AMERISERV FINANCIAL INC /PA/
Form 10-Q
May 06, 2016

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

FORM 10-Q

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the period ended **March 31, 2016**

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 **0-11204**

AmeriServ Financial, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania	25-1424278
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

15907-0430

Main & Franklin Streets,
P.O. Box 430, Johnstown, PA
(Address of principal executive offices) (Zip Code)
Registrant's telephone number, including area code **(814) 533-5300**

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 o

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

Indicate by check mark whether the registrant is a large accelerated filer, accelerated filer, non-accelerated filer or a smaller reporting company. See definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at May 2, 2016
Common Stock, par value $0.01	18,896,876

TABLE OF CONTENTS

AmeriServ Financial, Inc.

INDEX

	Page No.
PART I.	
FINANCIAL INFORMATION:	
Item 1.	
Financial Statements	
Consolidated Balance Sheets (Unaudited) March 31, 2016 and December 31, 2015	1
Consolidated Statements of Operations (Unaudited) Three months ended March 31, 2016 and 2015	2
Consolidated Statements of Comprehensive Income (Unaudited) Three months ended March 31, 2016 and 2015	3
Consolidated Statements of Cash Flows (Unaudited) Three months ended March 31, 2016 and 2015	4
Notes to Unaudited Consolidated Financial Statements	5
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	27
Item 3. Quantitative and Qualitative Disclosure About Market Risk	38
Item 4. Controls and Procedures	38
PART II.	
OTHER INFORMATION	
Item 1. Legal Proceedings	39
Item 1A. Risk Factors	39
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	39
Item 3. Defaults Upon Senior Securities	39

Item 4.
39
Mine Safety Disclosures
Item 5.
39
Other Information
Item 6.
39
Exhibits

i

TABLE OF CONTENTS

Item 1. Financial Statements

AmeriServ Financial, Inc.

CONSOLIDATED BALANCE SHEETS
(In thousands except shares)
(Unaudited)

	March 31, 2016	December 31, 2015
ASSETS		
Cash and due from depository institutions	$18,067	$23,443
Interest bearing deposits	2,796	6,960
Short-term investments in money market funds	2,760	18,107
Total cash and cash equivalents	23,623	48,510
Investment securities:		
Available for sale	115,742	119,467
Held to maturity (fair value $23,800 on March 31, 2016 and $21,533 on December 31, 2015)	23,258	21,419
Loans held for sale	2,438	3,003
Loans	880,496	881,541
Less: Unearned income	524	557
Allowance for loan losses	9,520	9,921
Net loans	870,452	871,063
Premises and equipment, net	11,899	12,108
Accrued interest income receivable	3,295	3,057
Goodwill	11,944	11,944
Bank owned life insurance	37,396	37,228
Net deferred tax asset	9,560	8,993
Federal Home Loan Bank stock	4,647	4,628
Federal Reserve Bank stock	2,125	2,125
Other assets	5,322	4,952
TOTAL ASSETS	$1,121,701	$1,148,497
LIABILITIES		
Non-interest bearing deposits	$180,348	$188,947
Interest bearing deposits	726,425	714,347
Total deposits	906,773	903,294
Short-term borrowings	39,952	48,748
Advances from Federal Home Loan Bank	49,000	48,000
Guaranteed junior subordinated deferrable interest debentures, net	12,896	12,892
Subordinated debt, net	7,424	7,418
Total borrowed funds	109,272	117,058
Other liabilities	8,067	9,172
TOTAL LIABILITIES	1,024,112	1,029,524

SHAREHOLDERS EQUITY		
Preferred stock, no par value; $1,000 per share liquidation preference; 2,000,000 shares authorized; 21,000 shares issued and outstanding on December 31, 2015		21,000
Common stock, par value $0.01 per share; 30,000,000 shares authorized; 26,512,380 shares issued and 18,894,561 outstanding on March 31, 2016; 26,488,630 shares issued and 18,870,811 outstanding on December 31, 2015	265	265
Treasury stock at cost, 7,617,819 shares on March 31, 2016 and December 31, 2015	(74,829)	(74,829)
Capital surplus	145,496	145,441
Retained earnings	33,181	34,651
Accumulated other comprehensive loss, net	(6,524)	(7,555)
TOTAL SHAREHOLDERS EQUITY	97,589	118,973
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$1,121,701	$1,148,497

See accompanying notes to unaudited consolidated financial statements.

1

TABLE OF CONTENTS

AmeriServ Financial, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Three months ended March 31,	
	2016	2015
INTEREST INCOME		
Interest and fees on loans	$ 9,465	$ 9,456
Interest bearing deposits	7	2
Short-term investments in money market funds	10	2
Investment securities:		
Available for sale	767	913
Held to maturity	173	150
Total Interest Income	10,422	10,523
INTEREST EXPENSE		
Deposits	1,254	1,174
Short-term borrowings	42	10
Advances from Federal Home Loan Bank	159	125
Guaranteed junior subordinated deferrable interest debentures	280	280
Subordinated debt	129	
Total Interest Expense	1,864	1,589
NET INTEREST INCOME	8,558	8,934
Provision for loan losses	3,100	250
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	5,458	8,684
NON-INTEREST INCOME		
Trust and investment advisory fees	2,075	2,056
Service charges on deposit accounts	415	419
Net gains on sale of loans	107	191
Mortgage related fees	63	115
Net realized gains on investment securities	57	
Bank owned life insurance	167	363
Other income	553	568
Total Non-Interest Income	3,437	3,712
NON-INTEREST EXPENSE		
Salaries and employee benefits	6,166	6,073
Net occupancy expense	737	841
Equipment expense	436	466
Professional fees	1,465	1,211
Supplies, postage and freight	195	178
Miscellaneous taxes and insurance	291	297
Federal deposit insurance expense	179	167
Other expense	1,242	1,177
Total Non-Interest Expense	10,711	10,410

PRETAX INCOME (LOSS)	(1,816)	1,986
Provision (benefit) for income tax expense	(549)	617
NET INCOME (LOSS)	(1,267)	1,369
Preferred stock dividends	15	53
NET INCOME (LOSS) AVAILABLE TO COMMON SHAREHOLDERS	$ (1,282)	$ 1,316
PER COMMON SHARE DATA:		
Basic:		
Net income (loss)	$ (0.07)	$ 0.07
Average number of shares outstanding	18,884	18,851
Diluted:		
Net income (loss)	$ (0.07)	$ 0.07
Average number of shares outstanding	18,884	18,909
Cash dividends declared	$ 0.01	$ 0.01

See accompanying notes to unaudited consolidated financial statements.

2

TABLE OF CONTENTS

AmeriServ Financial, Inc.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands)
(Unaudited)

	Three Months Ended March 31,	
	2016	2015
COMPREHENSIVE INCOME (LOSS)		
Net income (loss)	$(1,267)	$ 1,369
Other comprehensive income, before tax:		
Pension obligation change for defined benefit plan	504	655
Income tax effect	(171)	(223)
Unrealized holding losses on available for sale securities arising during period	1,115	346
Income tax effect	(379)	(117)
Reclassification adjustment for gains on available for sale securities included in net income	(57)	
Income tax effect	19	
Other comprehensive income	1,031	661
Comprehensive income (loss)	$(236)	$ 2,030

See accompanying notes to unaudited consolidated financial statements.

TABLE OF CONTENTS

AmeriServ Financial, Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three months ended March 31,	
	2016	2015
OPERATING ACTIVITIES		
Net income	$(1,267)	$1,369
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Provision for loan losses	3,100	250
Depreciation expense	445	456
Net amortization of investment securities	87	85
Net realized gains on investment securities available for sale	(57)	
Net gains on loans held for sale	(107)	(191)
Amortization of deferred loan fees	(74)	(67)
Origination of mortgage loans held for sale	(7,226)	(11,764)
Sales of mortgage loans held for sale	7,898	13,431
Increase in accrued interest income receivable	(238)	(173)
Decrease in accrued interest payable	(167)	(161)
Earnings on bank owned life insurance	(167)	(171)
Deferred income taxes	(976)	285
Amortization of deferred issuance costs	10	
Stock based compensation expense	55	132
Other, net	(912)	(696)
Net cash provided by operating activities	404	2,785
INVESTING ACTIVITIES		
Purchases of investment securities available for sale	(6,128)	
Purchases of investment securities held to maturity	(2,107)	
Proceeds from sales of investment securities available for sale	4,248	
Proceeds from maturities of investment securities available for sale	6,649	4,852
Proceeds from maturities of investment securities held to maturity	253	350
Purchases of regulatory stock	(4,929)	(3,878)
Proceeds from redemption of regulatory stock	4,910	4,425
Long-term loans originated	(52,432)	(68,544)
Principal collected on long-term loans	48,974	41,248
Loans purchased or participated	(3,995)	(4,000)
Loans sold or participated	5,000	7,755
Proceeds from sale of other real estate owned	13	53
Proceeds from life insurance policy		200
Purchases of premises and equipment	(227)	(220)
Net cash used in investing activities	229	(17,759)
FINANCING ACTIVITIES		

Net increase in deposit balances	3,479	22,722
Net decrease in other short-term borrowings	(8,796)	(11,661)
Principal borrowings on advances from Federal Home Loan Bank	2,000	2,000
Principal repayments on advances from Federal Home Loan Bank	(1,000)	
Preferred stock redemption	(21,000)	
Common stock dividends	(188)	(188)
Preferred stock dividends	(15)	(53)
Net cash provided by financing activities	(25,520)	12,820
NET DECREASE IN CASH AND CASH EQUIVALENTS	(24,887)	(2,154)
CASH AND CASH EQUIVALENTS AT JANUARY 1	48,510	32,872
CASH AND CASH EQUIVALENTS AT MARCH 31	$23,623	$30,718

See accompanying notes to unaudited consolidated financial statements.

4

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. Principles of Consolidation

The accompanying consolidated financial statements include the accounts of AmeriServ Financial, Inc. (the Company) and its wholly-owned subsidiaries, AmeriServ Financial Bank (the Bank), AmeriServ Trust and Financial Services Company (the Trust Company), and AmeriServ Life Insurance Company (AmeriServ Life). The Bank is a Pennsylvania state-chartered full service bank with 16 locations in Pennsylvania. The Trust Company offers a complete range of trust and financial services and administers assets valued at $2.0 billion that are not reported on the Company s balance sheet at March 31, 2016. AmeriServ Life is a captive insurance company that engages in underwriting as a reinsurer of credit life and disability insurance.

In addition, the Parent Company is an administrative group that provides support in such areas as audit, finance, investments, loan review, general services, and marketing. Significant intercompany accounts and transactions have been eliminated in preparing the consolidated financial statements.

2. Basis of Preparation

The unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information. In the opinion of management, all adjustments consisting of normal recurring entries considered necessary for a fair presentation have been included. They are not, however, necessarily indicative of the results of consolidated operations for a full-year.

For further information, refer to the consolidated financial statements and accompanying notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2015.

3. Recent Accounting Pronouncements

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. This Update applies to all entities that hold financial assets or owe financial liabilities and is intended to provide more useful information on the recognition, measurement, presentation, and disclosure of financial instruments. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. All entities that are not public business entities may adopt the amendments in this Update earlier as of the fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company is currently evaluating the impact the adoption of the standard will have on the Company s financial position or results of operations.

4. Earnings Per Common Share

Basic earnings per share include only the weighted average common shares outstanding. Diluted earnings per share include the weighted average common shares outstanding and any potentially dilutive common stock equivalent shares in the calculation. Treasury shares are excluded for earnings per share purposes. Due to the net loss as of March

31, 2016, all options to purchase common shares were not included in the computation of diluted earnings per common share because to do so would be antidilutive. Options to purchase 198,888 common shares, at exercise prices ranging from $2.98 to $4.70, were outstanding as of March 31, 2015, but were not included in the computation of diluted earnings per common share because to do so would be antidilutive. Dividends on preferred shares are deducted from net income in the calculation of earnings per common share.

5

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

4. Earnings Per Common Share (continued)

	Three months ended March 31,	
	2016	2015
	(In thousands, except per share data)	
Numerator:		
Net income (loss)	$ (1,267)	$ 1,369
Preferred stock dividends	15	53
Net income (loss) available to common shareholders	$ (1,282)	$ 1,316
Denominator:		
Weighted average common shares outstanding (basic)	18,884	18,851
Effect of stock options		58
Weighted average common shares outstanding (diluted)	18,884	18,909
Earnings (loss) per common share:		
Basic	$ (0.07)	$ 0.07
Diluted	(0.07)	0.07

5. Consolidated Statement of Cash Flows

On a consolidated basis, cash and cash equivalents include cash and due from depository institutions, interest-bearing deposits and short-term investments in money market funds**.** The Company made $438,500 in income tax payments in the first three months of 2016 and $331,000 in the same 2015 period. The Company made total interest payments of $2,031,000 in the first three months of 2016 compared to $1,750,000 in the same 2015 period. The Company had $38,000 non-cash transfers to other real estate owned (OREO) in the first three months of 2016 compared to $107,000 non-cash transfers in the same 2015 period.

6. Investment Securities

The cost basis and fair values of investment securities are summarized as follows (in thousands):

Investment securities available for sale (AFS):

	March 31, 2016			
	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
US Agency	$ 1,900	$ 2	$ (1)	$ 1,901
US Agency mortgage-backed securities	92,053	2,514	(59)	94,508

Corporate bonds	19,506	101	(274)	19,333
Total	$ 113,459	$ 2,617	$ (334)	$ 115,742

Investment securities held to maturity (HTM):

	March 31, 2016			
	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
US Agency mortgage-backed securities	$ 12,672	$ 408	$	$ 13,080
Taxable municipal	5,586	175	(2)	5,759
Corporate bonds and other securities	5,000	27	(66)	4,961
Total	$ 23,258	$ 610	$ (68)	$ 23,800

6

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

6. Investment Securities (continued)

Investment securities available for sale (AFS):

	December 31, 2015			
	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
US Agency	$ 2,900	$	$ (19)	$ 2,881
US Agency mortgage backed securities	96,801	1,975	(442)	98,334
Corporate bonds	18,541	18	(307)	18,252
Total	$ 118,242	$ 1,993	$ (768)	$ 119,467

Investment securities held to maturity (HTM):

	December 31, 2015			
	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
US Agency mortgage-backed securities	$ 10,827	$ 247	$ (53)	$ 11,021
Taxable municipal	5,592	67	(65)	5,594
Corporate bonds and other securities	5,000	3	(85)	4,918
Total	$ 21,419	$ 317	$ (203)	$ 21,533

Maintaining investment quality is a primary objective of the Company s investment policy which, subject to certain limited exceptions, prohibits the purchase of any investment security below a Moody s Investor s Service or Standard & Poor s rating of A. At March 31, 2016, 78.0% of the portfolio was rated AAA as compared to 79.1% at December 31, 2015. Approximately 5.8% of the portfolio was either rated below A or unrated at March 31, 2016 as compared to 5.7% at December 31, 2015.

The Company sold $4.2 million AFS securities in the first quarter of 2016 resulting in $63,000 of gross investment security gains and $6,000 of gross investment security losses. The Company had no investment security sales for the first three months of 2015.

The book value of securities, both available for sale and held to maturity, pledged to secure public and trust deposits, and certain Federal Home Loan Bank borrowings was $99,376,000 at March 31, 2016 and $87,096,000 at December 31, 2015.

The following tables present information concerning investments with unrealized losses as of March 31, 2016 and December 31, 2015 (in thousands):

Total investment securities:

	March 31, 2016					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
US Agency	$	$	$399	$ (1)	$399	$ (1)
Taxable municipal	832	(2)			832	(2)
US Agency mortgage-backed securities	1,795	(13)	7,166	(46)	8,961	(59)
Corporate bonds and other securities	6,869	(130)	6,789	(210)	13,658	(340)
Total	$9,496	$ (145)	$14,354	$ (257)	$23,850	$ (402)

7

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

6. Investment Securities (continued)

Total investment securities:

	December 31, 2015					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
US Agency	$1,486	$ (14)	$395	$ (5)	$1,881	$ (19)
US Agency mortgage-backed securities	33,359	(245)	9,088	(250)	42,447	(495)
Taxable municipal	3,617	(65)			3,617	(65)
Corporate bonds and other securities	8,884	(160)	7,766	(232)	16,650	(392)
Total	$47,346	$ (484)	$17,249	$ (487)	$64,595	$ (971)

The unrealized losses are primarily a result of increases in market yields from the time of purchase. In general, as market yields rise, the value of securities will decrease; as market yields fall, the fair value of securities will increase. There are 24 positions that are considered temporarily impaired at March 31, 2016. Management generally views changes in fair value caused by changes in interest rates as temporary; therefore, these securities have not been classified as other-than-temporarily impaired. Management has also concluded that based on current information we expect to continue to receive scheduled interest payments as well as the entire principal balance. Furthermore, management does not intend to sell these securities and does not believe it will be required to sell these securities before they recover in value.

Contractual maturities of securities at March 31, 2016 are shown below (in thousands). Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without prepayment penalties. The duration of the total investment securities portfolio at March 31, 2016 is 29.8 months and is lower than the duration at December 31, 2015 which was 34.2 months. The duration remains within our internal established guideline range of 24 to 42 months which we believe is appropriate to maintain proper levels of liquidity, interest rate risk, market valuation sensitivity and profitability.

Total investment securities:

	March 31, 2016			
	Available for sale		Held to maturity	
	Cost Basis	Fair Value	Cost Basis	Fair Value
Within 1 year	$ 1,999	$ 1,987	$ 1,000	$ 997
After 1 year but within 5 years	9,453	9,471	2,000	1,957
After 5 years but within 10 years	31,662	32,454	7,600	7,763
After 10 years but within 15 years	35,830	36,652	2,110	2,124

Over 15 years	34,515	35,178	10,548	10,959
Total	$ 113,459	$ 115,742	$ 23,258	$ 23,800

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

7. Loans

The loan portfolio of the Company consists of the following (in thousands):

	March 31, 2016	December 31, 2015
Commercial	$ 181,515	$ 181,066
Commercial loans secured by real estate	425,265	421,637
Real estate mortgage	253,565	257,937
Consumer	19,627	20,344
Loans, net of unearned income	$ 879,972	$ 880,984

Loan balances at March 31, 2016 and December 31, 2015 are net of unearned income of $524,000 and $557,000, respectively. Real estate-construction loans comprised 2.4% and 3.0% of total loans, net of unearned income at March 31, 2016 and December 31, 2015, respectively.

8. Allowance for Loan Losses

The following tables summarize the rollforward of the allowance for loan losses by portfolio segment for the three month periods ending March 31, 2016 and 2015 (in thousands).

	Three months ended March 31, 2016				
	Balance at December 31, 2015	Charge-Offs	Recoveries	Provision (Credit)	Balance at March 31, 2016
Commercial	$ 4,244	$ (3,339)	$ 7	$ 2,655	$ 3,567
Commercial loans secured by real estate	3,449		28	229	3,706
Real estate mortgage	1,173	(38)	42	(20)	1,157
Consumer	151	(205)	4	195	145
Allocation for general risk	904			41	945
Total	$ 9,921	$ (3,582)	$ 81	$ 3,100	$ 9,520

	Three months ended March 31, 2015				
	Balance at December 31,	Charge-Offs	Recoveries	Provision (Credit)	Balance at March 31, 2015

2014					
Commercial	$ 3,262	$ (121)	$ 6	$ 10	$ 3,157
Commercial loans secured by real estate	3,902		42	143	4,087
Real estate mortgage	1,310	(103)	30	67	1,304
Consumer	190	(47)	9	39	191
Allocation for general risk	959			(9)	950
Total	$ 9,623	$ (271)	$ 87	$ 250	$ 9,689

The substantially higher than typical provision in the first quarter of 2016 for the commercial portfolio was necessary to resolve the Company s only meaningful direct loan exposure to the energy industry. These loans are related to a single borrower in the fracking industry who had filed for bankruptcy protection in the fourth quarter of 2015. With the bankruptcy recently changing from Chapter 11 (reorganization) to Chapter 7 (liquidation) late in the first quarter of 2016, the Company concluded that its previously established reserves on these non-accrual loans were not sufficient to cover the discounted collateral values that will result from the liquidation process. As a result of this action, the Company also experienced heightened net loan charge-offs.

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

The following tables summarize the loan portfolio and allowance for loan loss by the primary segments of the loan portfolio (in thousands).

	At March 31, 2016					
	Commercial	Commercial Loans Secured by Real Estate	Real Estate-Mortgage	Consumer	Allocation for General Risk	Total
Loans:						
Individually evaluated for impairment	$1,053	$363	$	$		$1,416
Collectively evaluated for impairment	180,462	424,902	253,565	19,627		878,556
Total loans	$181,515	$425,265	$253,565	$19,627		$879,972
Allowance for loan losses:						
Specific reserve allocation	$573	$61	$	$	$	$634
General reserve allocation	2,994	3,645	1,157	145	945	8,886
Total allowance for loan losses	$3,567	$3,706	$1,157	$145	$ 945	$9,520

	At December 31, 2015					
	Commercial	Commercial Loans Secured by Real Estate	Real Estate-Mortgage	Consumer	Allocation for General Risk	Total
Loans:						
Individually evaluated for impairment	$4,416	$86	$	$		$4,502
Collectively evaluated for impairment	176,650	421,551	257,937	20,344		876,482
Total loans	$181,066	$421,637	$257,937	$20,344		$880,984
Allowance for loan losses:						
Specific reserve allocation	$1,387	$	$	$	$	$1,387
General reserve allocation	2,857	3,449	1,173	151	904	8,534
Total allowance for loan losses	$4,244	$3,449	$1,173	$151	$ 904	$9,921

The segments of the Company s loan portfolio are disaggregated to a level that allows management to monitor risk and performance. The loan segments used are consistent with the internal reports evaluated by the Company s management and Board of Directors to monitor risk and performance within various segments of its loan portfolio and therefore, no

further disaggregation into classes is necessary. The overall risk profile for the commercial loan segment is impacted by non-owner occupied CRE loans, which include loans secured by non-owner occupied nonfarm nonresidential properties, as a meaningful but declining portion of the commercial portfolio is centered in these types of accounts. The residential mortgage loan segment is comprised of first lien amortizing residential mortgage loans and home equity loans secured by residential real estate. The consumer loan segment consists primarily of installment loans and overdraft lines of credit connected with customer deposit accounts.

Management evaluates for possible impairment any individual loan in the commercial or commercial real estate segment with a loan balance in excess of $100,000 that is in nonaccrual status or classified as a Troubled Debt Restructure (TDR). Loans are considered to be impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in evaluating impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

delay, the borrower s prior payment record, and the amount of the shortfall in relation to the principal and interest owed. The Company does not separately evaluate individual consumer and residential mortgage loans for impairment, unless such loans are part of a larger relationship that is impaired, or are classified as a TDR.

Once the determination has been made that a loan is impaired, the determination of whether a specific allocation of the allowance is necessary is measured by comparing the recorded investment in the loan to the fair value of the loan using one of three methods: (a) the present value of expected future cash flows discounted at the loan s effective interest rate; (b) the loan s observable market price; or (c) the fair value of the collateral less selling costs for collateral dependent loans. The method is selected on a loan-by-loan basis, with management primarily utilizing the fair value of collateral method. The evaluation of the need and amount of a specific allocation of the allowance and whether a loan can be removed from impairment status is made on a quarterly basis. The Company s policy for recognizing interest income on impaired loans does not differ from its overall policy for interest recognition.

The need for an updated appraisal on collateral dependent loans is determined on a case-by-case basis. The useful life of an appraisal or evaluation will vary depending upon the circumstances of the property and the economic conditions in the marketplace. A new appraisal is not required if there is an existing appraisal which, along with other information, is sufficient to determine a reasonable value for the property and to support an appropriate and adequate allowance for loan losses. At a minimum, annual documented reevaluation of the property is completed by the Bank s internal Assigned Risk Department to support the value of the property.

When reviewing an appraisal associated with an existing collateral real estate dependent transaction, the Bank s internal Assigned Risk Department must determine if there have been material changes to the underlying assumptions in the appraisal which affect the original estimate of value. Some of the factors that could cause material changes to reported values include:

- the passage of time;
- the volatility of the local market;
- the availability of financing;
- natural disasters;
- the inventory of competing properties;
- new improvements to, or lack of maintenance of, the subject property or competing properties upon physical inspection by the Bank;
- changes in underlying economic and market assumptions, such as material changes in current and projected vacancy, absorption rates, capitalization rates, lease terms, rental rates, sales prices, concessions, construction overruns and delays, zoning changes, etc.; and/or
- environmental contamination.

The value of the property is adjusted to appropriately reflect the above listed factors and the value is discounted to reflect the value impact of a forced or distressed sale, any outstanding senior liens, any outstanding unpaid real estate taxes, transfer taxes and closing costs that would occur with sale of the real estate. If the Assigned Risk Department personnel determine that a reasonable value cannot be derived based on available information, a new appraisal is ordered. The determination of the need for a new appraisal, versus completion of a property valuation by the Bank s

Assigned Risk Department personnel rests with the Assigned Risk Department and not the originating account officer.

11

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

The following tables present impaired loans by class, segregated by those for which a specific allowance was required and those for which a specific allowance was not necessary (in thousands).

	March 31, 2016				
	Impaired Loans with Specific Allowance		Impaired Loans with no Specific Allowance	Total Impaired Loans	
	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	Unpaid Principal Balance
Commercial	$ 806	$ 573	$ 247	$ 1,053	$ 1,061
Commercial loans secured by real estate	302	61	61	363	786
Total impaired loans	$ 1,108	$ 634	$ 308	$ 1,416	$ 1,847

	December 31, 2015				
	Impaired Loans with Specific Allowance		Impaired Loans with no Specific Allowance	Total Impaired Loans	
	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	Unpaid Principal Balance
Commercial	$ 4,416	$ 1,387	$	$ 4,416	$ 4,421
Commercial loans secured by real estate			86	86	522
Total impaired loans	$ 4,416	$ 1,387	$ 86	$ 4,502	$ 4,943

The following table presents the average recorded investment in impaired loans and related interest income recognized for the periods indicated (in thousands).

	Three months ended March 31,	
	2016	2015
Average loan balance:		
Commercial	$ 1,162	$ 102
Commercial loans secured by real estate	615	901
Average investment in impaired loans	$ 1,777	$ 1,003
Interest income recognized:		
Commercial	$ 3	$ 1

Commercial loans secured by real estate		6
Interest income recognized on a cash basis on impaired loans	$ 3	$ 7

Management uses a nine point internal risk rating system to monitor the credit quality of the overall loan portfolio. The first six categories are considered not criticized. The first five Pass categories are aggregated, while the Pass-6, Special Mention, Substandard and Doubtful categories are disaggregated to separate pools. The criticized rating categories utilized by management generally follow bank regulatory definitions. The Special Mention category includes assets that are currently protected but are potentially weak, resulting in an undue and unwarranted credit risk, but not to the point of justifying a Substandard classification. Loans in the Substandard category have well-defined weaknesses that jeopardize the liquidation of the debt, and have a distinct possibility that some loss will be sustained if the weaknesses are not corrected. All loans greater than 90 days past due, or for which any portion of the loan represents a specific allocation of the allowance for loan losses are placed in Substandard or Doubtful.

To help ensure that risk ratings are accurate and reflect the present and future capacity of borrowers to repay a loan as agreed, the Company has a structured loan rating process, which dictates that, at a minimum, credit reviews are mandatory for all commercial and commercial mortgage loan relationships with aggregate balances in excess of $250,000 within a 12-month period. Generally, consumer and residential mortgage loans are included in the Pass categories unless a specific action, such as bankruptcy, delinquency, or death occurs

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

to raise awareness of a possible credit event. The Company s commercial relationship managers are responsible for the timely and accurate risk rating of the loans in their portfolios at origination and on an ongoing basis. Risk ratings are assigned by the account officer, but require independent review and rating concurrence from the Company s internal Loan Review Department. The Loan Review Department is an experienced independent function which reports directly to the Board s Audit Committee. The scope of commercial portfolio coverage by the Loan Review Department is defined and presented to the Audit Committee for approval on an annual basis. The approved scope of coverage for 2016 requires review of a minimum range of 50% to 55% of the commercial loan portfolio.

In addition to loan monitoring by the account officer and Loan Review Department, the Company also requires presentation of all credits rated Pass-6 with aggregate balances greater than $1,000,000, all credits rated Special Mention or Substandard with aggregate balances greater than $250,000, and all credits rated Doubtful with aggregate balances greater than $100,000 on an individual basis to the Company s Loan Loss Reserve Committee on a quarterly basis. Additionally, the Asset Quality Task Force, which is a group comprised of senior level personnel, meets monthly to monitor the status of problem loans.

The following table presents the classes of the commercial and commercial real estate loan portfolios summarized by the aggregate Pass and the criticized categories of Special Mention, Substandard and Doubtful within the internal risk rating system (in thousands).

	March 31, 2016				
	Pass	Special Mention	Substandard	Doubtful	Total
Commercial	$ 178,520	$ 793	$ 1,955	$ 247	$ 181,515
Commercial loans secured by real estate	415,949	7,764	1,533	19	425,265
Total	$ 594,469	$ 8,557	$ 3,488	$ 266	$ 606,780

	December 31, 2015				
	Pass	Special Mention	Substandard	Doubtful	Total
Commercial	$ 174,616	$ 1,811	$ 3,318	$ 1,321	$ 181,066
Commercial loans secured by real estate	416,331	3,100	2,188	18	421,637
Total	$ 590,947	$ 4,911	$ 5,506	$ 1,339	$ 602,703

It is generally the policy of the Bank that the outstanding balance of any residential mortgage loan that exceeds 90-days past due as to principal and/or interest is transferred to non-accrual status and an evaluation is completed to determine the fair value of the collateral less selling costs, unless the balance is minor. A charge down is recorded for any deficiency balance determined from the collateral evaluation. The remaining non-accrual balance is reported as impaired with no specific allowance. It is the policy of the bank that the outstanding balance of any consumer loan that exceeds 90-days past due as to principal and/or interest is charged off. The following tables present the performing and non-performing outstanding balances of the residential and consumer portfolios (in thousands).

	March 31, 2016	
	Performing	Non-Performing
Real estate-mortgage	$ 252,478	$ 1,087
Consumer	19,627	
Total	$ 272,105	$ 1,087

	December 31, 2015	
	Performing	Non-Performing
Real estate-mortgage	$ 256,149	$ 1,788
Consumer	20,344	
Total	$ 276,493	$ 1,788

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by the length of time a recorded payment is past due. The following tables present the classes of the loan portfolio summarized by the aging categories of performing loans and nonaccrual loans (in thousands).

	March 31, 2016						
	Current	30 59 Days Past Due	60 89 Days Past Due	90 Days Past Due	Total Past Due	Total Loans	90 Days Past Due and Still Accruing
Commercial	$180,598	$427	$ 243	$ 247	$917	$181,515	$
Commercial loans secured by real estate	420,538	4,727			4,727	425,265	
Real estate mortgage	249,427	3,005	456	677	4,138	253,565	
Consumer	19,541	84	2		86	19,627	
Total	$870,104	$8,243	$ 701	$ 924	$9,868	$879,972	$

	December 31, 2015						
	Current	30 59 Days Past Due	60 89 Days Past Due	90 Days Past Due	Total Past Due	Total Loans	90 Days Past Due and Still Accruing
Commercial	$176,216	$489	$4,361	$	$4,850	$181,066	$
Commercial loans secured by real estate	421,247	208	182		390	421,637	
Real estate mortgage	254,288	2,658	442	549	3,649	257,937	
Consumer	20,115	67	162		229	20,344	
Total	$871,866	$3,422	$5,147	$ 549	$9,118	$880,984	$

An allowance for loan losses (ALL) is maintained to absorb losses from the loan portfolio. The ALL is based on management s continuing evaluation of the risk characteristics and credit quality of the loan portfolio, assessment of current economic conditions, diversification and size of the portfolio, adequacy of collateral, past and anticipated loss experience, and the amount of non-performing loans.

Loans that are collectively evaluated for impairment are analyzed with general allowances being made as appropriate. For general allowances, historical loss trends are used in the estimation of losses in the current portfolio. These historical loss amounts are complemented by consideration of other qualitative factors.

Management tracks the historical net charge-off activity at each risk rating grade level for the entire commercial portfolio and at the aggregate level for the consumer, residential mortgage and small business portfolios. A historical charge-off factor is calculated utilizing a rolling 12 consecutive historical quarters for the commercial portfolios. This historical charge-off factor for the consumer, residential mortgage and small business portfolios are based on a three year historical average of actual loss experience.

The Company uses a comprehensive methodology and procedural discipline to maintain an ALL to absorb inherent losses in the loan portfolio. The Company believes this is a critical accounting policy since it involves significant estimates and judgments. The allowance consists of three elements: 1) an allowance established on specifically identified problem loans, 2) formula driven general reserves established for loan categories based upon historical loss experience and other qualitative factors which include delinquency, non-performing and TDR loans, loan trends, economic trends, concentrations of credit, trends in loan volume, experience and depth of management, examination and audit results, effects of any changes in lending policies, and trends in policy, financial information, and documentation exceptions, and 3) a general risk reserve which provides support for variance from our assessment of the previously listed qualitative factors, provides protection against credit risks resulting from other inherent risk factors contained in the Company s loan portfolio, and recognizes the model and estimation risk associated with the specific and formula driven

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

allowances. The qualitative factors used in the formula driven general reserves are evaluated quarterly (and revised if necessary) by the Company s management to establish allocations which accommodate each of the listed risk factors.

Pass rated credits are segregated from Criticized and Classified credits for the application of qualitative factors.

Management reviews the loan portfolio on a quarterly basis using a defined, consistently applied process in order to make appropriate and timely adjustments to the ALL. When information confirms all or part of specific loans to be uncollectible, these amounts are promptly charged off against the ALL.

9. Non-performing Assets Including Troubled Debt Restructurings (TDR)

The following table presents information concerning non-performing assets including TDR (in thousands, except percentages):

	March 31, 2016	December 31, 2015
Non-accrual loans		
Commercial	$ 910	$ 4,260
Commercial loans secured by real estate	194	18
Real estate mortgage	1,087	1,788
Total	2,191	6,066
Other real estate owned		
Commercial	570	
Real estate mortgage	102	75
Consumer	1	
Total	673	75
TDR s not in non-accrual	143	156
Total non-performing assets including TDR	$ 3,007	$ 6,297
Total non-performing assets as a percent of loans, net of unearned income, and other real estate owned	0.34 %	0.71 %

The Company had no loans past due 90 days or more for the periods presented which were accruing interest.

The following table sets forth, for the periods indicated, (1) the gross interest income that would have been recorded if non-accrual loans had been current in accordance with their original terms and had been outstanding throughout the period or since origination if held for part of the period, (2) the amount of interest income actually recorded on such loans, and (3) the net reduction in interest income attributable to such loans (in thousands).

	Three months ended March 31,	
	2016	2015
Interest income due in accordance with original terms	$ 59	$ 24
Interest income recorded		
Net reduction in interest income	$ 59	$ 24

Consistent with accounting and regulatory guidance, the Bank recognizes a TDR when the Bank, for economic or legal reasons related to a borrower s financial difficulties, grants a concession to the borrower that would not normally be considered. Regardless of the form of concession granted, the Bank s objective in offering a TDR is to increase the probability of repayment of the borrower s loan.

15

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

9. Non-performing Assets Including Troubled Debt Restructurings (TDR) (continued)

To be considered a TDR, both of the following criteria must be met:

- the borrower must be experiencing financial difficulties; and
- the Bank, for economic or legal reasons related to the borrower s financial difficulties, grants a concession to the borrower that would not otherwise be considered.

Factors that indicate a borrower is experiencing financial difficulties include, but are not limited to:

- the borrower is currently in default on their loan(s);
- the borrower has filed for bankruptcy;
- the borrower has insufficient cash flows to service their loan(s); and
- the borrower is unable to obtain refinancing from other sources at a market rate similar to rates available to a non-troubled debtor.

Factors that indicate that a concession has been granted include, but are not limited to:

- the borrower is granted an interest rate reduction to a level below market rates for debt with similar risk; or
- the borrower is granted a material maturity date extension, or extension of the amortization plan to provide payment relief. For purposes of this policy, a material maturity date extension will generally include any maturity date extension, or the aggregate of multiple consecutive maturity date extensions, that exceed 120 days. A restructuring that results in an insignificant delay in payment, i.e. 120 days or less, is not necessarily a TDR. Insignificant payment delays occur when the amount of the restructured payments subject to the delay is insignificant relative to the unpaid principal or collateral value, and will result in an insignificant shortfall in the originally scheduled contractual amount due, and/or the delay in timing of the restructured payment period is insignificant relative to the frequency of payments, the original maturity or the original amortization.

The determination of whether a restructured loan is a TDR requires consideration of all of the facts and circumstances surrounding the modification. No single factor is determinative of whether a restructuring is a TDR. An overall general decline in the economy or some deterioration in a borrower s financial condition does not automatically mean that the borrower is experiencing financial difficulty. Accordingly, determination of whether a modification is a TDR involves a large degree of judgment.

The Company had no loans modified as TDRs during the three month period ended March 31, 2016.

The following table details the loans modified as TDRs during the three month period ended March 31, 2015 (dollars in thousands).

Loans in accrual status	# of Loans	Current Balance	Concession Granted
Commercial loan	1	$ 204	Extension of maturity date

In all instances where loans have been modified in troubled debt restructurings the pre- and post-modified balances are the same. The specific ALL reserve for loans modified as TDR s was $24,000 and $502,000 as of March 31, 2016 and 2015, respectively. All TDR s are individually evaluated for impairment and a related allowance is recorded, as needed.

Once a loan is classified as a TDR, this classification will remain until documented improvement in the financial position of the borrower supports confidence that all principal and interest will be paid according to terms. Additionally, the customer must have re-established a track record of timely payments according to the restructured contract terms for a minimum of six consecutive months prior to consideration for removing the

16

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

9. Non-performing Assets Including Troubled Debt Restructurings (TDR) (continued)

loan from non-accrual TDR status. However, a loan will continue to be on non-accrual status until, consistent with our policy, the borrower has made a minimum of an additional six consecutive monthly payments in accordance with the terms of the loan.

The Company had no loans that were classified as TDR s or were subsequently modified during each 12-month period prior to the current reporting periods, which begin January 1, 2015 and 2014, respectively, and that subsequently defaulted during these reporting periods.

The Company is unaware of any additional loans which are required to either be charged-off or added to the non-performing asset totals disclosed above.

10. Federal Home Loan Bank Borrowings

Total Federal Home Loan Bank (FHLB) borrowings and advances consist of the following (in thousands, except percentages):

	At March 31, 2016			
Type	Maturing	Amount	Weighted Average Rate	
Open Repo Plus	Overnight	$ 39,952	0.57	%
Advances	2016	11,000	0.83	
	2017	12,000	1.06	
	2018	12,000	1.48	
	2019	8,000	1.67	
	2020 and over	6,000	1.68	
Total advances		49,000	1.29	
Total FHLB borrowings		$ 88,952	0.97	%

	At December 31, 2015			
Type	Maturing	Amount	Weighted Average Rate	
Open Repo Plus	Overnight	$ 48,748	0.43	%
Advances	2016	12,000	0.81	
	2017	12,000	1.06	

	2018	12,000	1.48	
	2019	7,000	1.73	
	2020 and over	5,000	1.69	
Total advances		48,000	1.27	
Total FHLB borrowings		$ 96,748	0.85	%

The rate on Open Repo Plus advances can change daily, while the rates on the advances are fixed until the maturity of the advance. All FHLB stock along with an interest in certain residential mortgage and CRE loans with an aggregate statutory value equal to the amount of the advances are pledged as collateral to the FHLB of Pittsburgh to support these borrowings.

11. Preferred Stock

On August 11, 2011, pursuant to the Small Business Lending Fund (SBLF), the Company issued and sold to the US Treasury 21,000 shares of its Senior Non-Cumulative Perpetual Preferred Stock, Series E (Series E Preferred Stock) for the aggregate proceeds of $21 million. The SBLF was a voluntary program sponsored by the US Treasury that encouraged small business lending by providing capital to qualified community banks at favorable rates. The Company used the proceeds from the Series E Preferred Stock issued to the US Treasury to repurchase all 21,000 shares of its outstanding preferred shares previously issued to the US Treasury under the Capital Purchase Program.

17

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

11. Preferred Stock (continued)

On January 27, 2016, we redeemed the Series E Preferred Stock, at a redemption price of 100% of the liquidation amount plus accrued but unpaid dividends, after receiving approval from our federal banking regulator and the US Treasury.

12. Accumulated Other Comprehensive Loss

The following table presents the changes in each component of accumulated other comprehensive loss, net of tax, for the three months ended March 31, 2016 and 2015 (in thousands):

	Three months ended March 31, 2016			Three months ended March 31, 2015		
	Net Unrealized Gains and (Losses) on Investment Securities AFS[1]	Defined Benefit Pension Items[1]	Total[1]	Net Unrealized Gains and (Losses) on Investment Securities AFS[1]	Defined Benefit Pension Items[1]	Total[1]
Beginning balance	$808	$(8,363)	$(7,555)	$1,843	$(8,745)	$(6,902)
Other comprehensive income before reclassifications	736	333	1,069	229	432	661
Amounts reclassified from accumulated other comprehensive loss	(38)		(38)			
Net current period other comprehensive income	698	333	1,031	229	432	661
Ending balance	$1,506	$(8,030)	$(6,524)	$2,072	$(8,313)	$(6,241)

(1) Amounts in parentheses indicate debits on the Consolidated Balance Sheets.

The following table presents the amounts reclassified out of each component of accumulated other comprehensive loss for the three months ended March 31, 2016 and 2015 (in thousands):

	Amount reclassified from accumulated other comprehensive loss[1]		Affected line item in the statement of operations
Details about accumulated other comprehensive loss components	For the three	For the three months	

	months ended March 31, 2016	ended March 31, 2015	
Unrealized gains and losses on sale of securities			
	$ (57)	$	Net realized (gains) losses on investment securities
	19		Provision for income tax expense
	$ (38)	$	Net of tax
Total reclassifications for the period	$ (38)	$	Net income

(1) Amounts in parentheses indicate credits.

18

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

13. Regulatory Capital

The Company is subject to various capital requirements administered by the federal banking agencies. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company must meet specific capital guidelines that involve quantitative measures of the Company s assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Company s capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company s consolidated financial statements.

Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital to risk-weighted assets, Tier 1 capital to average assets, and common equity Tier I capital (as defined in the regulations) to risk-weighted assets (RWA) (as defined). Additionally under Basel III rules, the decision was made to opt-out of including accumulated other comprehensive income in regulatory capital. As of March 31, 2016, the Bank was categorized as Well Capitalized under the regulatory framework for prompt corrective action promulgated by the Federal Reserve. The Company believes that no conditions or events have occurred that would change this conclusion as of such date. To be categorized as Well Capitalized, the Bank must maintain minimum Total Capital, Common Equity Tier 1 Capital, Tier 1 Capital, and Tier 1 leverage ratios as set forth in the table. Additionally, while not a regulatory capital ratio, the Company s tangible common equity ratio was 7.72% at March 31, 2016 (in thousands, except ratios).

	At March 31, 2016					
	Company		Bank		Minimum Required For Capital Adequacy Purposes	To be Well Capitalized Under Prompt Corrective Action Regulations*
	Amount	Ratio	Amount	Ratio	Ratio	Ratio
	(In Thousands, Except Ratios)					
Total Capital (To Risk Weighted Assets)	$120,661	13.11%	$105,065	11.49 %	8.63 %	10.00 %
Tier 1 Common Equity (To Risk Weighted Assets)	91,487	9.94	94,690	10.36	5.13	6.50
Tier 1 Capital (To Risk Weighted Assets)	102,862	11.18	94,690	10.36	6.63	8.00
Tier 1 Capital (To Average Assets)	102,862	9.28	94,690	8.73	4.00	5.00

19

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

13. Regulatory Capital (continued)

	At December 31, 2015					
	Company		Bank		Minimum Required For Capital Adequacy Purposes	To be Well Capitalized Under Prompt Corrective Action Regulations*
	Amount	Ratio	Amount	Ratio	Ratio	Ratio
	(In Thousands, Except Ratios)					
Total Capital (To Risk Weighted Assets)	$144,096	15.55%	$106,890	11.67%	8.00%	10.00%
Tier 1 Common Equity (To Risk Weighted Assets)	93,202	10.06	96,092	10.49	4.50	6.50
Tier 1 Capital (To Risk Weighted Assets)	125,648	13.56	96,092	10.49	6.00	8.00
Tier 1 Capital (To Average Assets)	125,648	11.41	96,092	8.97	4.00	5.00

* Applies to the Bank only.

On July 2, 2013, the Board of Governors of the Federal Reserve System approved final rules that substantially amend the regulatory risk-based capital rules applicable to the Company and the Bank. The final rules implement the Basel III regulatory capital reforms, as well as certain changes required by the Dodd-Frank Act, which will require institutions to, among other things, have more capital and a higher quality of capital by increasing the minimum regulatory capital ratios, and requiring capital buffers. The new rules became effective for the Company and the Bank on January 1, 2015, and have an implementation period that stretches to January 1, 2019. For a more detailed discussion see the Capital Resources section of the MD&A.

14. Segment Results

The financial performance of the Company is also monitored by an internal funds transfer pricing profitability measurement system which produces line of business results and key performance measures. The Company s major business units include retail banking, commercial banking, trust, and investment/parent. The reported results reflect the underlying economics of the business segments. Expenses for centrally provided services are allocated based upon the cost and estimated usage of those services. The businesses are match-funded and interest rate risk is centrally managed and accounted for within the investment/parent business segment. The key performance measure the Company focuses on for each business segment is net income contribution.

Retail banking includes the deposit-gathering branch franchise and lending to both individuals and small businesses. Lending activities include residential mortgage loans, direct consumer loans, and small business commercial loans. Commercial banking to businesses includes commercial loans, and CRE loans. The trust segment contains our wealth management businesses which include the Trust Company and West Chester Capital Advisors (WCCA), our registered investment advisory firm and financial services. Wealth management includes personal trust products and services such as personal portfolio investment management, estate planning and administration, custodial services and pre-need trusts. Also, institutional trust products and services such as 401(k) plans, defined benefit and defined contribution employee benefit plans, and individual retirement accounts are included in this segment. Financial services include the sale of mutual funds, annuities, and insurance products. The wealth management businesses also includes the union collective investment funds, namely the ERECT and BUILD funds which are designed to use union pension dollars in construction projects that utilize union labor. The investment/parent includes the net results of investment securities and borrowing activities, general corporate expenses not allocated to the business segments, interest

20

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

14. Segment Results (continued)

expense on guaranteed junior subordinated deferrable interest debentures, and centralized interest rate risk management. Inter-segment revenues were not material.

The contribution of the major business segments to the Consolidated Statements of Operations for the three months ended March 31, 2016 and 2015 were as follows (in thousands):

	Three months ended March 31, 2016		March 31, 2016
	Total revenue	Net income (loss)	Total assets
Retail banking	$ 6,297	$ 583	$ 355,224
Commercial banking	4,635	(835)	627,477
Trust	2,177	145	5,367
Investment/Parent	(1,114)	(1,160)	133,633
Total	$ 11,995	$ (1,267)	$ 1,121,701

	Three months ended March 31, 2015		December 31, 2015
	Total revenue	Net income (loss)	Total assets
Retail banking	$ 6,524	$ 659	$ 415,008
Commercial banking	4,738	1,291	589,840
Trust	2,167	380	5,263
Investment/Parent	(783)	(961)	138,386
Total	$ 12,646	$ 1,369	$ 1,148,497

15. Commitments and Contingent Liabilities

The Company had various outstanding commitments to extend credit approximating $171.1 million and $170.5 million along with standby letters of credit of $9.0 million and $7.5 million as of March 31, 2016 and December 31, 2015, respectively. The Company s exposure to credit loss in the event of nonperformance by the other party to these commitments to extend credit and standby letters of credit is represented by their contractual amounts. The Bank uses the same credit and collateral policies in making commitments and conditional obligations as for all other lending.

Additionally, the Company is also subject to a number of asserted and unasserted potential claims encountered in the normal course of business. In the opinion of the Company, neither the resolution of these claims nor the funding of these credit commitments will have a material adverse effect on the Company s consolidated financial position, results of operation or cash flows.

21

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

16. Pension Benefits

The Company has a noncontributory defined benefit pension plan covering certain employees who work at least 1,000 hours per year. The participants shall have a vested interest in their accrued benefit after five full years of service. The benefits of the plan are based upon the employee s years of service and average annual earnings for the highest five consecutive calendar years during the final ten year period of employment. Plan assets are primarily debt securities (including US Treasury and Agency securities, corporate notes and bonds), listed common stocks (including shares of AmeriServ Financial, Inc. common stock which is limited to 10% of the plan s assets), mutual funds, and short-term cash equivalent instruments. The net periodic pension cost for the three months ended March 31, 2016 and 2015 were as follows (in thousands):

	Three months ended March 31,	
	2016	2015
Components of net periodic benefit cost		
Service cost	$ 368	$ 400
Interest cost	344	325
Expected return on plan assets	(563)	(525)
Recognized net actuarial loss	314	300
Net periodic pension cost	$ 463	$ 500

The Company implemented a soft freeze of its defined benefit pension plan to provide that non-union employees hired on or after January 1, 2013 and union employees hired on or after January 1, 2014 are not eligible to participate in the pension plan. Instead, such employees are eligible to participate in a qualified 401(k) plan. This change was made to help reduce pension costs in future periods.

17. Disclosures about Fair Value Measurements

The following disclosures establish a hierarchal disclosure framework associated with the level of pricing observability utilized in measuring assets and liabilities at fair value. The three broad levels defined within this hierarchy are as follows:

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

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

Level III: Assets and liabilities that have little to no pricing observability as of the reported date. These items do not have two-way markets and are measured using management s best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation.

Assets and Liability Measured on a Recurring Basis

Securities classified as available for sale are reported at fair value utilizing Level 2 inputs. For these securities, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quoted market spreads, cash flows, the US Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond s terms and conditions, among other things.

The following tables present the assets reported on the Consolidated Balance Sheets at their fair value as of March 31, 2016 and December 31, 2015, by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

22

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

17. Disclosures about Fair Value Measurements (continued)

Assets and liability measured at fair value on a recurring basis are summarized below (in thousands):

	Fair Value Measurements at March 31, 2016 Using			
	Total	(Level 1)	(Level 2)	(Level 3)
US Agency securities	$ 1,901	$	$ 1,901	$
US Agency mortgage-backed securities	94,508		94,508	
Corporate bonds	19,333		19,333	

	Fair Value Measurements at December 31, 2015 Using			
	Total	(Level 1)	(Level 2)	(Level 3)
US Agency securities	$ 2,881	$	$ 2,881	$
US Agency mortgage-backed securities	98,334		98,334	
Corporate bonds	18,252		18,252	

Assets Measured on a Non-recurring Basis

Loans considered impaired are loans for which, based on current information and events, it is probable that the creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. As detailed in the allowance for loan loss footnote, impaired loans are reported at fair value of the underlying collateral if the repayment is expected solely from the collateral. Collateral values are estimated using Level 3 inputs based on observable market data which at times are discounted. At March 31, 2016, impaired loans with a carrying value of $1,416,000 were reduced by a specific valuation allowance totaling $634,000 resulting in a net fair value of $782,000. At December 31, 2015, impaired loans with a carrying value of $989,000 were reduced by a specific valuation allowance totaling $520,000 resulting in a net fair value of $469,000.

Other real estate owned is measured at fair value based on appraisals, less cost to sell at the date of foreclosure. Valuations are periodically performed by management. Income and expenses from operations and changes in valuation allowance are included in the net expenses from OREO.

Assets measured at fair value on a non-recurring basis are summarized below (in thousands, except range data):

	Fair Value Measurements at March 31, 2016 Using			
	Total	(Level 1)	(Level 2)	(Level 3)
Impaired loans	$ 782	$	$	$ 782
Other real estate owned	673			673

	Fair Value Measurements at December 31, 2015 Using			
	Total	(Level 1)	(Level 2)	(Level 3)
Impaired loans	$ 3,115	$	$	$ 3,115
Other real estate owned	75			75

	Quantitative Information About Level 3 Fair Value Measurements			
March 31, 2016	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range (Wgtd Ave)
Impaired loans	$782	Appraisal of collateral(1),(3)	Appraisal adjustments(2)	15% to 20% (18%)
Other real estate owned	673	Appraisal of collateral(1),(3)	Appraisal adjustments(2)	29% to 81% (47%)
			Liquidation expenses	9% to 55% (16%)

23

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

17. Disclosures about Fair Value Measurements (continued)

	Quantitative Information About Level 3 Fair Value Measurements			
December 31, 2015	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range (Wgtd Ave)
Impaired loans	$3,115	Appraisal of collateral(1),(3)	Appraisal adjustments(2)	15% to 20% (17%)
Other real estate owned	75	Appraisal of collateral(1),(3)	Appraisal adjustments(2) Liquidation expenses	23% to 49% (35%) 10% to 59% (25%)

(1) Fair Value is generally determined through independent appraisals of the underlying collateral, which generally include various level 3 inputs which are not identifiable.

(2) Appraisals may be adjusted by management for qualitative factors such as economic conditions.

(3) Includes qualitative adjustments by management and estimated liquidation expenses.

DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

For the Company, as for most financial institutions, approximately 90% of its assets and liabilities are considered financial instruments. Many of the Company s financial instruments, however, lack an available trading market characterized by a willing buyer and willing seller engaging in an exchange transaction. Therefore, significant estimates and present value calculations were used by the Company for the purpose of this disclosure.

Fair values have been determined by the Company using independent third party valuations that use the best available data (Level 2) and an estimation methodology (Level 3) the Company believes is suitable for each category of financial instruments. Management believes that cash, cash equivalents, and loans and deposits with floating interest rates have estimated fair values which approximate the recorded book balances. The estimation methodologies used, the estimated fair values based on US GAAP measurements, and recorded book balances at March 31, 2016 and December 31, 2015, were as follows (in thousands):

	March 31, 2016				
	Carrying Value	Fair Value	(Level 1)	(Level 2)	(Level 3)
FINANCIAL ASSETS:					
Cash and cash equivalents	$23,623	$23,623	$23,623	$	$
Investment securities AFS	115,742	115,742		115,742	
Investment securities HTM	23,258	23,800		20,846	2,954
Regulatory stock	6,772	6,772	6,772		
Loans held for sale	2,438	2,489	2,489		
	870,452	873,976			873,976

Loans, net of allowance for loan loss and unearned income					
Accrued interest income receivable	3,295	3,295	3,295		
Bank owned life insurance	37,396	37,396	37,396		
FINANCIAL LIABILITIES:					
Deposits with no stated maturities	$633,714	$633,714	$633,714	$	$
Deposits with stated maturities	273,059	275,261			275,261
Short-term borrowings	39,952	39,952	39,952		
All other borrowings	69,320	74,278			74,278
Accrued interest payable	1,484	1,484	1,484		

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

17. Disclosures about Fair Value Measurements (continued)

	December 31, 2015				
	Carrying Value	Fair Value	(Level 1)	(Level 2)	(Level 3)
FINANCIAL ASSETS:					
Cash and cash equivalents	$48,510	$48,510	$48,510	$	$
Investment securities AFS	119,467	119,467		119,467	
Investment securities HTM	21,419	21,533		18,608	2,925
Regulatory stock	6,753	6,753	6,753		
Loans held for sale	3,003	3,041	3,041		
Loans, net of allowance for loan loss and unearned income	871,063	869,591			869,591
Accrued interest income receivable	3,057	3,057	3,057		
Bank owned life insurance	37,228	37,228	37,228		
FINANCIAL LIABILITIES:					
Deposits with no stated maturities	$633,751	$633,751	$633,751	$	$
Deposits with stated maturities	269,543	271,909			271,909
Short-term borrowings	48,748	48,748	48,748		
All other borrowings	68,310	71,816			71,816
Accrued interest payable	1,651	1,651	1,651		

The fair value of cash and cash equivalents, regulatory stock, accrued interest income receivable, short-term borrowings, and accrued interest payable are equal to the current carrying value.

The fair value of investment securities is equal to the available quoted market price for similar securities. The fair value measurements consider observable data that may include dealer quoted market spreads, cash flows, the US Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond s terms and conditions, among other things. The Level 3 securities are valued by discounted cash flows using the US Treasury rate for the remaining term of the securities.

Loans held for sale are priced individually at market rates on the day that the loan is locked for commitment with an investor. All loans in the held for sale account conform to Fannie Mae underwriting guidelines, with the specific intent of the loan being purchased by an investor at the predetermined rate structure. Loans in the held for sale account have specific delivery dates that must be executed to protect the pricing commitment (typically a 30, 45, or 60 day lock period).

The net loan portfolio has been valued using a present value discounted cash flow. The discount rate used in these calculations is based upon the treasury yield curve adjusted for non-interest operating costs, credit loss, current market prices and assumed prepayment risk.

The fair value of bank owned life insurance is based upon the cash surrender value of the underlying policies and matches the book value.

Deposits with stated maturities have been valued using a present value discounted cash flow with a discount rate approximating current market for similar assets and liabilities. Deposits with no stated maturities have an estimated fair value equal to both the amount payable on demand and the recorded book balance.

The fair value of all other borrowings is based on the discounted value of contractual cash flows. The discount rates are estimated using rates currently offered for similar instruments with similar remaining maturities.

TABLE OF CONTENTS

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

17. Disclosures about Fair Value Measurements (continued)

Commitments to extend credit and standby letters of credit are financial instruments generally not subject to sale, and fair values are not readily available. The carrying value, represented by the net deferred fee arising from the unrecognized commitment, and the fair value, determined by discounting the remaining contractual fee over the term of the commitment using fees currently charged to enter into similar agreements with similar credit risk, is not considered material for disclosure. The contractual amounts of unfunded commitments are presented in Note 15.

Changes in assumptions or estimation methodologies may have a material effect on these estimated fair values. The Company s remaining assets and liabilities which are not considered financial instruments have not been valued differently than has been customary under historical cost accounting.

18. Accounting Changes

On January 1, 2016, the Company adopted ASU 2015-03, *Interest Imputation of Interest (Subtopic 835-30),* which changed the presentation of debt issuance costs. Whereas in prior periods debt issuance cost related to a recognized debt liability was presented on the balance sheet as an asset of the Company, the amendment requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The new method of accounting for debt issuance cost was adopted in accordance with the Update and comparative financial statements of prior years have been adjusted to apply the new method retrospectively. The guaranteed junior subordinated deferrable interest debentures and subordinated debt financial statement line items for the periods ended March 31, 2016 and December 31, 2015 were affected by this change in accounting principle.

Item 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (M.D.& A.)

.....2016 FIRST QUARTER SUMMARY OVERVIEW..... AmeriServ Financial, Inc. reported a first quarter 2016 loss available to common shareholders of $1,282,000, or ($0.07) per diluted common share, due primarily to an increased provision for loan losses. This net loss is consistent with the information previously disclosed in a Form 8-K filed on March 31, 2016. In the first quarter of 2015, net income available to common shareholders totaled $1,316,000 or $0.07 per diluted common share.

The net loss reported in the first quarter of 2016 was caused by an increased provision for loan losses that was needed to resolve our only meaningful direct loan exposure to the energy industry. In spite of this troubled loan, the Company s overall loan portfolio quality continues to be strong. The other item significantly impacting our financial performance in the first quarter of 2016 was operating expenses increasing at our Trust Company primarily due to additional one-time legal and accounting costs. Several meaningful positive accomplishments occurred during the quarter and included the pay-off of $21 million of SBLF preferred stock, continued year over year growth in both loans and deposits to record levels, and the identification of further non-interest expense savings which will benefit earnings in future quarters. It is fully expected that the negative items responsible for the loss are behind us and the Company should return to more typical profitability levels in the second quarter.

During the first quarter of 2016, it was appropriate for the AmeriServ Board of Directors and the AmeriServ management team to exercise the high degree of discipline that this risk versus reward banking business demands at times. The announcement of the first quarter financial results contained the details concerning a net loss of $1,267,000 or a negative $0.07 per common share. The need for discipline concerned two specific issues that we have now put behind us.

Typically, in recent history, the performance of AmeriServ Trust and Financial Services Company has been highlighted, noting the continuing growth in assets under management and assets under administration. This growth has triggered a steady increase in the net income contribution of the Trust Company. However, this steady growth had placed unavoidable stress on the infrastructure of the Company. Therefore, the management team began to search for solutions. The result was a decision to install a new state of the art software complex provided by one of the largest software companies in the financial industry. Suffice it to say that certain operational flaws appeared during the installation and conversion. Consequently, we reached out to other independent advisors to analyze the specific errors. That process is now over and we are now nearly finished with implementing the recommended solutions. We believe the system is now functioning as expected but it is a fact that the analysis phase and the corrective action phase did elevate the cost of the Trust Company. Fortunately, the issues were in what some of us still refer to as the back room operation areas. Actually, during the corrective actions the Trust Company continued to grow and we believe that the Trust Company will resume the growth pattern of the last five years. It was necessary to solve the shortfalls promptly and we did.

Concurrently in the Bank, we have been working with a local group who has been active in the new shale technology. The collapse in oil prices, which we have seen in the last year or years, has hurt many of these relatively new companies. It is our job to work with local companies for they provide precious jobs in the region. However, oil is an international commodity and this group will not survive. Therefore, with regret, we charged off their loan and this company will cease to exist. Fortunately over 99% of our borrowers continue to pay on schedule and our list of troubled loans remains much better than most banks our size. We must be disciplined to maintain this record and so

we took this difficult but necessary action.

Once again, let us emphasize that it is important to deal with problems. We have dealt with these two problems and now we will resume our emphasis on growth with earnings.

During the first quarter of 2015, we restructured our executive team. The results of these changes were quite positive but we continue to search for an improved level of performance every year. Therefore, during the first quarter of 2016 we placed James Huerth in the role of President and CEO of the Trust Company and added the title of Bank President and CEO to Jeffrey Stopko. Actually, this is merely a return to the structure

TABLE OF CONTENTS

we operated under from 2004 to 2015. It does enable us to benefit from bringing Mr. Huerth s boundless energies into the rapidly growing Trust Company and asks Mr. Stopko to find ways to improve the profitability of the bank.

In the midst of all this, the staff set a new record in loans outstanding and a new record in deposits. We all hear so much about the underperforming economy and the need to fix things. Our conclusion has been quite different from what we read and hear. Our solution is to rely on working harder. We do note that AmeriServ s tangible book value has been increasing at almost a 5% per year compound annual growth rate over the past 5 years. That growth rate puts us in the middle of our peer bank roster.

THREE MONTHS ENDED MARCH 31, 2016 VS. THREE MONTHS ENDED MARCH 31, 2015

.....PERFORMANCE OVERVIEW..... The following table summarizes some of the Company s key performance indicators (in thousands, except per share and ratios).

	Three months ended March 31, 2016	Three months ended March 31, 2015
Net income (loss)	$ (1,267)	$ 1,369
Net income (loss) available to common shareholders	(1,282)	1,316
Diluted earnings (loss) per share	(0.07)	0.07
Return on average assets (annualized)	(0.45)%	0.51 %
Return on average equity (annualized)	(4.86)%	4.80 %

The Company reported a first quarter 2016 net loss available to common shareholders of $1,282,000, or ($0.07) per diluted common share, due primarily to an increased provision for loan losses. In the first quarter of 2015, net income available to common shareholders totaled $1,316,000, or $0.07 per diluted common share. The negative impact of net interest margin compression more than offset continued solid loan and deposit growth and resulted in net interest income decreasing by $376,000. Additionally, the Company s earning s performance was also negatively impacted due to a lower level of non-interest income by $275,000 and a higher level of non-interest expense by $301,000.

.....NET INTEREST INCOME AND MARGIN..... The Company s net interest income represents the amount by which interest income on average earning assets exceeds interest paid on average interest bearing liabilities. Net interest income is a primary source of the Company s earnings, and it is affected by interest rate fluctuations as well as changes in the amount and mix of average earning assets and average interest bearing liabilities. The following table compares the Company s net interest income performance for the first quarter of 2016 to the first quarter of 2015 (in thousands, except percentages):

	Three months ended March 31, 2016	Three months ended March 31, 2015	$ Change	% Change
Interest income	$ 10,422	$ 10,523	$ (101)	(1.0)%
Interest expense	1,864	1,589		