EMCLAIRE FINANCIAL CORP
Form 10-K
March 24, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One):

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

For the fiscal year ended: December 31, 2015

.. 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: 000-18464

EMCLAIRE FINANCIAL CORP

(Exact name of registrant as specified in its charter)

Pennsylvania	25-1606091
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

612 Main Street, Emlenton, PA	16373
(Address of principal executive office)	(Zip Code)

Registrant's telephone number: (844) 767-2311

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, par value $1.25 per share	NASDAQ Capital Markets (NASDAQ)
(Title of Class)	(Name of exchange on which registered)

Securities registered pursuant 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 ¨ NO x.

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 ¨ NO x.

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 x NO ¨.

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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. x

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES ¨ NO x.

As of June 30, 2015, the aggregate value of the 1,809,195 shares of Common Stock of the Registrant issued and outstanding on such date, which excludes 324,663 shares held by the directors and officers of the Registrant as a group, was approximately $43.3 million. This figure is based on the last sales price of $23.94 per share of the Registrant's Common Stock on June 30, 2015. The number of outstanding shares of common stock as of March 24, 2016, was 2,144,808.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2016 Annual Meeting of Stockholders are incorporated by reference in Part III of this Form 10-K.

EMCLAIRE FINANCIAL CORP

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Discussions of certain matters in this Form 10-K and other related year end documents 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 Exchange Act), and as such, may involve risks and uncertainties. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies, and expectations, are generally identifiable by the use of words or phrases such as "believe", "plan", "expect", "intend", "anticipate", "estimate", "project", "forecast", "may increase", "may fluctuate", "may improve" and similar expr future or conditional verbs such as "will", "should", "would", and "could". These forward-looking statements relate to, amon other things, expectations of the business environment in which the Corporation operates, projections of future performance, potential future credit experience, perceived opportunities in the market and statements regarding the Corporation's mission and vision. The Corporation's actual results, performance and achievements may differ materially from the results, performance, and achievements expressed or implied in such forward-looking statements due to a wide range of factors. These factors include, but are not limited to, changes in interest rates, general economic conditions, the local economy, the demand for the Corporation's products and services, accounting principles or guidelines, legislative and regulatory changes, monetary and fiscal policies of the U.S. Government, U.S. Treasury, and Federal Reserve, real estate markets, competition in the financial services industry, attracting and retaining key personnel, performance of new employees, regulatory actions, changes in and utilization of new technologies and other risks detailed in the Corporation's reports filed with the Securities and Exchange Commission (SEC) from time to time. These factors should be considered in evaluating the forward-looking statements, and undue reliance should not be placed on such statements. The Corporation does not undertake, and specifically disclaims any obligation, to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

PART I

Item 1. Business

General

Emclaire Financial Corp (the Corporation) is a Pennsylvania corporation and financial holding company that provides a full range of retail and commercial financial products and services to customers in western Pennsylvania through its wholly owned subsidiary bank, The Farmers National Bank of Emlenton (the Bank). The Corporation also provides real estate settlement services through its subsidiary, Emclaire Settlement Services, LLC (the Title Company).

The Bank was organized in 1900 as a national banking association and is a financial intermediary whose principal business consists of attracting deposits from the general public and investing such funds in real estate loans secured by liens on residential and commercial property, consumer loans, commercial business loans, marketable securities and interest-earning deposits. The Bank currently operates through a network of fifteen retail branch offices in Venango, Butler, Clarion, Clearfield, Crawford, Elk, Jefferson and Mercer counties, Pennsylvania. The Corporation and the Bank are headquartered in Emlenton, Pennsylvania.

The Bank is subject to examination and comprehensive regulation by the Office of the Comptroller of the Currency (OCC), which is the Bank's chartering authority, and the Federal Deposit Insurance Corporation (FDIC), which insures customer deposits held by the Bank to the full extent provided by law. The Bank is a member of the Federal Reserve Bank of Cleveland (FRB) and the Federal Home Loan Bank of Pittsburgh (FHLB). The Corporation is a registered bank holding company pursuant to the Bank Holding Company Act of 1956, as amended (BHCA), and a financial holding company under the Gramm-Leach Bliley Act of 1999 (GLBA).

At December 31, 2015, the Corporation had \$600.6 million in total assets, \$52.8 million in stockholders' equity, \$429.9 million in net loans and \$489.9 million in total deposits.

On December 30, 2015, the Corporation announced the signing of a definitive merger agreement under which United American Savings Bank (United American) will merge into The Farmers National Bank of Emlenton in a cash transaction valued at approximately $14.1 million. United American is a traditional community bank with one branch location in Pittsburgh Pennsylvania, with reported assets of approximately $89.3 million at December 31, 2015.

Under the terms of the agreement, shareholders of United American will receive $42.67 in cash for each share of United American common stock. The transaction is expected to be completed in the second quarter of 2016, subject to the satisfaction of customary closing conditions, including regulatory approval and the approval of the shareholders of United American.

Lending Activities

General. The principal lending activities of the Corporation are the origination of residential mortgage, commercial mortgage, commercial business and consumer loans. Nearly all of the Corporation’s loans are originated in and secured by property within the Corporation’s primary market area.

One-to-Four Family Mortgage Loans. The Corporation offers first mortgage loans secured by one-to-four family residences located mainly in the Corporation’s primary lending area. One-to-four family mortgage loans amounted to 32.0% of the total loan portfolio at December 31, 2015. Typically such residences are single-family owner occupied units. The Corporation is an approved, qualified lender for the Federal Home Loan Mortgage Corporation (FHLMC) and the FHLB. As a result, the Corporation may sell loans to and service loans for the FHLMC and FHLB in market conditions and circumstances where this is advantageous in managing interest rate risk.

Home Equity Loans. The Corporation originates home equity loans secured by single-family residences. Home equity loans amounted to 20.1% of the total loan portfolio at December 31, 2015. These loans may be either a single advance fixed-rate loan with a term of up to 20 years or a variable rate revolving line of credit. These loans are made only on owner-occupied single-family residences.

Commercial Business and Commercial Real Estate Loans. Commercial lending constitutes a significant portion of the Corporation’s lending activities. Commercial business and commercial real estate loans amounted to 46.3% of the total loan portfolio at December 31, 2015. Commercial real estate loans generally consist of loans granted for commercial purposes secured by commercial or other nonresidential real estate. Commercial loans consist of secured and unsecured loans for such items as capital assets, inventory, operations and other commercial purposes.

Consumer Loans. Consumer loans generally consist of fixed-rate term loans for automobile purchases, home improvements not secured by real estate, capital and other personal expenditures. The Corporation also offers unsecured revolving personal lines of credit and overdraft protection. Consumer loans amounted to 1.6% of the total loan portfolio at December 31, 2015.

Loans to One Borrower. National banks are subject to limits on the amount of credit that they can extend to one borrower. Under current law, loans to one borrower are limited to an amount equal to 15% of unimpaired capital and surplus on an unsecured basis, and an additional amount equal to 10% of unimpaired capital and surplus if the loan is secured by readily marketable collateral. At December 31, 2015, the Bank's loans to one borrower limit based upon 15% of unimpaired capital was $8.4 million. The Bank may grant credit to borrowers in excess of the legal lending limit as part of the Legal Lending Limit Pilot Program approved by the OCC which allows the Bank to exceed its legal lending limit within certain parameters. At December 31, 2015, the Bank's largest single lending relationship had an outstanding balance of $8.4 million.

Loan Portfolio. The following table sets forth the composition and percentage of the Corporation's loans receivable in dollar amounts and in percentages of the portfolio as of December 31:

(Dollar amounts in thousands)	2015 Dollar Amount	%	2014 Dollar Amount	%	2013 Dollar Amount	%	2012 Dollar Amount	%	2011 Dollar Amount
Mortgage loans on real estate:									
Residential first mortgages	$139,305	32.0 %	$107,173	27.8 %	$105,541	29.5 %	$97,246	28.7 %	$93,610
Home equity loans and lines of credit	87,410	20.1 %	89,106	23.2 %	87,928	24.6 %	85,615	25.2 %	71,238
Commercial	129,691	29.8 %	110,810	28.8 %	101,499	28.5 %	98,823	29.2 %	94,765
Total real estate loans	356,406	81.9 %	307,089	79.8 %	294,968	82.6 %	281,684	83.1 %	259,613
Other loans:									
Commercial business	71,948	16.5 %	70,185	18.2 %	53,214	14.9 %	45,581	13.4 %	43,826
Consumer	6,742	1.6 %	7,598	2.0 %	9,117	2.6 %	11,886	3.5 %	12,642
Total other loans	78,690	18.1 %	77,783	20.2 %	62,331	17.4 %	57,467	16.9 %	56,468
Total loans receivable	435,096	100.0%	384,872	100.0%	357,299	100.0%	339,151	100.0%	316,081
Less:									
Allowance for loan losses	5,205		5,224		4,869		5,350		3,536
Net loans receivable	$429,891		$379,648		$352,430		$333,801		$312,545

The following table sets forth the final maturity of loans in the Corporation's portfolio as of December 31, 2015. Demand loans having no stated schedule of repayment and no stated maturity are reported as due within one year.

(Dollar amounts in thousands)	Due in one year or less	Due from one to five years	Due from five to ten years	Due after ten years	Total
Residential mortgages	$ 4,544	$ 1,805	$ 6,967	$125,989	$139,305
Home equity loans and lines of credit	94	8,624	24,539	54,153	87,410
Commercial mortgages	6,487	5,724	49,925	67,555	129,691
Commercial business	4,124	19,111	15,080	33,633	71,948
Consumer	153	3,521	955	2,113	6,742
	$ 15,402	$ 38,785	$ 97,466	$283,443	$435,096

The following table sets forth the dollar amount of the Corporation's fixed and adjustable rate loans with maturities greater than one year as of December 31, 2015:

(Dollar amounts in thousands)	Fixed rates	Adjustable rates
Residential mortgage	$123,741	$11,020
Home equity loans and lines of credit	73,751	13,564
Commercial mortgage	20,456	102,748
Commercial business	26,872	40,952
Consumer	4,873	1,717
	$249,693	$170,001

Contractual maturities of loans do not reflect the actual term of the Corporation's loan portfolio. The average life of mortgage loans is substantially less than their contractual terms because of loan prepayments and enforcement of due-on-sale clauses, which give the Corporation the right to declare a loan immediately payable in the event, among other things, that the borrower sells the real property subject to the mortgage. Scheduled principal amortization also reduces the average life of the loan portfolio. The average life of mortgage loans tends to increase when current market mortgage rates substantially exceed rates on existing mortgages and conversely, decrease when rates on existing mortgages substantially exceed current market interest rates.

Delinquencies and Classified Assets

Delinquent Loans and Other Real Estate Acquired Through Foreclosure (OREO). Typically, a loan is considered past due and a late charge is assessed when the borrower has not made a payment within fifteen days from the payment due date. When a borrower fails to make a required payment on a loan, the Corporation attempts to cure the deficiency by contacting the borrower. The initial contact with the borrower is made shortly after the seventeenth day following the due date for which a payment was not received. In most cases, delinquencies are cured promptly.

If the delinquency exceeds 60 days, the Corporation works with the borrower to set up a satisfactory repayment schedule. Typically, loans are considered nonaccruing upon reaching 90 days delinquent unless the credit is well secured and in the process of collection, although the Corporation may be receiving partial payments of interest and partial repayments of principal on such loans. When a loan is placed in nonaccrual status, previously accrued but unpaid interest is deducted from interest income. The Corporation institutes foreclosure action on secured loans only if all other remedies have been exhausted. If an action to foreclose is instituted and the loan is not reinstated or paid in full, the property is sold at a judicial or trustee's sale at which the Corporation may be the buyer.

Real estate properties acquired through, or in lieu of, foreclosure are to be sold and are initially recorded at fair value at the date of foreclosure less costs to sell, thereby establishing a new cost basis. After foreclosure, management periodically performs valuations and the real estate is carried at the lower of carrying amount or fair value less the cost to sell the property. Revenue and expenses from operations and changes in the valuation allowance are included in the loss on foreclosed real estate. The Corporation generally attempts to sell its OREO properties as soon as practical upon receipt of clear title.

As of December 31, 2015, the Corporation's nonperforming assets were $3.2 million, or 0.54% of the Corporation's total assets, compared to $7.1 million or 1.21% of the Corporation's total assets, at December 31, 2014. Nonperforming assets at December 31, 2015 included nonaccrual loans and OREO of $3.1 million and $160,000, respectively. Included in nonaccrual loans at December 31, 2015 were 5 loans totaling $363,000 considered to be troubled debt restructurings (TDRs). Interest income of $142,000 would have been recorded in 2015 if the nonaccrual loans had been current and performing during the entire period. Interest of $53,000 on these loans was included in income during 2015.

Classified Assets. Regulations applicable to insured institutions require the classification of problem assets as "substandard," "doubtful," or "loss" depending upon the existence of certain characteristics as discussed below. A category designated "special mention" must also be maintained for assets currently not requiring the above classifications but having potential weakness or risk characteristics that could result in future problems. An asset is classified as substandard if not adequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. A substandard asset is characterized by the distinct possibility that the Corporation will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all the weaknesses inherent in those classified as substandard. In addition, these weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable or improbable. Assets classified as loss are considered uncollectible and of such little value that their continuance as assets is not warranted.

The Corporation’s classification of assets policy requires the establishment of valuation allowances for loan losses in an amount deemed prudent by management. Valuation allowances represent loss allowances that have been established to recognize the inherent risk associated with lending activities. When the Corporation classifies a problem asset as a loss, the portion of the asset deemed uncollectible is charged off immediately.

The Corporation regularly reviews the problem loans and other assets in its portfolio to determine whether any require classification in accordance with the Corporation’s policy and applicable regulations. As of December 31, 2015, the Corporation’s classified and criticized assets amounted to $8.0 million or 1.3% of total assets, with $1.0 million identified as special mention and $6.9 million classified as substandard.

Included in classified and criticized assets at December 31, 2015 are two large loan relationships exhibiting credit deterioration impacting the ability of the borrowers to comply with their present loan repayment terms on a timely basis.

The first loan, with an outstanding balance of $2.7 million at December 31, 2015, was originated for the construction of a hotel, restaurant and retail plaza secured by such property and the borrower's personal residence. The hotel, restaurant and retail plaza are complete and operational. However, cash flows from operations have not been consistent and are impacted by the seasonal nature of the hotel. In addition, the borrower has limited liquid sources of repayment. As a result, the borrower has listed substantial real estate holdings for sale. At December 31, 2015, the loan was performing and classified as substandard. Ultimately, due to the estimated value of the borrower's significant real estate holdings, the Corporation does not currently expect to incur a loss on this loan.

The second relationship, with an outstanding balance of $1.0 million at December 31, 2015, is considered impaired and consists of one commercial real estate mortgage loan and two commercial business loans. The loans are secured by lien positions on the manufacturing facilities, equipment and other business assets. The borrower has experienced a substantial decrease in sales revenue due to a decrease in market demand for their primary product and pricing pressures in general. Sales efforts have been overhauled and new products segments have been launched. While revenues have stabilized, cash flow remains negative. All loans have remained current, due in part to financial support of the business owner. At December 31, 2015, the loans were nonperforming, classified as substandard and had a specific reserve of $47,000 allocated to them.

The following table sets forth information regarding the Corporation's nonperforming assets as of December 31:

(Dollar amounts in thousands)	2015	2014	2013	2012	2011
Nonperforming loans	$3,069	$6,942	$5,207	$6,988	$5,565
Total as a percentage of gross loans	0.71 %	1.80 %	1.46 %	2.06 %	1.76 %
Repossessions	-	-	-	-	-
Real estate acquired through foreclosure	160	124	107	180	307
Total as a percentage of total assets	0.03 %	0.02 %	0.02 %	0.04 %	0.06 %
Total nonperforming assets	$3,229	$7,066	$5,314	$7,168	$5,872
Total nonperforming assets as a percentage of total assets	0.54 %	1.21 %	1.01 %	1.41 %	1.19 %
Allowance for loan losses as a percentage of nonperforming loans	169.60%	75.25%	93.51%	76.56%	63.54%

Allowance for Loan Losses. Management establishes allowances for estimated losses on loans based upon its evaluation of the pertinent factors underlying the types and quality of loans; historical loss experience based on volume and types of loans; trend in portfolio volume and composition; level and trend on nonperforming assets; detailed analysis of individual loans for which full collectability may not be assured; determination of the existence and realizable value of the collateral and guarantees securing such loans and the current economic conditions affecting the collectability of loans in the portfolio. The Corporation analyzes its loan portfolio at least quarterly for valuation purposes and to determine the adequacy of its allowance for losses. Based upon the factors discussed above, management believes that the Corporation's allowance for losses as of December 31, 2015 of $5.2 million was adequate to cover probable incurred losses in the portfolio at such time.

The following table sets forth an analysis of the allowance for losses on loans receivable for the years ended December 31:

(Dollar amounts in thousands)	2015	2014	2013	2012	2011
Balance at beginning of period	$5,224	$4,869	$5,350	$3,536	$4,132
Provision for loan losses	381	670	580	2,154	420
Charge-offs:					
Residential mortgage loans	(79)	(134)	(36)	(90)	(224)
Home equity loans and lines of credit	(221)	(72)	(68)	(222)	(188)
Commercial mortgage loans	(35)	(2)	(941)	(35)	(200)
Commercial business loans	(182)	(17)	-	(50)	(415)
Consumer loans	(50)	(139)	(85)	(101)	(67)
	(567)	(364)	(1,130)	(498)	(1,094)
Recoveries:					
Residential mortgage loans	-	-	1	84	3
Home equity loans and lines of credit	30	1	-	27	1
Commercial mortgage loans	88	18	8	8	-
Commercial business loans	31	7	18	15	63
Consumer loans	18	23	42	24	11
	167	49	69	158	78
Net charge-offs	(400)	(315)	(1,061)	(340)	(1,016)
Balance at end of period	$5,205	$5,224	$4,869	$5,350	$3,536
Ratio of net charge-offs to average loans outstanding	0.10 %	0.08 %	0.30 %	0.10 %	0.32 %
Ratio of allowance to total loans at end of period	1.20 %	1.36 %	1.36 %	1.58 %	1.12 %

The following table provides a breakdown of the allowance for loan losses by major loan category for the years ended December 31:

(Dollar amounts in thousands)	2015		2014		2013		2012		2011	
Loan Categories:	Dollar Amount	Percent of loans in each category to total loans	Dollar Amount	Percent of loans in each category to total loans	Dollar Amount	Percent of loans in each category to total loans	Dollar Amount	Percent of loans in each category to total loans	Dollar Amount	Percent of loans in each category to total loans

Commercial, financial and agricultural	$960	16.5%	$1,336	18.2%	$822	14.9%	$636	13.4%	$590	13.9%
Commercial mortgages	2,185	29.8%	2,338	28.8%	2,450	28.4%	3,090	29.2%	1,737	30.0%
Residential mortgages	1,429	32.0%	955	27.8%	923	29.5%	828	28.7%	832	29.6%
Home equity loans	586	20.1%	543	23.2%	625	24.6%	730	25.2%	320	22.5%
Consumer loans	45	1.6 %	52	2.0 %	49	2.6 %	66	3.5 %	57	4.0 %
	$5,205	100 %	$5,224	100 %	$4,869	100 %	$5,350	100 %	$3,536	100 %

Investment Activities

General. The Corporation maintains an investment portfolio of securities such as U.S. government agencies, mortgage-backed securities, municipal and equity securities.

Investment decisions are made within policy guidelines as established by the Board of Directors. This policy is aimed at maintaining a diversified investment portfolio, which complements the overall asset/liability and liquidity objectives of the Corporation, while limiting the related credit risk to an acceptable level.

The following table sets forth certain information regarding the fair value, weighted average yields and contractual maturities of the Corporation's securities as of December 31, 2015:

(Dollar amounts in thousands)	Due in 1 year or less	Due from 1 to 3 years	Due from 3 to 5 years	Due from 5 to 10 years	Due after 10 years	No scheduled maturity	Total
U.S. Treasury and federal agency	$ -	$ -	$ 1,466	$ -	$ -	$ -	$ 1,466
U.S. government sponsored entities and agencies	-	1,989	6,964	-	-	-	8,953
U.S. agency mortgage-backed securities: residential	-	-	-	-	33,150	-	33,150
U.S. agency collateralized mortgage obligations: residential	-	-	-	-	31,440	-	31,440
Corporate securities	499	3,495	-	3,493	-	-	7,487
State and political subdivision	723	1,552	5,457	20,609	250	-	28,591
Equity securities	-	-	-	-	-	1,894	1,894
Estimated fair value	$ 1,222	$ 7,036	$ 13,887	$ 24,102	$ 64,840	$ 1,894	$ 112,981
Weighted average yield (1)	3.41 %	1.85 %	2.09 %	3.64 %	2.58 %	3.05 %	2.72 %

(1) Taxable equivalent adjustments have been made in calculating yields on state and political subdivision securities.

The following table sets forth the fair value of the Corporation's investment securities as of December 31:

(Dollar amounts in thousands)	2015	2014	2013
U.S. Treasury and federal agency	$ 1,466	$ 1,456	$ 4,168
U.S. government sponsored entities and agencies	8,953	35,224	22,892
U.S. agency mortgage-backed securities: residential	33,150	38,771	11,361
U.S. agency collateralized mortgage obligations: residential	31,440	36,617	39,722
Corporate securities	7,487	1,998	241
State and political subdivision	28,591	33,024	36,499
Equity securities	1,894	2,771	2,421
	$ 112,981	$ 149,861	$ 117,304

For additional information regarding the Corporation's investment portfolio see "Note 4 – Securities" on page F-16 to the consolidated financial statements.

Sources of Funds

General. Deposits are the primary source of the Corporation's funds for lending and investing activities. Secondary sources of funds are derived from loan repayments, investment maturities and borrowed funds. Loan repayments can be considered a relatively stable funding source, while deposit activity is greatly influenced by interest rates and general market conditions. The Corporation also has access to funds through other various sources. For additional information about the Corporation's sources of funds, see "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity" in item 7.

Deposits. The Corporation offers a wide variety of deposit account products to both consumer and commercial deposit customers, including time deposits, noninterest bearing and interest bearing demand deposit accounts, savings deposits and money market accounts.

Deposit products are promoted in periodic newspaper, radio and other forms of advertisements, along with notices provided in customer account statements. The Corporation's marketing strategy is based on its reputation as a community bank that provides quality products and personalized customer service.

The Corporation sets interest rates on its interest bearing deposit products that are competitive with rates offered by other financial institutions in its market area. Management reviews interest rates on deposits bi-weekly and considers a number of factors, including: (1) the Corporation's internal cost of funds; (2) rates offered by competing financial institutions; (3) investing and lending opportunities; and (4) the Corporation's liquidity position.

The following table summarizes the Corporation's deposits as of December 31:

(Dollar amounts in thousands)	2015			2014		
Type of accounts	Weighted average rate	Amount	%	Weighted average rate	Amount	%
Non-interest bearing deposits	-	$119,790	24.4 %	-	$111,282	22.2 %
Interest bearing demand deposits	0.15%	256,620	52.4 %	0.15%	269,402	53.7 %
Time deposits	1.46%	113,477	23.2 %	1.52%	121,135	24.1 %
	0.42%	$489,887	100.0%	0.45%	$501,819	100.0%

The following table sets forth maturities of the Corporation's time deposits of $250,000 or more at December 31, 2015 by time remaining to maturity:

(Dollar amounts in thousands)	Amount
Three months or less	$2,773
Over three months to six months	1,101
Over six months to twelve months	6,366
Over twelve months	11,999
	$22,239

Borrowings. Borrowings may be used to compensate for reductions in deposit inflows or net deposit outflows, or to support lending and investment activities. These borrowings include FHLB advances, federal funds, repurchase agreements, advances from the Federal Reserve Discount Window and lines of credit at the Bank and the Corporation with other correspondent banks. The following table summarizes information with respect to borrowings at or for the years ending December 31:

(Dollar amounts in thousands)	2015	2014
Ending balance	$49,250	$21,500
Average balance	21,489	19,417
Maximum balance	55,750	39,650
Average rate	3.21 %	3.49 %

For additional information regarding the Corporation's deposit base and borrowed funds, see "Management's Discussion and Analysis of Financial Condition and Results of Operations – Deposits and Borrowed Funds" in item 7 and "Note 10 – Deposits" on page F-28 and "Note 11 – Borrowed Funds" on page F-29 to the consolidated financial statements.

Subsidiary Activity

The Corporation has two wholly owned subsidiaries, the Bank and the Title Company. The Title Company provides real estate settlement services to the Bank and other customers. As of December 31, 2015, the Bank and the Title Company had no subsidiaries.

Personnel

At December 31, 2015, the Corporation had 122 full time equivalent employees. There is no collective bargaining agreement between the Corporation and its employees, and the Corporation believes its relationship with its employees is satisfactory.

Competition

The Corporation competes for loans, deposits and customers with other commercial banks, savings and loan associations, securities and brokerage companies, mortgage companies, insurance companies, finance companies, money market funds, credit unions and other nonbank financial service providers.

Supervision and Regulation

General. Bank holding companies and banks are extensively regulated under both federal and state law. Set forth below is a summary description of certain provisions of certain laws that relate to the regulation of the Corporation and the Bank. The description does not purport to be complete and is qualified in its entirety by reference to the applicable laws and regulations.

The Corporation. The Corporation is a registered bank holding company and subject to regulation and examination by the FRB under the BHCA. The Corporation is required to file periodic reports with the FRB and such additional information as the FRB may require. Recent changes to the Bank Holding Company rating system emphasize risk management and evaluation of the potential impact of non-depository entities on safety and soundness.

The FRB may require the Corporation to terminate an activity or terminate control of or liquidate or divest certain subsidiaries, affiliates or investments when the FRB believes the activity or the control of the subsidiary or affiliate constitutes a significant risk to the financial safety, soundness or stability of any of its banking subsidiaries. The FRB also has the authority to regulate provisions of certain bank holding company debt, including the authority to impose interest rate ceilings and reserve requirements on such debt. Under certain circumstances, the Corporation must file written notice and obtain FRB approval prior to purchasing or redeeming its equity securities.

The Corporation is required to obtain prior FRB approval for the acquisition of more than 5% of the outstanding shares of any class of voting securities or substantially all of the assets of any bank or bank holding company. Prior FRB approval is also required for the merger or consolidation of the Corporation and another bank holding company.

The BHCA generally prohibits a bank holding company from acquiring direct or indirect ownership or control of more than 5% of the outstanding voting shares of any company that is not a bank or bank holding company and from engaging directly or indirectly in activities other than those of banking, managing or controlling banks, or furnishing services to its subsidiaries. However, subject to the prior FRB approval, a bank holding company may engage in any, or acquire shares of companies engaged in, activities that the FRB deems to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.

The BHCA also authorizes bank holding companies to engage in securities, insurance and other activities that are financial in nature or incidental to a financial activity. In order to undertake these activities, a bank holding company must become a financial holding company by submitting to the appropriate FRB a declaration that the company elects to be a financial holding company and a certification that all of the depository institutions controlled by the company are well capitalized and well managed. The Corporation submitted the declaration of election to become a financial holding company with the FRB of Cleveland in February 2007, and the election became effective in March 2007. Recent federal legislation also directed federal regulators to require depository institution holding companies to serve as a source of strength for their depository institution subsidiaries.

Under FRB regulations, the Corporation is required to serve as a source of financial and managerial strength to the Bank and may not conduct operations in an unsafe or unsound manner. In addition, it is the FRB's policy that a bank holding company should stand ready to use available resources to provide adequate capital funds to its subsidiary banks during periods of financial stress or adversity and should maintain the financial flexibility and capital raising capacity to obtain additional resources for assisting its subsidiary banks. A bank holding company's failure to meet its obligations to serve as a source of strength to its subsidiary banks will generally be considered by the FRB to be an unsafe and unsound banking practice or a violation of FRB regulations or both.

The Corporation is also a bank holding company within the meaning of the Pennsylvania Banking Code. As such, the Corporation and its subsidiaries are subject to examination by, and may be required to file reports with, the Pennsylvania Department of Banking and Securities.

The Corporation's securities are registered with the SEC under the Exchange Act. As such, the Corporation is subject to the information, proxy solicitation, insider trading, corporate governance, and other requirements and restrictions of the Exchange Act. The public may obtain all forms and information filed with the SEC through its website http://www.sec.gov.

In December 2013, federal regulators adopted final rules to implement the provisions of the Dodd Frank Act commonly referred to as the Volcker Rule and established July 21, 2015 as the end of the conformance period. The regulations contain prohibitions and restrictions on the ability of financial institutions, holding companies and their affiliates to engage in proprietary trading and to hold certain interests in, or to have certain relationships with, various types of investment funds, including hedge funds and private equity funds.

The Bank. As a national banking association, the Bank is subject to primary supervision, examination and regulation by the OCC. The Bank is also subject to regulations of the FDIC as administrator of the Deposit Insurance Fund (DIF) and the FRB. If, as a result of an examination of the Bank, the OCC should determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity or other aspects of the Bank's operations are unsatisfactory or that the Bank is violating or has violated any law or regulation, various remedies are available to the OCC. Such remedies include the power to enjoin "unsafe or unsound practices," to require affirmative action to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in capital, to restrict the Bank's growth, to assess civil monetary penalties, and to remove officers and directors. The FDIC has similar enforcement authority, in addition to its authority to terminate the Bank's deposit insurance in the absence of action by the OCC and upon a finding that the Bank is operating in an unsafe or unsound condition, is engaging in unsafe or unsound activities, or that the Bank's conduct poses a risk to the deposit insurance fund or may prejudice the interest of its depositors.

A national bank may have a financial subsidiary engaged in any activity authorized for national banks directly or certain permissible activities. Generally, a financial subsidiary is permitted to engage in activities that are “financial in nature” or incidental thereto, even though they are not permissible for the national bank itself. The definition of “financial in nature” includes, among other items, underwriting, dealing in or making a market in securities, including, for example, distributing shares of mutual funds. The subsidiary may not, however, engage as principal in underwriting insurance, issue annuities or engage in real estate development or investment or merchant banking.

The Sarbanes-Oxley Act of 2002. The Sarbanes-Oxley Act of 2002 established a comprehensive framework to modernize and reform the oversight of public company auditing, improve the quality and transparency of financial reporting by those companies and strengthen the independence of auditors. Among other things, the legislation (i) created a public company accounting oversight board that is empowered to set auditing, quality control and ethics standards, to inspect registered public accounting firms, to conduct investigations and to take disciplinary actions, subject to SEC oversight and review; (ii) strengthened auditor independence from corporate management by limiting the scope of consulting services that auditors can offer their public company audit clients; (iii) heightened the responsibility of public company directors and senior managers for the quality of the financial reporting and disclosure made by their companies; (iv) adopted a number of provisions to deter wrongdoing by corporate management; (v) imposed a number of new corporate disclosure requirements; (vi) adopted provisions which generally seek to limit and expose to public view possible conflicts of interest affecting securities analysis; and (vii) imposed a range of new criminal penalties for fraud and other wrongful acts and extended the period during which certain types of lawsuits can be brought against a company or its insiders.

2010 Regulatory Reform. On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 was signed into law. The goals of the Dodd-Frank Act included restoring public confidence in the financial system following the financial crisis, preventing another financial crisis and permitting regulators to identify shortfalls in the system before another financial crisis can occur. The Dodd Frank Act is also intended to promote a fundamental restructuring of federal banking regulation by taking a systemic view of regulation rather than focusing on regulation of individual financial institutions.

Many of the provisions in the Dodd Frank Act require that regulatory agencies draft implementing regulations. Implementation of the Dodd Frank Act has had and will continue to have a broad impact on the financial services industry by introducing significant regulatory and compliance changes including, among other things: (i) changing the assessment base for federal deposit insurance from the amount of insured deposits to average consolidated total assets less average tangible equity, eliminating the ceiling and increasing the size of the floor of the DIF and offsetting the impact of the increase in the minimum floor on institutions with less than $10 billion in assets; (ii) making permanent the $250,000 limit for federal deposit insurance and increasing the cash limit of Securities Investor Protection Corporation protection to $250,000; (iii) eliminating the requirement that the FDIC pay dividends from the DIF when the reserve ratio is between 1.35% and 1.50%, but continuing the FDIC's authority to declare dividends when the reserve ratio at the end of a calendar year is at least 1.50%; however, the FDIC is granted sole discretion in determining whether to suspend or limit the declaration or payment of dividends; (iv) repealing the federal prohibition on payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts; (v) implementing certain corporate governance revisions that apply to all public companies, including regulations that require publicly traded companies to give shareholders a non-binding advisory vote to approve executive compensation, commonly referred to as a "say-on-pay" vote and an advisory role on so-called "golden parachute" payments in connection with approvals of mergers and acquisitions; new director independence requirements and considerations to be taken into account by compensation committees and their advisers relating to executive compensation; additional executive compensation disclosures; and a requirement that companies adopt a policy providing for the recovery of executive compensation in the even t of a restatement of its financial statements, commonly referred to as a "clawback" policy; (vi) centralizing responsibility for consumer financial protection by creating a new independent federal agency, the Consumer Financial Protection Bureau (CFPB) responsible for implementing federal consumer protection laws to be applicable to all depository institutions; (vii) imposing new requirements for mortgage lending, including new minimum underwriting standards, limitations on prepayment penalties and imposition of new mandated disclosures to mortgage borrowers; (viii) imposing new limits on affiliate transactions and causing derivative transactions to be subject to lending limits and other restrictions including adoption of the "Volcker Rule" regulating transactions in derivative securities; (ix) limiting debit card interchange fees that financial institutions with $10 billion or more in assets are permitted to charge their customers; and (x) implementing regulations to incentivize and protect individuals, commonly referred to as whistleblowers to report violations of federal securities laws.

Many aspects of the Dodd Frank Act continue to be subject to rulemaking and will take effect over several additional years, making it difficult to anticipate the overall financial impact on us or across the industry. The changes resulting from the Dodd Frank Act may impact the profitability of our business activities, require changes to certain of our business practices, impose upon us more stringent capital, liquidity and leverage requirements or otherwise adversely affect our business.

Anti-Money Laundering. All financial institutions, including national banks, are subject to federal laws that are designed to prevent the use of the U.S. financial system to fund terrorist activities. Financial institutions operating in the United States must develop anti-money laundering compliance programs, due diligence policies and controls to ensure the detection and reporting of money laundering. Such compliance programs are intended to supplement compliance requirements, also applicable to financial institutions, under the Bank Secrecy Act and the Office of Foreign Assets Control Regulations. The Bank has established policies and procedures to ensure compliance with these provisions.

Privacy. Federal banking rules limit the ability of banks and other financial institutions to disclose non-public information about consumers to nonaffiliated third parties. Pursuant to these rules, financial institutions must provide (i) initial notices to customers about their privacy policies, describing conditions under which they may disclose nonpublic personal information to nonaffiliated third parties and affiliates; (ii) annual notices of their privacy policies to current customers and (iii) a reasonable method for customers to "opt out" of disclosures to nonaffiliated third parties. These privacy provisions affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors. The Corporation's privacy policies have been implemented in accordance with the law.

Dividends and Other Transfers of Funds. Dividends from the Bank constitute the principal source of income to the Corporation. The Corporation is a legal entity separate and distinct from the Bank. The Bank is subject to various statutory and regulatory restrictions on its ability to pay dividends to the Corporation. In addition, the Bank's regulators have the authority to prohibit the Bank from paying dividends, depending upon the Bank's financial condition, if such payment is deemed to constitute an unsafe or unsound practice.

Limitations on Transactions with Affiliates. Transactions between national banks and any affiliate are governed by Sections 23A and 23B of the Federal Reserve Act. An affiliate of a national bank includes any company or entity which controls the national bank or that is controlled by a company that controls the national bank. In a holding company context, the holding company of a national bank (such as the Corporation) and any companies which are controlled by such holding company are affiliates of the national bank. Generally, Section 23A limits the extent to which the national bank of its subsidiaries may engage in "covered transactions" with any one affiliate to an amount equal to 10% of such bank's capital stock and surplus, and contains an aggregate limit on all such transactions with all affiliates to an amount equal to 20% of such capital stock and surplus. Section 23B applies to "covered transactions" as well as certain other transactions and requires that all transactions be on terms substantially the same, or at least favorable, to the national bank as those provided to a non-affiliate. The term "covered transaction" includes the making of loans to, purchase of assets from and issuance of a guarantee to an affiliate and similar transactions. Section 23B transactions also include the provision of services and the sale of assets by a national bank to an affiliate.

In addition, Sections 22(g) and (h) of the Federal Reserve Act place restrictions on loans to executive officers, directors and principal shareholders of the national bank and its affiliates. Under Section 22(h), loans to a director, an executive officer and to a greater than 10% shareholder of a national bank, and certain affiliated interests of either, may not exceed, together with all other outstanding loans to such person and affiliated interests, the national bank's loans to one borrower limit (generally equal to 15% of the bank's unimpaired capital and surplus). Section 22(h) also requires that loans to directors, executive officers and principal shareholders be made on terms substantially the same as offered in comparable transactions to other persons unless the loans are made pursuant to a benefit or compensation program that (i) is widely available to employees of the bank and (ii) does not give preference to any director, executive officer or principal shareholder, or certain affiliated interests of either, over other employees of the national bank. Section 22(h) also requires prior board approval for certain loans. In addition, the aggregate amount of extensions of credit by a national bank to all insiders cannot exceed the bank's unimpaired capital and surplus. Furthermore, Section 22(g) places additional restrictions on loans to executive officers. The Bank currently is subject to Sections 22(g) and (h) of the Federal Reserve Act and at December 31, 2015, was in compliance with the above restrictions.

Loans to One Borrower Limitations. With certain limited exceptions, the maximum amount that a national bank may lend to any borrower (including certain related entities of the borrower) at one time may not exceed 15% of the unimpaired capital and surplus of the institution, plus an additional 10% of unimpaired capital and surplus for loans fully secured by readily marketable collateral. At December 31, 2015, the Bank's loans-to-one-borrower limit was $8.4 million based upon the 15% of unimpaired capital and surplus measurement. The Bank may grant credit to borrowers in excess of the legal lending limit as part of the Legal Lending Limit Pilot Program approved by the OCC which allows the Bank to exceed its legal lending limit within certain parameters. At December 31, 2015, the Bank's largest single lending relationship had an outstanding balance of $8.4 million.

Capital Standards. The Bank is required to comply with applicable capital adequacy standards established by the federal banking agencies. Beginning on January 1, 2015, the Bank became subject to a new comprehensive capital framework for U.S. banking organizations. In July 2013, the Federal Reserve Board, FDIC and OCC adopted a final rule that implements the Basel III changes to the international regulatory capital framework. The Basel III rules include requirements contemplated by the Dodd Frank Act as well as certain standards initially adopted by the Basel Committee on Banking Supervision in December 2010.

The Basel III rules include new risk-based and leverage capital ratio requirements that refine the definition of what constitutes "capital" for purposes of calculating those ratios. The minimum capital level requirements are (i) a new common equity Tier 1 risk-based capital ratio of 4.5%; (ii) a Tier 1 risk-based capital ratio of 6% (increased from 4%); (iii) a total risk-based capital ratio of 8% (unchanged from previous rules); and (iv) a Tier 1 leverage ratio of 4% for all institutions. Common equity Tier 1 capital will consist of retained earnings and common stock instruments, subject to certain adjustments.

The Basel III rules also establish a fully-phased “capital conservation buffer” of 2.5% above the new regulatory minimum risk-based capital requirements. The conversation buffer, when added to the capital requirements, results in the following minimum ratios: (i) a common equity Tier 1 risk-based capital ratio of 7.0%, (ii) a Tier 1 risk-based capital ratio of 8.5% and (iii) a total risk-based capital ratio of 10.5%. The new capital conservation buffer requirement is to be phased in beginning January 2016 at 0.625% of risk-weighted assets and will increase by that amount each year until fully implemented in January 2019. An institution is subject to limitations on certain activities including payment of dividends, share repurchases and discretionary bonuses to executive officers if its capital level is below the buffer amount.

The Basel III rules also revise the prompt corrective action framework, which is designed to place restrictions on insured depository institutions if their capital levels do not meet certain thresholds. These revisions were effective January 1, 2015. The prompt corrective action rules were modified to include a common equity Tier 1 capital component and to increase certain other capital requirements for the various thresholds. Under the proposed prompt corrective action rules, insured depository institutions are required to meet the following capital levels in order to qualify as “well capitalized”: (i) a new common equity Tier 1 risk-based capital ratio of 6.5%; (ii) a Tier 1 risk-based capital ratio of 8% (increased from 6%); (iii) a total risk-based capital ratio of 10% (unchanged from previous rules); and (iv) a Tier 1 leverage ratio of 5% (unchanged from previous rules).

The Basel III rules set forth certain changes in the methods of calculating risk-weighted assets, which in turn affect the calculation of risk based ratios. Under the Basel III rules, higher or more sensitive risk weights are assigned to various categories of assets including certain credit facilities that finance the acquisition, development or construction of real property, certain exposures of credits that are 90 days past due or on nonaccrual, foreign exposures and certain corporate exposures. In addition, Basel III rules include (i) alternate standards of credit worthiness consistent with the Dodd Frank Act; (ii) greater recognition of collateral guarantees and (iii) revised capital treatment for derivatives and repo-style transactions.

In addition, the final rule includes certain exemptions to address concerns about the regulatory burden on community banks. Banking organizations with less than $15 billion in consolidated assets as of December 31, 2009 are permitted to include in Tier 1 capital trust preferred securities and cumulative perpetual preferred stock issued and included in Tier 1 capital prior to May 19, 2010 on a permanent basis without any phase out. Community banks were required to make this election by their March 31, 2015 quarterly filings with the appropriate federal regulator to opt-out of the requirement to include most accumulated other comprehensive income (AOCI) components in the calculation of Common equity Tier 1 capital and in effect retain the AOCI treatment under the current capital rules. The Bank made in its March 31, 2015 quarterly filing a one-time permanent election to continue to exclude accumulated other comprehensive income from capital. If it would not have made this election, unrealized gains and losses would have been included in the calculation of its regulatory capital.

The Basel III rules generally became effective beginning January 1, 2015; however, certain calculations under the Basel III rules have phase-in periods. In 2015, the Board of Governors of the Federal Reserve System amended its Small Bank Holding Company Policy Statement by increasing the policy’s consolidated assets threshold from $500 million to $1 billion. The primary benefit of being deemed a “small bank holding company’ is the exemption from the requirement to maintain consolidated regulatory capital ratios; instead, regulatory capital ratios only apply at the subsidiary bank level.

The following table sets forth certain information concerning regulatory capital ratios of the Bank as of the dates presented:

(Dollar amounts in thousands)	December 31, 2015 Amount	Ratio	December 31, 2014 Amount	Ratio
Total capital to risk-weighted assets:				
Actual	$ 56,090	13.99 %	$ 52,329	14.84 %
For capital adequacy purposes	32,070	8.00 %	28,201	8.00 %
To be well capitalized	40,087	10.00 %	35,251	10.00 %
Tier 1 capital to risk-weighted assets:				
Actual	$ 51,073	12.74 %	$ 47,878	13.58 %
For capital adequacy purposes	24,052	6.00 %	14,101	4.00 %
To be well capitalized	32,070	8.00 %	21,151	6.00 %
Common Equity Tier 1 capital to risk-weighted assets:				
Actual	$ 51,073	12.74 %	N/A	N/A
For capital adequacy purposes	18,039	4.50 %	N/A	N/A
To be well capitalized	26,057	6.50 %	N/A	N/A
Tier 1 capital to average assets:				
Actual	$ 51,073	8.83 %	$ 47,878	8.25 %
For capital adequacy purposes	23,131	4.00 %	23,222	4.00 %
To be well capitalized	28,914	5.00 %	29,028	5.00 %

Prompt Corrective Action and Other Enforcement Mechanisms. Federal banking agencies possess broad powers to take corrective and other supervisory action to resolve the problems of insured depository institutions, including but not limited to those institutions that fall below one or more prescribed minimum capital ratios. Each federal banking agency has promulgated regulations defining the following five categories in which an insured depository institution will be placed, based on its capital ratios: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized. At December 31, 2015, the Bank exceeded the required ratios for classification as “well capitalized.”

An institution that, based upon its capital levels, is classified as well capitalized, adequately capitalized, or undercapitalized may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition or an unsafe or unsound practice warrants such treatment. At each successive lower capital category, an insured depository institution is subject to more restrictions. The federal banking agencies, however, may not treat a significantly undercapitalized institution as critically undercapitalized.

In addition to measures taken under the prompt corrective action provisions, commercial banking organizations may be subject to potential enforcement actions by the federal regulators for unsafe or unsound practices in conducting their businesses or for violations of any law, rule, regulation, or any condition imposed in writing by the agency or any written agreement with the agency. Finally, pursuant to an interagency agreement, the FDIC can examine any institution that has a substandard regulatory examination score or is considered undercapitalized – without the permission of the institution's primary regulator.

Safety and Soundness Standards. The federal banking agencies have adopted guidelines designed to assist the federal banking agencies in identifying and addressing potential safety and soundness concerns before capital becomes impaired. The guidelines set forth operational and managerial standards relating to: (i) internal controls, information systems and internal audit systems, (ii) loan documentation, (iii) credit underwriting, (iv) asset growth, (v) earnings, and (vi) compensation, fees and benefits. In addition, the federal banking agencies have also adopted safety and soundness guidelines with respect to asset quality and earnings standards. These guidelines provide six standards for establishing and maintaining a system to identify problem assets and prevent those assets from deteriorating. Under these standards, an insured depository institution should: (i) conduct periodic asset quality reviews to identify problem assets, (ii) estimate the inherent losses in problem assets and establish reserves that are sufficient to absorb estimated losses, (iii) compare problem asset totals to capital, (iv) take appropriate corrective action to resolve problem assets, (v) consider the size and potential risks of material asset concentrations, and (vi) provide periodic asset quality reports with adequate information for management and the board of directors to assess the level of asset risk. These guidelines also set forth standards for evaluating and monitoring earnings and for ensuring that earnings are sufficient for the maintenance of adequate capital and reserves.

Insurance of Accounts. Deposit insurance assessment payments, which are determined through a risk-based assessment system, are made to the DIF. Deposit accounts are currently insured by the DIF generally up to a maximum of $250,000 per separately insured depositor.

Under the current assessment system, the FDIC assigns an institution to one of four risk categories designed to measure risk. Total base assessment rates currently range from 0.025% of deposits for an institution in the highest rated category to 0.45% of deposits for an institution in the lowest rated category. In addition, all FDIC insured institutions are required to pay assessments to the FDIC at an annual rate of approximately six tenths of a basis point of insured deposits to fund interest payments on bonds issued by the Financing Corporation, an agency of the federal government established to recapitalize the predecessor to the Savings Association Insurance Fund. These assessments will continue until the Financing Corporation bonds mature in 2017 through 2019.

Under the Federal Deposit Insurance Act, the FDIC may terminate deposit insurance upon a finding 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.

Interstate Banking and Branching. Banks have the ability, subject to certain state restrictions, to acquire, by acquisition or merger, branches outside its home state. In addition, recent federal legislation permits a bank headquartered in Pennsylvania to enter another state through de novo branching (as compared to an acquisition) if under the state law in the state which the proposed branch is to be located a state-chartered institution would be permitted to establish the branch. Interstate branches are subject to certain laws of the states in which they are located. Competition may increase further as banks branch across state lines and enter new markets.

Consumer Protection Laws and Regulations. The bank regulatory agencies are focusing greater attention on compliance with consumer protection laws and their implementing regulations. Examination and enforcement have become more intense in nature, and insured institutions have been advised to carefully monitor compliance with such laws and regulations. The Bank is subject to many federal consumer protection statutes and regulations, some of which are discussed below.

The Community Reinvestment Act (CRA) is intended to encourage insured depository institutions, while operating safely and soundly, to help meet the credit needs of their communities. The CRA specifically directs the federal regulatory agencies, in examining insured depository institutions, to assess a bank's record of helping meet the credit needs of its entire community, including low- and moderate-income neighborhoods, in a manner consistent with safe and sound banking practices. On September 1, 2005, the federal banking agencies amended the CRA regulations to (i) establish the definition of "Intermediate Small Bank" as an institution with total assets of $250 million to $1 billion, without regard to any holding company; and (ii) take into account abusive lending practices by a bank or its affiliates in determining a bank's CRA rating. The CRA further requires the agencies to take a financial institution's record of meeting its community credit needs into account when evaluating applications for, among other things, domestic branches, mergers or acquisitions, or holding company formations. The agencies use the CRA assessment factors in order to provide a rating to the financial institution. The ratings range from a high of "outstanding" to a low of "substantial noncompliance." In its last examination for CRA compliance, as of September 10, 2015, the Bank was rated "satisfactory."

The Fair Credit Reporting Act (FCRA), as amended by the Fair and Accurate Credit Transactions Act of 2003 (FACTA), requires financial firms to help deter identity theft, including developing appropriate fraud response programs, and give consumers more control of their credit data. It also reauthorizes a federal ban on state laws that interfere with corporate credit granting and marketing practices. In connection with the FACTA, financial institution regulatory agencies proposed rules that would prohibit an institution from using certain information about a consumer it received from an affiliate to make a solicitation to the consumer, unless the consumer has been notified and given a chance to opt out of such solicitations. A consumer's election to opt out would be applicable for at least five years.

The Federal Trade Commission (FTC), the federal bank regulatory agencies and the National Credit Union Administration (NCUA) have issued regulations (the Red Flag Rules) requiring financial institutions and creditors to develop and implement written identity theft prevention programs as part of the FACTA. The programs were required to be in place by May 1, 2009 and must provide for the identification, detection and response to patterns, practices or specific activities – known as red flags – that could indicate identity theft. These red flags may include unusual account activity, fraud alerts on a consumer report or attempted use of suspicious account application documents. The program must also describe appropriate responses that would prevent and mitigate the crime and detail a plan to update the program. The program must be managed by the Board of Directors or senior employees of the institution or creditor, include appropriate staff training and provide oversight of any service providers.

The Check Clearing for the 21st Century Act (Check 21) facilitates check truncation and electronic check exchange by authorizing a new negotiable instrument called a "substitute check," which is the legal equivalent of an original check. Check 21, effective October 28, 2004, does not require banks to create substitute checks or accept checks electronically; however, it does require banks to accept a legally equivalent substitute check in place of an original.

The Equal Credit Opportunity Act (ECOA) generally prohibits discrimination in any credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, age (except in limited circumstances), receipt of income from public assistance programs, or good faith exercise of any rights under the Consumer Credit Protection Act.

The Truth in Lending Act (TILA) is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably. As a result of the TILA, all creditors must use the same credit terminology to express rates and payments, including the annual percentage rate, the finance charge, the amount financed, the total of payments and the payment schedule, among other things.

The Fair Housing Act (FHA) regulates many practices, including making it unlawful for any lender to discriminate in its housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap or familial status. A number of lending practices have been found by the courts to be, or may be considered, illegal under the FHA, including some that are not specifically mentioned in the FHA itself.

The Home Mortgage Disclosure Act (HMDA) grew out of public concern over credit shortages in certain urban neighborhoods and provides public information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. The HMDA also includes a “fair lending” aspect that requires the collection and disclosure of data about applicant and borrower characteristics as a way of identifying possible discriminatory lending patterns and enforcing anti-discrimination statutes.

The term “predatory lending,” much like the terms “safety and soundness” and “unfair and deceptive practices,” is far-reaching and covers a potentially broad range of behavior. As such, it does not lend itself to a concise or a comprehensive definition. Generally speaking, predatory lending involves at least one, and perhaps all three, of the following elements (i) making unaffordable loans based on the assets of the borrower rather than on the borrower’s ability to repay an obligation (“asset-based lending”); (ii) inducing a borrower to refinance a loan repeatedly in order to charge high points and fees each time the loan is refinanced (“loan flipping”); and (iii) engaging in fraud or deception to conceal the true nature of the loan obligation from an unsuspecting or unsophisticated borrower.

FRB regulations aimed at curbing such lending significantly widened the pool of high-cost home-secured loans covered by the Home Ownership and Equity Protection Act of 1994, a federal law that requires extra disclosures and consumer protections to borrowers. Lenders that violate the rules face cancellation of loans and penalties equal to the finance charges paid.

Effective April 8, 2005, OCC guidelines require national banks and their operating subsidiaries to comply with certain standards when making or purchasing loans to avoid predatory or abusive residential mortgage lending practices. Failure to comply with the guidelines could be deemed an unsafe and unsound or unfair or deceptive practice, subjecting the bank to supervisory enforcement actions.

Finally, the Real Estate Settlement Procedures Act (RESPA) requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, RESPA prohibits certain abusive practices, such as kickbacks, and places limitations on the amount of escrow accounts. Penalties under the above laws may include fines, reimbursements and other penalties. Due to heightened regulatory concern related to compliance with the CRA, FACTA, TILA, FHA, ECOA, HMDA and RESPA generally, the Bank may incur additional compliance costs or be required to expend additional funds for investments in its local community.

Federal Home Loan Bank System. The Bank is a member of the FHLB. Among other benefits, each FHLB serves as a reserve or central bank for its members within its assigned region. Each FHLB is financed primarily from the sale of consolidated obligations of the FHLB system. Each FHLB makes available loans or advances to its members in compliance with the policies and procedures established by the Board of Directors of the individual FHLB. As an FHLB member, the Bank is required to own a certain amount of capital stock in the FHLB. At December 31, 2015, the Bank was in compliance with the stock requirements.

Federal Reserve System. The FRB requires all depository institutions to maintain noninterest bearing reserves at specified levels against their transaction accounts (primarily checking) and non-personal time deposits. At December 31, 2015, the Bank was in compliance with these requirements.

Item 1A. Risk Factors

Not required as the Corporation is a smaller reporting company.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Corporation owns no real property but utilizes the main office of the Bank, which is owned by the Bank. The Corporation's and the Bank's executive offices are located at 612 Main Street, Emlenton, Pennsylvania. The Corporation pays no rent or other form of consideration for the use of this facility.

The Bank owns and leases numerous other premises for use in conducting business activities. The Bank considers these facilities owned or occupied under lease to be adequate. For additional information regarding the Bank's properties, see "Note 7 - Premises and Equipment" on page F-26 to the consolidated financial statements.

Item 3. Legal Proceedings

Neither the Bank nor the Corporation is involved in any material legal proceedings. The Bank, from time to time, is party to litigation that arises in the ordinary course of business, such as claims to enforce liens, claims involving the origination and servicing of loans, and other issues related to the business of the Bank. In the opinion of management, the resolution of any such issues would not have a material adverse impact on the financial position, results of operation, or liquidity of the Bank or the Corporation.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market, Holder and Dividend Information

Emclaire Financial Corp common stock is traded on NASDAQ Capital Market (NASDAQ) under the symbol "EMCF". The listed market makers for the Corporation's common stock include:

Boenning and Scattergood, Inc.	**Janney Montgomery Scott LLC**	**Monroe Securities, Inc.**
4 Tower Bridge	1717 Arch Street	100 North Riverside Plaza
200 Barr Harbor Drive, Suite 300	Philadelphia, PA 19103	Suite 1620
West Conshohocken, PA 19428-2979	Telephone: (215) 665-6000	Chicago, IL 60606
Telephone: (800) 883-1212		Telephone: (312) 327-2530

The Corporation has traditionally paid regular quarterly cash dividends. Future dividends will be determined by the Board of Directors after giving consideration to the Corporation's financial condition, results of operations, tax status, industry standards, economic conditions, regulatory requirements and other factors.

The following table sets forth the high and low sale and quarter-end closing market prices of our common stock for the last two years as reported by the Nasdaq Capital Market as well as cash dividends paid for the quarterly periods presented.

	Market Price			Cash
	High	Low	Close	Dividend
2015:				
Fourth quarter	$25.00	$22.90	$24.00	$ 0.24
Third quarter	24.96	22.85	22.90	0.24
Second quarter	25.96	22.52	23.94	0.24
First quarter	27.15	23.50	25.10	0.24
2014:				
Fourth quarter	$26.95	$23.48	$25.00	$ 0.22
Third quarter	27.50	24.82	25.46	0.22
Second quarter	27.04	24.20	26.89	0.22
First quarter	26.09	24.26	25.62	0.22

As of March 1, 2016, there were approximately 649 stockholders of record and 2,144,808 shares of common stock entitled to vote, receive dividends and considered outstanding for financial reporting purposes. The number of stockholders of record does not include the number of persons or entities who hold their stock in nominee or “street” name.

Common stockholders may have dividends reinvested to purchase additional shares through the Corporation’s dividend reinvestment plan. Participants may also make optional cash purchases of common stock through this plan. To obtain a plan document and authorization card to participate in the plan, please call 888-509-4619.

Purchases of Equity Securities

The Corporation did not repurchase any of its equity securities in the year ended December 31, 2015.

Item 6. Selected Financial Data

Not required as the Corporation is a smaller reporting company.

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

The following discussion and analysis represents a review of the Corporation's consolidated financial condition and results of operations for the years ended December 31, 2015 and 2014. This review should be read in conjunction with the consolidated financial statements beginning on page F-3.

Overview

The Corporation reported consolidated net income available to common stockholders of $4.1 million or $2.05 per diluted common share for 2015, compared to $3.9 million or $2.20 per diluted common share for 2014. Net income available to common stockholders was impacted by the following:

- Net interest income increased $512,000 or 3.0% in 2015. This increase primarily related to an increase in interest income of $320,000 or 1.6% and a decrease in interest expense of $192,000 or 6.3%. Interest income for 2015 included $145,000 of recovered interest related to the full payoff of a $2.8 million nonperforming loan relationship and interest income for 2014 included $533,000 of recovered interest related to the full payoff of a $1.3 million nonperforming loan relationship. Driving the decrease in interest expense, the Corporation's cost of funds decreased 6 basis points to 0.53% for 2015 from 0.59% for 2014. Despite the impact of recovered interest and the management of funding costs, the net interest margin decreased 2 basis points to 3.33% for 2015, from 3.35% for 2014, as a result of an overall decline in asset yields.

- Noninterest income was stable at $4.1 million for the years ended December 31, 2015 and 2014. Net gains realized on the sale of securities increased $96,000, or 12.7%, to $854,000 in 2015 from $758,000 in 2014, while fees and service charges decreased $119,000.
- Noninterest expense increased $578,000, or 3.7%, to $16.2 million for the year ended December 31, 2015 from $15.6 million for 2014. The increase primarily related to increases in compensation and benefits, premises and equipment and professional fees of $584,000, $164,000 and $263,000, respectively.

Changes in Financial Condition

Total assets increased $18.7 million, or 3.2%, to $600.6 million at December 31, 2015 from $581.9 million at December 31, 2014. This increase primarily related to an increase in net loans receivable of $50.2 million. The loan growth and an $11.9 million decrease in deposits was funded by a $36.9 million decrease in securities and a $27.8 million increase in borrowed funds.

Cash and cash equivalents. Cash and cash equivalents decreased $310,000, or 2.6%, to $11.5 million at December 31, 2015 from $11.9 million at December 31, 2014. This decrease primarily resulted from the funding of loans and customer deposit withdrawals, partially offset by an increase in cash related to the sale of investment securities and borrowed funds advances. Typically, cash accounts are increased by net operating results, deposits by customers into savings and checking accounts, loan and security repayments and proceeds from borrowed funds. Decreases result from customer deposit withdrawals, new loan originations or other loan fundings, security purchases, repayments of borrowed funds and cash dividends to stockholders.

Securities. Securities decreased $36.9 million, or 24.6%, to $113.0 million at December 31, 2015 from $149.9 million at December 31, 2014. This decrease primarily resulted from investment security sales and calls totaling $36.1 million and $17.3 million, respectively, offset by purchases totaling $27.8 million during the year.

Loans receivable. Net loans receivable increased $50.2 million, or 13.2%, to $429.9 million at December 31, 2015 from $379.6 million at December 31, 2014. The increase was driven by growth in the Corporation’s residential mortgage, commercial mortgage and commercial business portfolios of $32.1 million, $18.9 million and $1.8 million, respectively, partially offset by decreases in the home equity and consumer portfolios of $1.7 million and $856,000, respectively. The growth of the Corporation’s residential mortgage portfolio included loan pool purchases totaling $19.2 million.

Nonperforming assets. Nonperforming assets include nonaccrual loans, loans 90 days past due and still accruing, repossessions and real estate owned. Nonperforming assets were $3.2 million, or 0.54% of total assets, at December 31, 2015 compared to $7.1 million, or 1.21% of total assets, at December 31, 2014. Nonperforming assets consisted of nonperforming loans and real estate owned of $3.1 million and $160,000, respectively, at December 31, 2015 and $6.9 million and $124,000, respectively, at December 31, 2014. This decrease in nonperforming loans was primarily due to the payoff of three nonperforming loan relationships totaling $4.7 million and the return of one previously nonperforming loan relationship totaling $447,000 to accrual status, partially offset by loan relationships of $1.0 million and $398,000 being placed on nonaccrual status during the year. At December 31, 2015, nonperforming loans consisted primarily of residential mortgage, commercial mortgage and commercial business loans.

Federal bank stocks. Federal bank stocks were comprised of FHLB stock and FRB stock of $3.2 million and $1.0 million, respectively, at December 31, 2015. These stocks are purchased and redeemed at par as directed by the federal banks and levels maintained are based primarily on borrowing and other correspondent relationships between the Corporation and the banks.

Bank-owned life insurance (BOLI). The Corporation maintains single premium life insurance policies on certain current and former officers and employees of the Bank. In addition to providing life insurance coverage, whereby the Bank as well as the officers and employees receive life insurance benefits, the appreciation of the cash surrender value of the BOLI will serve to offset and finance existing and future employee benefit costs. Increases in this account are typically associated with an increase in the cash surrender value of the policies, partially offset by certain administrative expenses. BOLI increased $328,000, or 3.1%, to $11.1 million at December 31, 2015 from $10.7 million at December 31, 2014.

Premises and equipment. Premises and equipment increased $970,000, or 6.4%, to $16.1 million at December 31, 2015 from $15.1 million at December 31, 2014. The overall increase in premises and equipment during the year was due to capital expenditures of $2.0 million, partially offset by depreciation and amortization of $1.0 million. Capital expenditures for 2015 included the purchase of equipment and software related to disaster recovery and mainframe upgrades and costs associated with the remodeling of two branch banking offices.

Goodwill. Goodwill was $3.7 million at December 31, 2015 and 2014. Goodwill is evaluated for impairment at least annually and more frequently if events and circumstances indicate that the asset might be impaired. Management evaluated goodwill and concluded that no impairment existed at December 31, 2015.

Core deposit intangible. The core deposit intangible was $554,000 at December 31, 2015. In connection with the assumption of deposits in the 2009 Titusville branch acquisition, the Corporation recorded a core deposit intangible of $2.8 million. This asset represents the long-term value of the core deposits acquired. Fair value was determined using a third-party valuation expert specializing in estimating fair values of core deposit intangibles. The fair value was derived using an industry standard financial instrument present value methodology. All-in costs and runoff balances by year were discounted by comparable term FHLB advance rates, used as an alternative cost of funds measure. This intangible asset amortizes utilizing the double declining balance method of amortization over a weighted average estimated life of nine years. The core deposit intangible asset is not estimated to have a significant residual value. The Corporation recorded $195,000 and $216,000 of intangible amortization in 2015 and 2014, respectively.

Deposits. Total deposits decreased $11.9 million to $489.9 million at December 31, 2015 from $501.8 million at December 31, 2014. Noninterest bearing deposits increased $8.5 million, or 7.7%, during the year while interest bearing deposits decreased $20.4 million, or 5.2%. The deposit decline was due in part to municipal customers drawing down deposit accounts due to their not receiving timely payments of anticipated government funding as a result of the Pennsylvania budget impasse.

Borrowed funds. Borrowed funds increased $27.8 million to $49.3 million at December 31, 2015 from $21.5 million at December 31, 2014. Borrowed funds at December 31, 2015 consisted of short-term borrowings of $14.3 million and long-term borrowings of $35.0 million. Long-term advances were utilized primarily to fund loan growth and short-term advances were utilized primarily to compensate for the abnormal year-end deposit decreases.

Accrued expenses and other liabilities. Accrued expenses and other liabilities decreased $2.0 million to $8.4 million at December 31, 2015 from $10.4 million at December 31, 2014. The Corporation’s pension obligation decreased $2.6 million to $806,000 at December 31, 2015 from $3.4 million at December 31, 2014 as the Corporation made a $3.0 million cash contribution to the plan during the year.

Stockholders’ equity. Stockholders’ equity increased $4.8 million, or 10.1%, to $52.8 million at December 31, 2015 from $48.0 million at December 31, 2014. The increase primarily related to an $8.2 million private placement common stock offering completed during the second quarter of 2015 and a $2.2 million increase in retained earnings as a result of net income totaling $4.2 million less dividends paid of $1.9 million. These increases were partially offset by a $5.0 million redemption of preferred stock and a $764,000 decrease in accumulated other comprehensive income resulting from changes in the net unrealized losses on securities available for sale and the funded status of the Corporation’s defined benefit plan.

Changes in Results of Operations

The Corporation reported net income before preferred stock dividends of $4.2 million and $4.0 million in 2015 and 2014, respectively. The following "Average Balance Sheet and Yield/Rate Analysis" and "Analysis of Changes in Net Interest Income" tables should be utilized in conjunction with the discussion of the interest income and interest expense components of net interest income.

Average Balance Sheet and Yield/Rate Analysis. The following table sets forth, for the periods indicated, information concerning the total dollar amounts of interest income from interest-earning assets and the resulting average yields, the total dollar amounts of interest expense on interest-bearing liabilities and the resulting average costs, net interest income, interest rate spread and the net interest margin earned on average interest-earning assets. For purposes of this table, average loan balances include nonaccrual loans and exclude the allowance for loan losses and interest income includes accretion of net deferred loan fees. Interest and yields on tax-exempt loans and securities (tax-exempt for federal income tax purposes) are shown on a fully tax equivalent basis. The information is based on average daily balances during the periods presented.

(Dollar amounts in thousands)	Year ended December 31,					
	2015			2014		
	Average Balance	Interest	Yield / Rate	Average Balance	Interest	Yield / Rate
Interest-earning assets:						
Loans, taxable	$375,164	$16,706	4.45 %	$341,183	$16,280	4.77 %
Loans, tax-exempt	25,535	1,244	4.87 %	22,619	1,140	5.04 %
Total loans receivable	400,699	17,950	4.48 %	363,802	17,420	4.79 %
Securities, taxable	107,009	1,965	1.84 %	106,282	1,958	1.84 %
Securities, tax-exempt	31,879	1,126	3.53 %	34,378	1,394	4.06 %
Total securities	138,888	3,091	2.23 %	140,660	3,352	2.38 %
Interest-earning deposits with banks	12,328	68	0.55 %	29,359	92	0.31 %
Federal bank stocks	2,419	164	6.78 %	2,832	145	5.12 %
Total interest-earning cash equivalents	14,747	232	1.57 %	32,191	237	0.74 %
Total interest-earning assets	554,334	21,273	3.84 %	536,653	21,009	3.91 %
Cash and due from banks	2,440			2,251		
Other noninterest-earning assets	34,347			31,318		
Total Assets	$591,121			$570,222		
Interest-bearing liabilities:						
Interest-bearing demand deposits	$272,582	412	0.15 %	$265,516	409	0.15 %
Time deposits	118,701	1,732	1.46 %	119,808	1,939	1.62 %
Total interest-bearing deposits	391,283	2,144	0.55 %	385,324	2,348	0.61 %
Borrowed funds, short-term	6,284	87	1.38 %	3,581	98	2.72 %
Borrowed funds, long-term (1)	15,205	604	3.97 %	15,836	581	3.67 %

Total borrowed funds	21,489	691	3.21 %	19,417	679	3.49 %
Total interest-bearing liabilities	412,772	2,835	0.69 %	404,741	3,027	0.75 %
Noninterest-bearing demand deposits	117,455	-	-	112,243	-	-
Funding and cost of funds	530,227	2,835	0.53 %	516,984	3,027	0.59 %
Other noninterest-bearing liabilities	8,254			5,828		
Total Liabilities	538,481			522,812		
Stockholders' Equity	52,640			47,410		
Total Liabilities and Stockholders' Equity	$591,121			$570,222		
Net interest income		$18,438			$17,982	
Interest rate spread (difference between weighted average rate on interest-earning assets and interest-bearing liabilities)			3.15 %			3.16 %
Net interest margin (net interest income as a percentage of average interest-earning assets)			3.33 %			3.35 %

(1) Interest on long-term borrowed funds for the period ended December 31, 2014 was reduced by $53,000 related to capitalized interest costs on construction in progress.

Analysis of Changes in Net Interest Income. The following table analyzes the changes in interest income and interest expense in terms of: (1) changes in volume of interest-earning assets and interest-bearing liabilities and (2) changes in yields and rates. The table reflects the extent to which changes in the Corporation's interest income and interest expense are attributable to changes in rate (change in rate multiplied by prior year volume), changes in volume (changes in volume multiplied by prior year rate) and changes attributable to the combined impact of volume/rate (change in rate multiplied by change in volume). The changes attributable to the combined impact of volume/rate are allocated on a consistent basis between the volume and rate variances. Changes in interest income on loans and securities reflect the changes in interest income on a fully tax equivalent basis.

(Dollar amounts in thousands)	2015 versus 2014		
	Increase (decrease) due to		
	Volume	Rate	Total
Interest income:			
Loans	$1,697	$(1,167)	$530
Securities	(42)	(219)	(261)
Interest-earning deposits with banks	(71)	47	(24)
Federal bank stocks	(23)	42	19
Total interest-earning assets	1,561	(1,297)	264
Interest expense:			
Deposits	36	(240)	(204)
Borrowed funds, short term	52	(63)	(11)
Borrowed funds, long term	(24)	47	23
Total interest-bearing liabilities	64	(256)	(192)
Net interest income	$1,497	$(1,041)	$456

2015 Results Compared to 2014 Results

The Corporation reported net income before preferred stock dividends of $4.2 million and $4.0 million for 2015 and 2014, respectively. The $137,000, or 3.4%, increase in net income was attributed to increases in net interest income and noninterest income of $512,000 and $7,000, respectively, and a decrease in provision for loan losses of $289,000, partially offset by increases in noninterest expense and the provision for income taxes of $578,000 and $93,000, respectively. Returns on average equity and assets were 7.89% and 0.70%, respectively, for 2015.

Net interest income. The primary source of the Corporation's revenue is net interest income. Net interest income is the difference between interest income on earning assets such as loans and securities, and interest expense on liabilities, such as deposits and borrowed funds, used to fund the earning assets. Net interest income is impacted by the volume and composition of interest-earning assets and interest-bearing liabilities, and changes in the level of interest rates. Tax equivalent net interest income increased $456,000 to $18.4 million for 2015, compared to $18.0 million for 2014. This increase in net interest income can be attributed to an increase in tax equivalent interest income of $264,000 and a decrease in interest expense of $192,000.

Interest income. Tax equivalent interest income increased $264,000, or 1.3%, to $21.3 million for 2015, compared to $21.0 million for 2014. This increase can be attributed to increases in interest earned on loans and dividends received on federal bank stocks of $530,000 and $19,000, respectively, partially offset by decreses in securities and interest earning cash equivalents of $261,000 and $24,000, respectively.

Tax equivalent interest earned on loans receivable increased $530,000, or 3.0%, to $18.0 million for 2015, compared to $17.4 million for 2014. The average balance of loans increased $36.9 million, or 10.1%, generating $1.7 million of additional interest income on loans. Offsetting this favorable variance, the average yield on loans decreased 31 basis points to 4.48% for 2015, versus 4.79% for 2014 causing a $1.2 million decrease in interest income.

Tax equivalent interest earned on securities decreased $261,000, or 7.8%, to $3.1 million for 2015 compared to $3.4 million for 2014. The average balance of securities decreased $1.8 million, or 1.3%, causing a $42,000 decrease in interest income. Also contributing to the unfavorable variance, the average yield on securities decreased 15 basis points to 2.23% for 2015 versus 2.38% for 2014 causing a $219,000 decrease in interest income.

Interest earned on interest-earning deposit accounts decreased $24,000, or 26.1%, to $68,000 for 2015 compared to $92,000 for 2014. The average balance of interest-earning deposits decreased $17.0 million causing a $71,000 decrease in interest income. Offsetting this unfavorable variance, the average yield on these accounts increased 24 basis points to 55 basis points for 2015 versus 31 basis points for 2014 generating $20,000 on additional interest income.

Interest earned on federal bank stocks increased $19,000, or 13.1%, to $164,000 for 2015 compared to $145,000 for 2014. The average yield on these accounts increased 166 basis points to 6.78% for 2015 versus 5.12% for 2014 generating a $42,000 increase in interest income. Offsetting this favorable yield variance, average federal bank stocks decreased $413,000, or 14.6%, causing a $23,000 decrease in interest income.

Interest expense. Interest expense decreased $192,000, or 6.3%, to $2.8 million for 2015 compared to $3.0 million for 2014. This decrease can be attributed to a decrease in interest expense on interest-bearing deposits of $204,000, partially offset by an increase in interest expense on borrowed funds of $12,000.

Interest expense on deposits decreased $204,000, or 8.7%, to $2.1 million for 2015 compared to $2.3 million for 2014. The average rate on interest-bearing deposits decreased by 6 basis points to 0.55% for 2015 versus 0.61% for 2014 causing a $240,000 decrease in interest expense. Offsetting this favorable variance, the average balance of interest-bearing deposits increased $6.0 million, or 1.5%, causing a $36,000 increase in interest expense.

Interest expense on borrowed funds increased $12,000, or 1.8%, to $691,000 for 2015 compared to $679,000 for 2014. The average balance of borrowed funds increased $2.1 million, or 10.7%, to $21.5 million for 2015 compared to $19.4 million for 2014 causing a $28,000 increase in interest expense. Partially offsetting this favorable variance, the average cost of borrowed funds decreased 28 basis points to 3.21% for 2015 versus 3.49% for 2014 causing a $16,000 decrease in interest expense. This was the result of the Corporation utilizing more overnight borrowed funds at a lower rate.

Provision for loan losses. The Corporation records provisions for loan losses to maintain a level of total allowance for loan losses that management believes, to the best of its knowledge, covers all probable incurred losses estimable at each reporting date. Management considers historical loss experience, the present and prospective financial condition of borrowers, current conditions (particularly as they relate to markets where the Corporation originates loans), the status of nonperforming assets, the estimated underlying value of the collateral and other factors related to the collectability of the loan portfolio.

Nonperforming loans decreased $3.9 million, or 55.8%, to $3.1 million at December 31, 2015 from $6.9 million at December 31, 2014. The decrease in nonperforming loans was primarily related to the payoff of three nonperforming loan relationships totaling $4.7 million, and the return of one previously nonperforming loan relationship totaling $447,000 to accrual status, partially offset by loan relationships of $1.0 million and $398,000 being placed on nonaccrual status during the year.

The provision for loan losses decreased $289,000, or 43.1%, to $381,000 for 2015 from $670,000 for 2014. The Corporation's allowance for loan losses amounted to $5.2 million, or 1.20% of the Corporation's total loan portfolio at December 31, 2015 compared to $5.2 million or 1.36% of total loans at December 31, 2014. The allowance for loan losses, as a percentage of nonperforming loans at December 31, 2015 and 2014, was 169.6% and 75.3%, respectively. The allocation of the allowance for loan losses related to residential mortgage loans increased during the year as a result of growth in the loan portfolio, while the allocation related to commercial loans decreased as a result of the resolution of loans individually evaluated for impairment.

Noninterest income. Noninterest income includes revenue that is not related to interest rates, but rather to services rendered and activities conducted in the financial services industry, including fees on depository accounts, general transaction and service fees, commissions on financial services, title premiums, security and loan gains and losses, and earnings on bank-owned life insurance (BOLI). Noninterest income increased $7,000, or 0.2%, to $4.1 million for 2015 and 2014. This increase was primarily due to increases in gains on the sale of securities and other noninterest income of $96,000 and $41,000, respectively. During 2015, the Corporation realized net securities gains of $854,000 compared to $758,000 realized in 2014. Partially offsetting these increases in noninterest income, fees and service charges and commissions on financial services decreased by $119,000 and $11,000, respectively.

Noninterest expense. Noninterest expense increased $578,000, or 3.7%, to $16.2 million for 2015, compared to $15.6 million for 2014. This increase was primarily related to increases in compensation and employee benefits, professional fees and premises and equipment expense, partially offset by decreases in intangible amortization, professional fees and FDIC insurance expense.

The largest component of noninterest expense, compensation and employee benefits, increased $584,000, or 7.6%, to $8.2 million for 2015 compared to $7.6 million for 2014. This increase primarily related to an increase in benefits expense and normal wage and salary increases.

Premises and equipment expense increased $164,000, or 6.6%, to $2.7 million for 2015 compared to $2.5 million for 2014. This increase primarily related to increases in expenses associated with the Bank's new branch office in Cranberry Township, Pennsylvania, which opened in May 2014 and an upgrade to the Bank's ATM fleet in the fourth quarter of 2014.

Professional fees increased $263,000, or 38.3%, to $950,000 for 2015 compared to $687,000 for 2014. This increase primarily related to costs associated with merger and acquisition activities.

Other noninterest expense decreased $412,000, or 9.9%, to $3.8 million for 2015 compared to $4.2 million for 2014. Included in other noninterest expense for 2014 was $550,000 in prepayment penalties incurred in the first quarter of 2014 associated with the early retirement of a $5.0 million FHLB long-term advance.

The Corporation recognized $195,000 of intangible amortization in 2015 compared to $216,000 in 2014 associated with a core deposit intangible asset of $2.8 million that was recorded in connection with the 2009 Titusville branch acquisition.

The provision for income taxes increased $93,000, or 8.9%, to $1.1 million for 2015 compared to $1.0 million for 2014 primarily due to an increase in taxable income. The difference between the statutory rate of 35% and the Corporation's effective tax rate of 21.5% for 2015 was due to tax-exempt income earned on certain tax-free loans and securities and bank-owned life insurance.

Market Risk Management

Market risk for the Corporation consists primarily of interest rate risk exposure and liquidity risk. The Corporation is not subject to currency exchange risk or commodity price risk, and has no trading portfolio, and therefore, is not subject to any trading risk. In addition, the Corporation does not participate in hedging transactions such as interest rate swaps and caps. Changes in interest rates will impact both income and expense recorded and also the market value of long-term interest-earning assets.

The primary objective of the Corporation's asset liability management function is to maximize the Corporation's net interest income while simultaneously maintaining an acceptable level of interest rate risk given the Corporation's operating environment, capital and liquidity requirements, balance sheet mix, performance objectives and overall business focus. One of the primary measures of the exposure of the Corporation's earnings to interest rate risk is the timing difference between the repricing or maturity of interest-earning assets and the repricing or maturity of its interest-bearing liabilities.

The Corporation's Board of Directors has established a Finance Committee, consisting of four outside directors, the President and Chief Executive Officer (CEO), Treasurer and Chief Financial Officer (CFO) and Principal Accounting Officer (PAO), to monitor market risk, including primarily interest rate risk. This committee, which meets at least quarterly, generally establishes and monitors the investment, interest rate risk and asset liability management policies of the Corporation.

In order to minimize the potential for adverse affects of material and prolonged changes in interest rates on the Corporation's results of operations, the Corporation's management team has implemented and continues to monitor asset liability management policies to better match the maturities and repricing terms of the Corporation's interest-earning assets and interest-bearing liabilities. Such policies have consisted primarily of (i) originating adjustable-rate mortgage loans; (ii) originating short-term secured commercial loans with the rate on the loan tied to the prime rate or reset features in which the rate changes at determined intervals; (iii) emphasizing investment in shorter-term (expected duration of five years or less) investment securities; (iv) selling longer-term (30-year) fixed-rate residential mortgage loans in the secondary market; (v) maintaining a high level of liquid assets (including securities classified as available for sale) that can be readily reinvested in higher yielding investments should interest rates rise; (vi) emphasizing the retention of lower-costing savings accounts and other core deposits; and (vii) lengthening liabilities and locking in lower borrowing rates with longer terms whenever possible.

Interest Rate Sensitivity Gap Analysis

The implementation of asset and liability initiatives and strategies and compliance with related policies, combined with other external factors such as demand for the Corporation's products and economic and interest rate environments in general, has resulted in the Corporation maintaining a one-year cumulative interest rate sensitivity gap within internal policy limits of between a positive and negative 15% of total assets. The one-year interest rate sensitivity gap is identified as the difference between the Corporation's interest-earning assets that are scheduled to mature or reprice within one year and its interest-bearing liabilities that are scheduled to mature or reprice within one year.

The interest rate sensitivity gap is defined as the difference between the amount of interest-earning assets maturing or repricing within a specific time period and the amount of interest-bearing liabilities maturing or repricing within that time period. A gap is considered positive when the amount of interest rate-sensitive assets exceeds the amount of interest rate-sensitive liabilities, and is considered negative when the amount of interest rate-sensitive liabilities exceeds the amount of interest rate-sensitive assets. Generally, during a period of rising interest rates, a negative gap would adversely affect net interest income while a positive gap would result in an increase in net interest income. Conversely, during a period of falling interest rates, a negative gap would result in an increase in net interest income and a positive gap would adversely affect net interest income. The closer to zero, or more neutral, that gap is maintained, generally, the lesser the impact of market interest rate changes on net interest income.

Based on certain assumptions derived from the Corporation's historical experience, at December 31, 2015, the Corporation's interest-earning assets maturing or repricing within one year totaled $166.5 million while the Corporation's interest-bearing liabilities maturing or repricing within one year totaled $160.2 million, providing an excess of interest-earning assets over interest-bearing liabilities of $6.3 million or 1.1% of total assets. At December 31, 2015, the percentage of the Corporation's assets to liabilities maturing or repricing within one year was 104.0%.

The following table presents the amounts of interest-earning assets and interest-bearing liabilities outstanding as of December 31, 2015 which are expected to mature, prepay or reprice in each of the future time periods presented:

(Dollar amounts in thousands)	Six months or less	Six months to one year	One to three years	Three to four years	Over four years	Total
Total interest-earning assets	$ 124,553	$ 41,989	$ 133,414	$ 57,041	$ 199,887	$ 556,884
Total interest-bearing liabilities	84,649	75,563	162,044	36,208	61,008	419,472
Interest rate sensitivity gap	$ 39,904	$ (33,574)	$ (28,630)	$ 20,833	$ 138,879	$ 137,412
Cumulative rate sensitivity gap	$ 39,904	$ 6,330	$ (22,300)	$ (1,467)	$ 137,412	
Ratio of gap during the period to total interest earning assets	7.17 %	(6.03) %	(5.14) %	3.74 %	24.94 %	
Ratio of cumulative gap to total interest earning assets	7.17 %	1.14 %	(4.00) %	(0.26) %	24.68 %	

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. The interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types of assets and liabilities may lag behind changes in market interest rates. In the event of a change in interest rates, prepayment and early withdrawal levels would likely deviate significantly from those assumed in calculating the table. The ability of many borrowers to service their debt may decrease in the event of an interest rate increase.

Interest Rate Sensitivity Simulation Analysis

The Corporation also utilizes income simulation modeling in measuring its interest rate risk and managing its interest rate sensitivity. The Finance Committee of the Board of Directors believes that simulation modeling enables the Corporation to more accurately evaluate and manage the possible effects on net interest income due to the exposure to changing market interest rates and different loan and security prepayment and deposit decay assumptions under various interest rate scenarios.

As with gap analysis and earnings simulation modeling, assumptions about the timing and variability of cash flows are critical in net portfolio equity valuation analysis. Particularly important are the assumptions driving mortgage prepayments and the assumptions about expected attrition of the core deposit portfolios. These assumptions are based on the Corporation's historical experience.

The Corporation has established the following guidelines for assessing interest rate risk:

Net interest income simulation. Given a 200 basis point immediate increase or decrease in market interest rates, net interest income may not change by more than 15% for a one-year period.

Economic value of equity simulation. Economic value of equity is the present value of the Corporation's existing assets less the present value of the Corporation's existing liabilities. Given a 200 basis point immediate and permanent increase or decrease in market interest rates, economic value of equity may not correspondingly decrease or increase by more than 20%.

These guidelines take into consideration the current interest rate environment, the Corporation's financial asset and financial liability product mix and characteristics and liquidity sources among other factors. Given the current rate environment, a drop in short-term market interest rates of 200 basis points immediately or over a one-year horizon would seem unlikely. This should be considered in evaluating modeling results outlined in the table below.

The following table presents the simulated impact of a 100 basis point or 200 basis point upward or downward shift of market interest rates on net interest income for the years ended December 31, 2015 and 2014, respectively. This analysis was done assuming that the interest-earning asset and interest-bearing liability levels at December 31, 2015 remained constant. The impact of the market rate movements on net interest income was developed by simulating the effects of rates changing immediately for a one-year period from the December 31, 2015 levels for net interest income.

	Increase		Decrease	
	+100 BP	+200 BP	-100 BP	-200 BP
2015 Net interest income - increase (decrease)				