	% of Pretax Income
Provision at statutory rate	$ 1,573	34.0 %	$ 1,822	34.0 %
Effect of tax-free income	(633)	(13.7)	(666)	(12.4)
Nondeductible interest expense	25	0.6	53	1.0
Actual tax expense and effective rate	$ 965	20.9 %	$ 1,209	22.6 %

NOTE 7 - INCOME TAXES (Continued)

The Company prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Benefits from tax positions should be recognized in the financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority that would have full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be derecognized in the first subsequent financial reporting period in which that threshold is no longer met.

There is currently no liability for uncertain tax positions and no known unrecognized tax benefits. The Company recognizes, when applicable, interest and penalties related to unrecognized tax benefits in the provision for income taxes in the Consolidated Statement of Income. With few exceptions, the Company is no longer subject to U.S. federal or state income tax examinations by tax authorities for years before 2011.

NOTE 8 - COMMITMENTS AND CONTINGENCIES

In the normal course of business, the Company makes various commitments that are not reflected in the accompanying consolidated financial statements. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the Consolidated Balance Sheet. The Company's exposure to credit loss in the event of nonperformance by the other parties to the financial instruments is represented by the contractual amounts as disclosed. Losses, if any, are charged to the allowance for loan losses. The Company minimizes its exposure to credit loss under these commitments by subjecting them to credit approval, review procedures, and collateral requirements as deemed necessary.

The off-balance sheet commitments consisted of the following:

	2014	2013
Commitments to extend credit	$ 40,838	$ 44,888
Standby letters of credit	4,277	3,550

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the loan agreement. These commitments are composed primarily of available commercial lines of credit and mortgage loan commitments. The Company uses the same credit policies in making loan commitments and conditional obligations as it does for on-balance sheet instruments. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, as deemed necessary, is based upon management's credit evaluation in compliance with the Company's lending policy guidelines. Customers use credit commitments to ensure funds will be available for working capital purposes, for capital expenditures, and to ensure access to funds at specified terms and conditions.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Performance letters of credit represent conditional commitments issued by the Company to guarantee the performance of a customer to a third party. These instruments are issued primarily to support bid- or performance-related contracts. The coverage period for these instruments is typically a one-year period with an annual renewal option subject to prior approval by management. Fees earned from the issuance of these letters are recognized over the coverage period. For secured letters of credit, the collateral is typically Company deposit instruments or customer business assets.

(Amounts in thousands except share data)

NOTE 8 - COMMITMENTS AND CONTINGENCIES (Continued)

The Bank is a defendant in one lawsuit that arose out of the normal course of business, which management does not believe will have a material impact on the financial condition of the Company. The Company is currently involved in an investigation related to certain fiduciary activities of the Bank. Because the Company is in the early stages of the investigation, management is unable, at this time, to determine the probability of any claims being asserted in relation to the activities being investigated or the probability of an unfavorable outcome to any claims which may be asserted. Additionally, management is unable to reasonably estimate the amount of any potential loss.

NOTE 9 - PENSION PLAN

The Bank sponsors a defined benefit pension plan covering substantially all employees and officers. The plan calls for benefits to be paid to eligible employees at retirement, based primarily upon years of service with the Bank and compensation rates during employment. The Bank's funding policy is to make annual contributions, if needed, based upon the funding formula developed by the plan's actuary.

The following table sets forth the obligation and funded status as of December 31:

	2014	2013
Change in benefit obligation		
Benefit obligation at beginning of year	$ 6,868	$ 7,331
Service cost	617	683
Interest cost	336	288
Change in assumptions	2,420	(1,162)
Actuarial loss (gains)	51	(71)
Benefits paid	(114)	(201)
Benefit obligation at end of year	10,178	6,868
Change in plan assets		
Fair value of plan assets at beginning of year	7,157	5,474
Actual return on plan assets	749	1,084
Employer contribution	700	800
Benefits paid	(114)	(201)
Fair value of plan assets at end of year	8,492	7,157
Funded status	$ (1,686)	$ 289
Amounts recognized in accumulated other comprehensive loss consists of:		
Net loss	$ 3,169	$ 893
Total	$ 3,169	$ 893

The accumulated benefit obligation for the defined benefit pension plan was $8,196,000 and $5,574,000 at December 31, 2014 and 2013, respectively.

(Amounts in thousands except share data)

NOTE 9 - PENSION PLAN (Continued)

Components of Net Periodic Benefit Cost

	2014	2013
Net periodic pension cost:		
Service cost	$ 617	$ 683
Interest cost	336	288
Expected return on plan assets	(568)	(434)
Amortization of net loss	14	124
Net periodic benefit cost	$ 399	$ 661

The estimated net loss for the defined benefit pension plan that will be amortized from accumulated other comprehensive loss into net periodic benefit cost over the next fiscal year is $568,000.

Assumptions

The weighted-average assumptions used to determine benefit obligations at December 31:

	2014	2013
Discount rate	3.96 %	4.89 %
Rate of compensation increase	4.00	4.25

The weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:

	2014	2013
Discount rate	4.89 %	4.00 %
Expected long-term return on plan assets	8.00	8.00
Rate of compensation increase	4.00	4.25

The long-term rate of return on plan assets gives consideration to returns currently being earned on plan assets, as well as future rates expected to be returned.

(Amounts in thousands except share data)

NOTE 9 - PENSION PLAN (Continued)

Plan Assets

The Bank's defined benefit pension plan weighted-average asset allocations at December 31 by asset category are as follows:

Asset Category	2014		2013	
Mutual funds	65.64	%	70.91	%
Corporate bonds	15.85		16.64	
U.S. government agency securities	14.45		11.72	
Cash and cash equivalents	4.06		0.73	
Total	100.00	%	100.00	%

The Bank believes that the plan's risk and liquidity position are, in large part, a function of the asset class mix. The Bank desires to utilize a portfolio mix that results in a balanced investment strategy. The investment objective for the defined benefit pension plan is to maximize total return with tolerance for average to slightly above average risk. Asset allocation strongly favors mutual funds.

The following table sets forth by level, within the fair value hierarchy, the plan's assets at fair value as of December 31, 2014 and 2013:

	December 31, 2014			
	Level I	Level II	Level III	Total
Assets:				
Cash and cash equivalents	$ 332	$ -	$ -	$ 332
U.S. government agency securities	-	1,229	-	1,229
Corporate bonds	-	1,348	-	1,348
Mutual funds	5,583	-	-	5,583
Total assets at fair value	$ 5,915	$ 2,577	$ -	$ 8,492

	December 31, 2013			
	Level I	Level II	Level III	Total
Assets:				
Cash and cash equivalents	$ 52	$ -	$ -	$ 52
U.S. government agency securities	-	839	-	839
Corporate bonds	-	1,191	-	1,191
Mutual funds	5,075	-	-	5,075
Total assets at fair value	$ 5,127	$ 2,030	$ -	$ 7,157

Cash Flows

The Bank expects to contribute $800,000 to its defined benefit pension plan in 2015.

(Amounts in thousands except share data)

NOTE 9 - PENSION PLAN (Continued)

Cash Flows (Continued)

The following benefit payments that reflect expected future service, as appropriate, are expected to be paid:

	Pension Benefits
2015	$ 134
2016	133
2017	207
2018	301
2019	324
2020 through 2024	2,403

NOTE 10 - ACCUMULATED OTHER COMPREHENSIVE LOSS

The following tables present the changes in accumulated other comprehensive loss by component net of tax for the years ended December 31, 2014 and 2013:

	Unrealized Gains on Available-for-Sale Securities	Unrecognized Pension Costs	Total
Balance as of December 31, 2013	$ (297)	$ (589)	$ (886)
Other comprehensive income (loss) before reclassification	924	(1,511)	(587)
Amount reclassified from accumulated other comprehensive loss	(148)	9	(139)
Total other comprehensive income (loss)	776	(1,502)	(726)
Balance as of December 31, 2014	$ 479	$ (2,091)	$ (1,612)

	Unrealized Gains on Available-for-Sale Securities	Unrecognized Pension Costs	Total
Balance as of December 31, 2012	$ 2,223	$ (1,914)	$ 309
Other comprehensive income (loss) before reclassification	(2,272)	1,243	(1,029)
Amount reclassified from accumulated other comprehensive loss	(248)	82	(166)
Total other comprehensive income (loss)	(2,520)	1,325	(1,195)
Balance as of December 31, 2013	$ (297)	$ (589)	$ (886)

(Amounts in thousands except share data)

NOTE 10 - ACCUMULATED OTHER COMPREHENSIVE LOSS (Continued)

The following table presents significant amounts reclassified out of each component of accumulated other comprehensive loss for the years ended December 31, 2014 and 2013::

Details About Other Comprehensive Income	Amount Reclassified from Accumulated Other Comprehensive Loss 2014	Amount Reclassified from Accumulated Other Comprehensive Loss 2013	Affected Line Item in the Statement Where Net Income is Presented
Unrealized gains on available for sale securities			
	$ (224)	$ (376)	Investment securities gains, net
	76	128	Income taxes
	$ (148)	$ (248)	Net of tax
Unrecognized pension costs			
	$ 14	$ 124	Salaries and employee benefits
	(5)	(42)	Income taxes
	$ 9	$ 82	Net of tax

NOTE 11 - REGULATORY MATTERS

Cash and Due from Banks

The Bank is required to maintain average cash reserve balances in vault cash or with the Federal Reserve Bank. The amount of these restricted cash reserve balances at December 31, 2014 and 2013, was approximately $0 and $0, respectively.

Loans

Federal law prevents the Company from borrowing from the Bank unless the loans are secured by specific collateral. Further, such secured loans are limited in amount to 10 percent of the Bank's common stock and capital surplus.

Dividends

The Bank is subject to a dividend restriction that generally limits the amount of dividends that can be paid by a national bank. Prior approval of the Office of the Comptroller of the Currency ("OCC") is required if the total of all dividends declared by a national bank in any calendar year exceeds net profits, as defined for the year, combined with its retained net profits for the two preceding calendar years less any required transfers to surplus. Using this formula, the amount available for payment of dividends by the Bank in 2014, without approval of the OCC, is approximately $5,853,000 plus 2015 net profits retained up to the date of the dividend declaration.

Capital Requirements

Federal regulations require the Company and the Bank to maintain minimum amounts of capital. Specifically, each is required to maintain certain minimum dollar amounts and ratios of Total and Tier I capital to risk-weighted assets and of Tier I capital to average total assets.

(Amounts in thousands except share data)

NOTE 11 - REGULATORY MATTERS (Continued)

Capital Requirements (Continued)

In addition to the capital requirements, the Federal Deposit Insurance Corporation Improvement Act ("FDICIA") established five capital categories ranging from "well capitalized" to "critically undercapitalized." Should any institution fail to meet the requirements to be considered "adequately capitalized," it would become subject to a series of increasingly restrictive regulatory actions.

As of December 31, 2014 and 2013, the FDIC categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be classified as a well-capitalized financial institution, Total risk-based, Tier I risk-based, and Tier I leverage capital ratios must be at least 10 percent, 6 percent, and 5 percent, respectively.

The Company's actual capital ratios are presented in the following table that shows the Company met all regulatory capital requirements. The capital position of the Bank does not differ significantly from the Company's capital position.

	2014		2013	
	Amount	Ratio	Amount	Ratio
Total capital (to risk-weighted assets)				
Actual	$ 49,880	20.48 %	$ 47,167	20.65 %
For capital adequacy purposes	19,489	8.00	18,277	8.00
To be well capitalized	24,361	10.00	22,846	10.00
Tier I capital (to risk-weighted assets)				
Actual	$ 47,327	19.43 %	$ 44,662	19.55 %
For capital adequacy purposes	9,744	4.00	9,138	4.00
To be well capitalized	14,617	6.00	13,707	6.00
Tier I capital (to average assets)				
Actual	$ 47,327	9.89 %	$ 44,662	9.26 %
For capital adequacy purposes	19,144	4.00	19,229	4.00
To be well capitalized	23,930	5.00	24,124	5.00

(Amounts in thousands except share data)

NOTE 12 - FAIR VALUE MEASUREMENTS

The following disclosures show the hierarchal disclosure framework associated with the level of pricing observations utilized in measuring assets and liabilities at fair value. The three broad levels of pricing observations are as follows:

Level I: Quoted prices are available in active markets for identical assets or liabilities as of the reported date.

Level II: Pricing inputs are other than the quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these assets and liabilities includes items for which quoted prices are available but traded less frequently and items that are fair-valued using other financial instruments, the parameters of which can be directly observed.

Level III: Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

This hierarchy requires the use of observable market data when available.

The following tables present the assets measured on a recurring basis on the Consolidated Balance Sheet at their fair value as of December 31, 2014 and 2013, by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

	December 31, 2014			
	Level I	Level II	Level III	Total
Assets measured on a recurring basis:				
Investment securities available for sale:				
Obligations of states and political subdivisions	$ -	$ 57,445	$ -	$ 57,445
Mortgage-backed securities in government-sponsored entities	-	101,729	-	101,729
Corporate debt securities	-	755	-	755
Equity securities in financial institutions	210	-	-	210
Total	$ 210	$ 159,929	$ -	$ 160,139

	December 31, 2013			
	Level I	Level II	Level III	Total
Assets measured on a recurring basis:				
Investment securities available for sale:				
Obligations of states and political subdivisions	$ -	$ 57,241	$ -	$ 57,241
Mortgage-backed securities in government-sponsored entities	-	118,230	-	118,230
Corporate debt securities	-	756	-	756
Equity securities in financial institutions	211	-	-	211
Total	$ 211	$ 176,227	$ -	$ 176,438

(Amounts in thousands except share data)

NOTE 12 - FAIR VALUE MEASUREMENTS (Continued)

The following tables presents the assets measured on a nonrecurring basis on the Consolidated Balance Sheet at their fair value as of December 31, 2014 and 2013, by level within the fair value hierarchy. Impaired loans that are collateral dependent are written down to fair value through the establishment of specific reserves. Techniques used to value the collateral that secure the impaired loan include quoted market prices for identical assets classified as Level I inputs; and observable inputs, employed by certified appraisers, for similar assets classified as Level II inputs. In cases where valuation techniques included inputs that are unobservable and are based on estimates and assumptions developed by management based on the best information available under each circumstance, the asset valuation is classified as Level III inputs. The fair values consist of the loan balances of $2,318,000 and $1,780,000 less their valuation allowances of $283,000 and $0 at December 31, 2014 and 2013, respectively.

Other real estate owned ("OREO") is measured at fair value, less cost to sell at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value, less cost to sell.

	December 31, 2014			
	Level I	Level II	Level III	Total
Fair value measurements on nonrecurring basis:				
Impaired loans	$ -	$ -	$ 2,035	$ 2,035
Total	$ -	$ -	$ 2,035	$ 2,035

	December 31, 2013			
	Level I	Level II	Level III	Total
Fair value measurements on nonrecurring basis:				
Impaired loans	$ -	$ -	$ 1,780	$ 1,780
Other real estate owned	-	-	23	23
Total	$ -	$ -	$ 1,803	$ 1,803

(Amounts in thousands except share data)

NOTE 12 - FAIR VALUE MEASUREMENTS (Continued)

The following table provides information describing the valuation processes used to determine nonrecurring fair value measurements categorized within Level III of the fair value hierarchy:

	December 31, 2014			
	Quantitative Information About Level III Fair Value Measurements			
	Fair Value	Valuation Techniques	Unobservable Input	Range (Weighted Average)
Impaired loans	$ 2,035	Appraisal of collateral (1)	Appraisal adjustments (2)	0% - 46% (36%)

	December 31, 2013			
	Quantitative Information About Level III Fair Value Measurements			
	Fair Value	Valuation Techniques	Unobservable Input	Range (Weighted Average)
Impaired loans	$ 1,780	Appraisal of collateral (1)	Appraisal adjustments (2)	10% - 20% (14%)
Other real estate owned	23	Appraisal of collateral (1), (3)	Appraisal adjustments (2)	6% - 7% (7%)

(1) Fair value is generally determined through independent appraisals of the underlying collateral, which include various Level III inputs which are not identifiable.
(2) Appraisals may be adjusted by management for qualitative factors such as economic conditions, aging, and/or estimated liquidation expenses incurred when selling the collateral. The range and weighted average of appraisal adjustments and liquidation expenses are presented as a percentage of the appraisal.
(3) Includes qualitative adjustments by management and estimate liquidation expenses.

(Amounts in thousands except share data)

NOTE 13 - FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair values at December 31 of the Company's financial instruments are as follows:

	2014				
	Carrying Value	Fair Value	Level I	Level II	Level III
Financial assets:					
Cash and cash equivalents	$ 13,738	$ 13,738	$ 13,738	$ -	$ -
Investment securities:					
Available for sale	160,139	160,139	210	159,929	-
Held to maturity	3,621	3,643	-	3,643	-
Loans held for sale	1,249	1,249	1,249	-	-
Net loans	275,901	276,880	-	-	276,880
Regulatory stock	2,987	2,987	2,987	-	-
Bank-owned life insurance	8,252	8,252	8,252	-	-
Mortgage servicing rights	939	939	-	939	-
Accrued interest receivable	1,469	1,469	1,469	-	-
Financial liabilities:					
Deposits	$ 430,295	$ 431,689	$ 304,039	$ -	$ 127,650
Accrued interest payable	114	114	114	-	-

	2013				
	Carrying Value	Fair Value	Level I	Level II	Level III
Financial assets:					
Cash and cash equivalents	$ 8,325	$ 8,325	$ 8,325	$ -	$ -
Investment securities:					
Available for sale	176,438	176,438	211	176,227	-
Held to maturity	4,663	4,695	-	4,695	-
Loans held for sale	1,585	1,585	1,585	-	-
Net loans	262,249	260,724	-	-	260,724
Regulatory stock	3,148	3,148	3,148	-	-
Bank-owned life insurance	8,001	8,001	8,001	-	-
Mortgage servicing rights	887	894	-	894	-
Accrued interest receivable	1,557	1,557	1,557	-	-
Financial liabilities:					
Deposits	$ 432,023	$ 434,181	$ 299,714	$ -	$ 134,467
Accrued interest payable	136	136	136	-	-

Financial instruments are defined as cash, evidence of ownership interest in an entity, or a contract that creates an obligation or right to receive or deliver cash or another financial instrument from/to a second entity on potentially favorable or unfavorable terms.

NOTE 13 - FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Fair value is defined as the amount at which a financial instrument could be exchanged in a current transaction between willing parties other than in a forced or liquidation sale. If a quoted market price is available for a financial instrument, the estimated fair value would be calculated based upon the market price per trading unit of the instrument.

If no readily available market exists, the fair value estimates for financial instruments should be based upon management's judgment regarding current economic conditions, interest rate risk, expected cash flows, future estimated losses, and other factors as determined through various option pricing formulas. As many of these assumptions result from judgments made by management based upon estimates that are inherently uncertain, the resulting estimated fair values may not be indicative of the amount realizable in the sale of a particular financial instrument. In addition, changes in assumptions on which the estimated fair values are based may have a significant impact on the resulting estimated fair values.

As certain assets, such as deferred tax assets and premises and equipment, are not considered financial instruments, the estimated fair value of financial instruments would not represent the full value of the Company.

The Company employed simulation modeling in determining the estimated fair value of financial instruments for which quoted market prices were not available based upon the following assumptions:

Cash and Cash Equivalents, Loans Held for Sale, Regulatory Stock, Accrued Interest Receivable, and Accrued Interest Payable

The fair value is equal to the current carrying value.

Investment Securities

The fair market value of investment securities is equal to the available quoted market price. If no quoted market price is available, fair value is estimated using the quoted market price for similar securities. Fair values for certain corporate bonds were determined utilizing discounted cash flow models, due to the absence of a current market to provide reliable market quotes for the instruments.

Loans

Fair value is estimated by discounting future cash flows using current market inputs at which loans with similar terms and qualities would be made to borrowers of similar credit quality. Where quoted market prices were available, primarily for certain residential mortgage loans, such market rates were utilized as estimates for fair value.

Bank-Owned Life Insurance

The fair value is equal to the cash surrender value of the life insurance policies.

Mortgage Servicing Rights

The fair value for mortgage servicing rights is estimated by discounting contractual cash flows and adjusting for prepayment estimates. Discount rates are based upon rates generally charged for such loans with similar characteristics.

NOTE 13 - FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Deposits

The fair values of certificates of deposit are based on the discounted value of contractual cash flows. The discount rates are estimated using rates currently offered for similar instruments with similar remaining maturities. Demand, savings, and money market deposit accounts are valued at the amount payable on demand as of year-end.

Commitments to Extend Credit and Commercial Letters of Credit

These financial instruments are generally not subject to sale, and estimated fair values are not readily available.

The carrying value, represented by the net deferred fee arising from the unrecognized commitment or letter of credit, and the fair value, determined by discounting the remaining contractual fee over the term of the commitment using fees currently charged to enter into similar agreements with similar credit risk, are not considered material for disclosure. The contractual amounts of unfunded commitments and letters of credit are presented in Note 8.

NOTE 14 - SUBSEQUENT EVENTS

Management has reviewed events occurring through March 27, 2015, the date the financial statements were issued and no subsequent events occurred requiring accrual or disclosure.