PENNS WOODS BANCORP INC
Form 10-K
March 10, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC. 20549

FORM 10-K

ý ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2015

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (NO FEE REQUIRED)

For the transition period from to

Commission file number 0-17077

PENNS WOODS BANCORP, INC.
(Exact name of registrant as specified in its charter)

Pennsylvania (State or other jurisdiction of incorporation or organization)	23-2226454 (I.R.S. Employer Identification No.)
300 Market Street, P.O. Box 967 Williamsport, Pennsylvania	17703-0967

Registrant's telephone number, including area code (570) 322-1111

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

Title of each class	Name of each exchange which registered
Common Stock, par value $8.33 per share	The NASDAQ Stock Market LLC

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. o Yes ý No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. o Yes ý No

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 ý No o

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 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No o

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. ý

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

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

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

State the aggregate market value of the voting stock held by non-affiliates of the registrant $210,101,151 at June 30, 2015.

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 March 1, 2016
Common Stock, $8.33 Par Value	4,738,166 Shares

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement prepared in connection with its annual meeting of shareholders to be held on April 27, 2016 are incorporated by reference in Part III hereof.

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PART I

ITEM 1 BUSINESS

A. General Development of Business and History

On January 7, 1983, Penns Woods Bancorp, Inc. (the “Company”) was incorporated under the laws of the Commonwealth of Pennsylvania as a bank holding company. In connection with the organization of the Company, Jersey Shore State Bank ("JSSB"), a Pennsylvania state-chartered bank, became a wholly owned subsidiary of the Company. On June 1, 2013 the Company acquired Luzerne Bank ("Luzerne") with Luzerne operating as a subsidiary of the Company (JSSB and Luzerne are collectively referred to as the "Banks"). The Company’s two other wholly-owned subsidiaries are Woods Real Estate Development Company, Inc. and Woods Investment Company, Inc. The Company’s business has consisted primarily of managing and supervising the Banks, and its principal source of income has been dividends paid by the Banks and Woods Investment Company, Inc.

The Banks are engaged in commercial and retail banking which includes the acceptance of time, savings, and demand deposits, the funding of commercial, consumer, and mortgage loans, and safe deposit services. Utilizing a branch office network, ATMs, Internet, and telephone banking delivery channels, the Banks deliver their products and services to the communities they reside in.

In October 2000, JSSB acquired The M Group, Inc. D/B/A The Comprehensive Financial Group (“The M Group”). The M Group, which operates as a subsidiary of JSSB, offers insurance and securities brokerage services. Securities are offered by The M Group through Voya Financial a registered broker-dealer.

Neither the Company nor the Banks anticipate that compliance with environmental laws and regulations will have any material effect on capital expenditures, earnings, or their competitive position. The Banks are not dependent on a single customer or a few customers, the loss of whom would have a material effect on the business of the Banks.

JSSB employed 233 persons, Luzerne employed 71 persons, and The M Group employed 4 persons as of December 31, 2015 in either a full-time or part-time capacity. The Company does not have any employees. The principal officers of the Banks also serve as officers of the Company.

Woods Investment Company, Inc., a Delaware holding company, maintains an investment portfolio that is managed for total return and to fund dividend payments to the Company.

Woods Real Estate Development Company, Inc. serves the Company through its acquisition and ownership of certain properties utilized by the Bank.

We post publicly available reports required to be filed with the SEC on our website, www.jssb.com, as soon as reasonably practicable after filing such reports with the SEC. The required reports are available free of charge through our website. Information available on our website is not part of or incorporated by reference into this Report or any other report filed by this Company with the SEC.

B. Regulation and Supervision

The Company is a registered bank holding company and, as such is subject to the provisions of the Bank Holding Company Act of 1956, as amended (the “BHCA”) and to supervision and examination by the Board of Governors of the Federal Reserve System (the “FRB”). The Banks are also subject to the supervision and examination by the Federal Deposit Insurance Corporation (the “FDIC”), as their primary federal regulator and as the insurer of the Banks' deposits.

The Banks are also regulated and examined by the Pennsylvania Department of Banking and Securities (the "Department").

The insurance activities of The M Group are subject to regulation by the insurance departments of the various states in which The M Group, conducts business including principally the Pennsylvania Department of Insurance. The securities brokerage activities of The M Group are subject to regulation by federal and state securities commissions.

The FRB has issued regulations under the BHCA that require a bank holding company to serve as a source of financial and managerial strength to its subsidiary banks. As a result, the FRB, pursuant to such regulations, may require the Company to stand ready to use its resources to provide adequate capital funds to the Banks during periods of financial stress or adversity. The BHCA requires the Company to secure the prior approval of the FRB before it can acquire all or substantially all of the assets of any bank, or acquire ownership or control of 5% or more of any voting shares of any bank. Such a transaction would also require approval of the Department.

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A bank holding company is prohibited under the BHCA from engaging in, or acquiring direct or indirect control of, more than 5% of the voting shares of any company engaged in non-banking activities unless the FRB, by order or regulation, has found such activities to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Under the BHCA, the FRB has the authority to require a bank holding company to terminate any activity or relinquish control of a non-bank subsidiary (other than a non-bank subsidiary of a bank) upon the FRB's determination that such activity or control constitutes a serious risk to the financial soundness and stability of any bank subsidiary of the bank holding company.

In July 2013, the federal bank regulatory agencies adopted revisions to the agencies' capital adequacy guidelines and prompt corrective action rules, which were designed to enhance such requirements and implement the revised standards of the Basel Committee on Banking Supervision, commonly referred to as Basel III. The final rules generally implement higher minimum capital requirements, add a new common equity tier 1 capital requirement, and establish criteria that instruments must meet to be considered common equity tier 1 capital, additional tier 1 capital or tier 2 capital. The new minimum capital to risk-adjusted assets requirements are a common equity tier 1 capital ratio of 4.5% (6.5% to be considered "well capitalized") and a tier 1 capital ratio of 6.0%, increased from 4.0% (and increased from 6.0% to 8.0% to be considered "well capitalized"); the total capital ratio remains at 8.0% under the new rules (10.0% to be considered "well capitalized"). Under the new rules, in order to avoid limitations on capital distributions (including dividend payments and certain discretionary bonus payments to executive officers), a banking organization must hold a capital conservation buffer comprised of common equity tier 1 capital above its minimum risk-based capital requirements in an amount greater than 2.5% of total risk-weighted assets. The new minimum capital requirements became effective on January 1, 2015. The capital contribution buffer requirements phase in over a three-year period beginning January 1, 2016.

In addition to the risk-based capital guidelines, the FRB requires each bank holding company to comply with the leverage ratio, under which the bank holding company must maintain a minimum level of Tier 1 capital to average total consolidated assets of 4.0% (5.0% to be considered "well capitalized"). The Banks are subject to similar capital requirements adopted by the FDIC.

Dividends

Federal and state laws impose limitations on the payment of dividends by the Banks. The Pennsylvania Banking Code restricts the availability of capital funds for payment of dividends by the Banks to their additional paid-in capital.

In addition to the dividend restrictions described above, the banking regulators have the authority to prohibit or to limit the payment of dividends by the Banks if, in the banking regulator's opinion, payment of a dividend would constitute an unsafe or unsound practice in light of the financial condition of the Banks.

Under Pennsylvania law, the Company may not pay a dividend, if, after giving effect thereto, it would be unable to pay its debts as they become due in the usual course of business and, after giving effect to the dividend, the total assets of the Company would be less than the sum of its total liabilities plus the amount that would be needed, if the Company were to be dissolved at the time of distribution, to satisfy the preferential rights upon dissolution of shareholders whose rights are superior to those receiving the dividend.

It is also the policy of the FRB that a bank holding company generally only pay dividends on common stock out of net income available to common shareholders over the past twelve months and only if the prospective rate of earnings retention appears consistent with a bank holding company's capital needs, asset quality, and overall financial condition. In the current financial and economic environment, the FRB has indicated that bank holding companies should carefully review their dividend policy and has discouraged dividend pay-out ratios at the 100% level unless both asset quality and capital are very strong. A bank holding company also should not maintain a dividend level that places undue pressure on the capital of such institution's subsidiaries, or that may undermine the bank holding company's ability to serve as a source of strength for such subsidiaries.

C. Regulation of the Banks

The Banks are highly regulated by the FDIC and the Department. The laws that such agencies enforce limit the specific types of businesses in which the Banks may engage, and the products and services that the Banks may offer to customers. Generally, these limitations are designed to protect the insurance fund of the FDIC and/or the customers of the Banks, and not the Banks or its shareholders. From time to time, various types of new federal and state legislation have been proposed that could result in additional regulation of, and restrictions on, the business of the Banks. It cannot be predicted whether any such legislation will be adopted or how such legislation would affect business of the Banks. As a consequence of the extensive regulation of commercial banking activities in the United States, the Banks' business is particularly susceptible to being affected by federal legislation and regulations that may increase the costs of doing business. Some of the major regulatory provisions that affect the business of the Banks are discussed briefly below.

Prompt Corrective Action

The FDIC has specified the levels at which an insured institution will be considered “well-capitalized,” “adequately capitalized,” “undercapitalized,” and “critically undercapitalized.” In the event an institution’s capital deteriorates to the “undercapitalized” category or below, the Federal Deposit Insurance Act (the “FDIA”) and FDIC regulations prescribe an increasing amount of regulatory intervention, including: (1) the institution of a capital restoration plan by a bank and a guarantee of the plan by a parent institution and liability for civil money damages for failure to fulfill its commitment on that guarantee; and (2) the placement of a hold on increases in assets, number of branches, or lines of business. If capital has reached the significantly or critically undercapitalized levels, further material restrictions can be imposed, including restrictions on interest payable on accounts, dismissal of management and (in critically undercapitalized situations) appointment of a receiver. For well-capitalized institutions, the FDIA provides authority for regulatory intervention where the institution is deemed to be engaging in unsafe or unsound practices or receives a less than satisfactory examination report rating for asset quality, management, earnings or liquidity.

Deposit Insurance

The FDIC maintains the Deposit Insurance Fund ("DIF") by assessing depository institutions an insurance premium. The FDIC has set the amount of deposits it insures to $250,000.

As mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”), the assessment base that the FDIC uses to calculate assessment premiums is a bank’s average assets minus average tangible equity. The range of assessment rates is a low of 2.5 basis points to a high of 45 basis points, per $100 of assets.

The FDIC is required under the Dodd-Frank Act to establish assessment rates that will allow the DIF to achieve a reserve ratio of 1.35% of insured deposits by September 2020. In addition, the FDIC has established a “designated reserve ratio” of 2.0%, a target ratio that, until it is achieved, will not likely result in the FDIC reducing assessment rates. In attempting to achieve the mandated 1.35% ratio, the FDIC is required to implement assessment formulas that charge banks over $10 billion in asset size more than banks under that size. Under the Dodd-Frank Act, the FDIC is authorized to make reimbursements from the insurance fund to banks if the reserve ratio exceeds 1.50%, but the FDIC has adopted the “designated reserve ratio” of 2.0% and has announced that any reimbursements from the fund are indefinitely suspended.

Federal Home Loan Bank System

The Banks are a member of the Federal Home Loan Bank of Pittsburgh (the “FHLB”), which is one of 12 regional Federal Home Loan Banks. Each Federal Home Loan Bank serves as a reserve or central bank for its members within its assigned region. It is funded primarily from funds deposited by member institutions and proceeds from the sale of consolidated obligations of the Federal Home Loan Bank System. It makes loans to members (i.e., advances) in accordance with policies and procedures established by the board of directors of the Federal Home Loan Bank. At December 31, 2015, the Banks had $118,929,000 in FHLB advances.

As a member, the Banks are required to purchase and maintain stock in the FHLB. The amount of required stock varies based on the FHLB products utilitied by the Banks and the amount of the products utilized. At December 31, 2015, the Banks had $8,323,600 in stock of the FHLB which was in compliance with this requirement.

Other Legislation

The Dodd-Frank Act was enacted on July 21, 2010 and significantly changed the bank regulatory structure and affected the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The federal agencies are given significant discretion in drafting rules and regulations to implement the Dodd-Frank Act, and consequently, much of the impact of the Dodd-Frank Act may not be known for some time.

Certain provisions of the Dodd-Frank Act have already impacted the Company. For example, effective July 21, 2011, a provision of the Dodd-Frank Act eliminated the federal prohibitions on paying interest on demand deposits, thus allowing businesses to have interest bearing checking accounts. Depending on competitive responses, this significant change to existing law could have an adverse impact on the Company’s interest expense. The Dodd-Frank Act also permanently increased the maximum amount of deposit insurance for banks, savings institutions and credit unions to $250,000 per depositor, retroactive to January 1, 2008.

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Bank and thrift holding companies with assets of less than $15 billion as of December 31, 2009, such as the Company, will be permitted to include trust preferred securities that were issued before May 19, 2010, as Tier 1 capital; however, trust preferred securities issued by a bank or thrift holding company (other than those with assets of less than $500 million) after May 19, 2010, will no longer count as Tier 1 capital. Trust preferred securities still will be entitled to be treated as Tier 2 capital.

The Dodd-Frank Act requires publicly traded companies to give shareholders a non-binding vote on executive compensation and so-called “golden parachute” arrangements, and may allow greater access by shareholders to the company’s proxy material by authorizing the SEC to promulgate rules that would allow shareholders to nominate their own candidates using a company’s proxy materials. The legislation also directs the FRB to promulgate rules prohibiting excessive compensation paid to bank holding company executives, regardless of whether the company is publicly traded.

The Dodd-Frank Act created a new Consumer Financial Protection Bureau with broad powers to supervise and enforce consumer protection laws. The Consumer Financial Protection Bureau has broad rule-making authority for a wide range of consumer protection laws that apply to all banks and savings institutions, including the authority to prohibit “unfair, deceptive or abusive” acts and practices. The Consumer Financial Protection Bureau has examination and enforcement authority over all banks and savings institutions with more than $10 billion in assets. Banks and savings institutions with $10 billion or less in assets such as the Banks will continue to be examined for compliance with the consumer laws by their primary bank regulators. The Dodd-Frank Act also weakens the federal preemption rules that have been applicable for national banks and federal savings associations, and gives state attorneys general the ability to enforce federal consumer protection laws.

It is difficult to predict at this time the specific impact the Dodd-Frank Act and the yet to be written implementing rules and regulations will have on community banks. Given the uncertainty associated with the manner in which the provisions of the Dodd-Frank Act will be implemented by the various regulatory agencies and through regulations, the full extent of the impact such requirements will have on financial institutions’ operations is presently unclear. The changes resulting from the Dodd-Frank Act may impact the profitability of our business activities, require changes to certain of our business practices, or otherwise adversely affect our business. These changes may also require us to invest significant management attention and resources to evaluate and make necessary changes in order to comply with new statutory and regulatory requirements.

The Sarbanes-Oxley Act of 2002 was enacted to enhance penalties for accounting and auditing improprieties at publicly traded companies and to protect investors by improving the accuracy and reliability of corporate disclosures under the federal securities laws. The Sarbanes-Oxley Act generally applies to all companies, including the Company, that file or are required to file periodic reports with the Securities and Exchange Commission under the Securities Exchange Act of 1934, or the Exchange Act. The legislation includes provisions, among other things, governing the services that can be provided by a public company’s independent auditors and the procedures for approving such services, requiring the chief executive officer and principal accounting officer to certify certain matters relating to the company’s periodic filings under the Exchange Act, requiring expedited filings of reports by insiders of their securities transactions and containing other provisions relating to insider conflicts of interest, increasing disclosure requirements relating to critical financial accounting policies and their application, increasing penalties for securities law violations, and creating a new public accounting oversight board, a regulatory body subject to SEC jurisdiction with broad powers to set auditing, quality control, and ethics standards for accounting firms. In response to the legislation, the national securities exchanges and NASDAQ have adopted new rules relating to certain matters, including the independence of members of a company’s audit committee as a condition to listing or continued listing.

Congress is often considering some financial industry legislation, and the federal banking agencies routinely propose new regulations. The Company cannot predict how any new legislation, or new rules adopted by federal or state banking agencies, may affect the business of the Company and its subsidiaries in the future. Given that the financial industry remains under stress and severe scrutiny, and given that the U.S. economy has not yet fully recovered to pre-crisis levels of activity, the Company expects that there will be significant legislation and regulatory actions that may materially affect the banking industry for the foreseeable future.

Environmental Laws

Environmentally related hazards have become a source of high risk and potential liability for financial institutions relating to their loans. Environmentally contaminated properties owned by an institution's borrowers may result in a drastic reduction in the value of the collateral securing the institution's loans to such borrowers, high environmental clean up costs to the borrower affecting its ability to repay the loans, the subordination of any lien in favor of the institution to a state or federal lien securing clean up costs, and liability to the institution for clean up costs if it forecloses on the contaminated property or becomes involved in the management of the borrower. The Company is not aware of any borrower who is currently subject to any environmental investigation or clean up proceeding which is likely to have a material adverse effect on the financial condition or results of operations of the Company.

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Effect of Government Monetary Policies

The earnings of the Company are and will be affected by domestic economic conditions and the monetary and fiscal policies of the United States Government and its agencies. The monetary policies of the FRB have had, and will likely continue to have, an important impact on the operating results of commercial banks through its power to implement national monetary policy in order, among other things, to curb inflation or combat a recession. The FRB has a major effect upon the levels of bank loans, investments, and deposits through its open market operations in the United States Government securities and through its regulation of, among other things, the discount rate on borrowings by member banks and the reserve requirements against member bank deposits. It is not possible to predict the nature and impact of future changes in monetary and fiscal policies.

DESCRIPTION OF THE BANKS

History and Business

JSSB was incorporated under the laws of the Commonwealth of Pennsylvania as a state bank in 1934 and became a wholly owned subsidiary of the Company on July 12, 1983.

As of December 31, 2015, JSSB had total assets of $965,803,000; total shareholders’ equity of $82,364,000; and total deposits of $722,657,000. JSSB's deposits are insured by the FDIC for the maximum amount provided under current law.

Luzerne was acquired by the Company on June 1, 2013. As of December 31, 2015, Luzerne had total assets of $368,685,000; total shareholders’ equity of $44,762,000; and total deposits of $310,036,000. Luzerne's deposits are insured by the FDIC for the maximum amount provided under current law.

The Banks engage in business as commercial banks, doing business at locations in Lycoming, Clinton, Centre, Montour, Union and Luzerne Counties, Pennsylvania. The Banks offer insurance, securities brokerage services, annuity and mutual fund investment products, and financial planning through the M Group.

Services offered by the Banks include accepting time, demand and savings deposits including Super NOW accounts, statement savings accounts, money market accounts, and fixed rate certificates of deposit. Their services also include making secured and unsecured business and consumer loans that include financing commercial transactions as well as construction and residential mortgage loans and revolving credit loans with overdraft protection.

The Banks' loan portfolio mix can be classified into three principal categories. These are commercial and agricultural, real estate, and consumer. Real estate loans can be further segmented into residential, commercial, and construction. Qualified borrowers are defined by our loan policy and our underwriting standards. Owner provided equity requirements range from 0% to 35%, depending on the collateral offered for the loan. Terms are generally restricted to 30 years or less with the exception of construction and land development, which are generally limited to one and five years, respectively. Real estate appraisals, property construction verifications, and site visitations comply with our loan policy and with industry regulatory standards.

Prospective residential mortgage customer’s repayment ability is determined from information contained in the application and recent income tax returns, or other verified income sources. Emphasis is on credit, employment, income, and residency verification. Broad hazard insurance is always required and flood insurance where applicable. In the case of construction mortgages, builders risk insurance is requested.

Agricultural loans for the purchase or improvement of real estate must meet the Banks' real estate underwriting criteria. Agricultural loans made for the purchase of equipment are usually payable in five years, but never more than ten, depending upon the useful life of the purchased asset. Minimum borrower equity ranges from 0% to 35% depending on the purpose. Livestock financing criteria depends upon the nature of the operation. Agricultural loans are also made for crop production purposes. Such loans are structured to repay within the production cycle and not carried over into a subsequent year.

Commercial loans are made for the acquisition and improvement of real estate, purchase of equipment, and for working capital purposes on a seasonal or revolving basis. General purpose working capital loans are also available with repayment expected within one year. Equipment loans are generally amortized over three to ten years. Insurance coverage with the Banks as loss payee is required, especially in the case where the equipment is rolling stock. It is also a general policy to collateralize non-real estate loans with the asset purchased and, dependant upon loan terms, junior liens are filed on other available assets. Financial information required on all commercial mortgages includes the most current three years balance sheets and income statements and projections on income to be developed through the project. In the case of corporations and partnerships, the principals are often asked to personally guaranty the entity’s debt.

Seasonal and revolving lines of credit are offered for working capital purposes. Collateral for such a loan may vary but often includes the pledge of inventory and/or receivables. Drawing availability is usually 50% of inventory and 80% of eligible receivables. Eligible receivables are defined as invoices less than 90 days delinquent. Exclusive reliance is very seldom placed on such collateral; therefore, other lienable assets are also taken into the collateral pool. Where reliance is placed on inventory and accounts receivable, the applicant must provide financial information including agings on a specified basis. In addition, the guaranty of the principals is usually obtained.

Letter of credit availability is usually limited to standby or performance letters of credit where the customer is well known to the Banks. The credit criteria is the same as that utilized in making a direct loan. Collateral is obtained in most cases.

Consumer loan products include residential mortgages, home equity loans and lines, automobile financing, personal loans and lines of credit, overdraft and check lines. Our policy includes standards used in the industry on debt service ratios and terms are consistent with prudent underwriting standards and the use of proceeds. Verifications are made of employment and residency, along with credit history.

Second mortgages are confined to equity borrowing and home improvements. Terms are generally fifteen years or less. Loan to collateral value criteria is 90% or less and verifications are made to determine values. Automobile financing is generally restricted to five years and done on a direct basis. The Banks, as a practice, do not floor plan and therefore do not discount dealer paper. Small loan requests are to accommodate personal needs such as debt consolidation or the purchase of small appliances. Overdraft check lines are usually limited to $5,000 or less.

The Banks' investment portfolios are analyzed and priced on a monthly basis. Investments are made in U.S. Treasuries, U.S. Agency issues, bank qualified tax-exempt municipal bonds, taxable municipal bonds, corporate bonds, and corporate stocks which consist of Pennsylvania bank stocks. Bonds with BAA or better ratings are used, unless a local issue is purchased that has a lesser or no rating. Factors taken into consideration when investments are purchased include liquidity, the Company’s tax position, tax equivalent yield, third party investment ratings, and the policies of the Asset/Liability Committee.

The banking environment in Lycoming, Clinton, Centre, Montour, Union and Luzerne Counties, Pennsylvania is highly competitive. The Banks operate twenty-three full service offices in these markets and compete for loans and deposits with numerous commercial banks, savings and loan associations, and other financial institutions. The economic base of the region is developed around small business, health care, educational facilities (college and public schools), light manufacturing industries, and agriculture.

The Banks have a relatively stable deposit base and no material amount of deposits is obtained from a single depositor or group of depositors, excluding public entities that account for approximately 15% of total deposits. Although the Banks have regular opportunities to bid on pools of funds of $100,000 or more in the hands of municipalities, hospitals, and others, it does not rely on these monies to fund loans or intermediate or longer-term investments.

The Banks have not experienced any significant seasonal fluctuations in the amount of deposits. The Banks have experienced an outflow of deposits related to municipalities and school districts due to the ongoing Commonwealth of Pennsylvania budget impass.

Supervision and Regulation

As referenced elsewhere, the banking business is highly regulated, and the Banks are only able to engage in business activities, and to provide products and services, that are permitted by applicable law and regulation. In addition, the earnings of the Banks are affected by the policies of regulatory authorities including the FDIC and the FRB. An important function of the FRB is to regulate the money supply and interest rates. Among the instruments used to implement these objectives are open market operations in U.S. Government Securities, changes in reserve requirements against member bank deposits, and limitations on interest rates that member banks may pay on time and savings deposits. These instruments are used in varying combinations to influence overall growth and distribution of bank loans, and their use may also affect interest rates charged on loans or paid for deposits.

The policies and regulations of the FRB have had and will probably continue to have a significant effect on the Banks' deposits, loans and investment growth, as well as the rate of interest earned and paid, and are expected to affect the Banks' operation in the future. The effect of such policies and regulations upon the future business and earnings of the Banks cannot accurately be predicted.

ITEM 1A RISK FACTORS

The following sets forth several risk factors that may affect the Company's financial condition or results of operations.

Changes in interest rates could reduce our income, cash flows and asset values.

Our income and cash flows and the value of our assets depend to a great extent on the difference between the interest rates we earn on interest-earning assets, such as loans and investment securities, and the interest rates we pay on interest-bearing liabilities such as deposits and borrowings. These rates are highly sensitive to many factors which are beyond our control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Board of Governors of the Federal Reserve System. Changes in monetary policy, including changes in interest rates, will influence not only the interest we receive on our loans and investment securities and the amount of interest we pay on deposits and borrowings but will also affect our ability to originate loans and obtain deposits and the value of our investment portfolio. If the rate of interest we pay on our deposits and other borrowings increases more than the rate of interest we earn on our loans and other investments, our net interest income, and therefore our earnings, could be adversely affected. Our earnings also could be adversely affected if the rates on our loans and other investments fall more quickly than those on our deposits and other borrowings.

Economic conditions either nationally or locally in areas in which our operations are concentrated may adversely affect our business.

Deterioration in local, regional, national, or global economic conditions could cause us to experience a reduction in deposits and new loans, an increase in the number of borrowers who default on their loans, and a reduction in the value of the collateral securing their loans, all of which could adversely affect our performance and financial condition. Unlike larger banks that are more geographically diversified, we provide banking and financial services locally. Therefore, we are particularly vulnerable to adverse local economic conditions.

Our financial condition and results of operations would be adversely affected if our allowance for loan losses is not sufficient to absorb actual losses or if we are required to increase our allowance.

Despite our underwriting criteria, we may experience loan delinquencies and losses. In order to absorb losses associated with nonperforming loans, we maintain an allowance for loan losses based on, among other things, historical experience, an evaluation of economic conditions, and regular reviews of delinquencies and loan portfolio quality. Determination of the allowance inherently involves a high degree of subjectivity and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes. At any time there are likely to be loans in our portfolio that will result in losses but that have not been identified as nonperforming or potential problem credits. We cannot be sure that we will be able to identify deteriorating credits before they become nonperforming assets or that we will be able to limit losses on those loans that are identified. We may be required to increase our allowance for loan losses for any of several reasons. Federal regulators, in reviewing our loan portfolio as part of a regulatory examination, may request that we increase our allowance for loan losses. Changes in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of our control, may require an increase in our allowance. In addition, if charge-offs in future periods exceed our allowance for loan losses, we will need additional increases in our allowance for loan losses. Any increases in our allowance for loan losses will result in a decrease in our net income and, possibly, our capital, and may materially affect our results of operations in the period in which the allowance is increased.

Many of our loans are secured, in whole or in part, with real estate collateral which is subject to declines in value.

In addition to considering the financial strength and cash flow characteristics of a borrower, we often secure our loans with real estate collateral. Real estate values and the real estate market are generally affected by, among other things, changes in local, regional or national economic conditions, fluctuations in interest rates and the availability of loans to potential purchasers, changes in tax laws and other governmental statutes, regulations and policies, and acts of nature.

The real estate collateral provides an alternate source of repayment in the event of default by the borrower. If real estate prices in our markets decline, the value of the real estate collateral securing our loans could be reduced. If we are required to liquidate real estate collateral securing loans during a period of reduced real estate values to satisfy the debt, our earnings and capital could be adversely affected.

Our information systems may experience an interruption or breach in security.
We rely heavily on communications and information systems to conduct our business. Any failure, interruption or breach in security of these systems could result in failures or disruptions in our customer-relationship management, general ledger, deposit, loan and other systems. While we have policies and procedures designed to prevent or limit the effect of the failure, interruption or security breach of our information systems, there can be no assurance that any such failures, interruptions or security breaches will not occur; or, if they do occur, that they will be adequately addressed. The occurrence of any failures, interruptions or security breaches of our information systems could damage our reputation, result in a loss of customer business, subject us to additional

regulatory scrutiny or expose us to civil litigation and possible financial liability; any of which could have a material adverse effect on our financial condition and results of operations.

We face the risk of cyber-attack to our computer systems.

Our computer systems, software and networks have been and will continue to be vulnerable to unauthorized access, loss or destruction of data (including confidential client information), account takeovers, unavailability of service, computer viruses or other malicious code, cyber-attacks and other events. These threats may derive from human error, fraud or malice on the part of employees or third parties, or may result from accidental technological failure. If one or more of these events occurs, it could result in the disclosure of confidential client information, damage to our reputation with our clients and the market, additional costs to us (such as repairing systems or adding new personnel or protection technologies), regulatory penalties and financial losses, to both us and our clients and customers. Such events could also cause interruptions or malfunctions in our operations (such as the lack of availability of our online banking system), as well as the operations of our clients, customers or other third parties. Although we maintain safeguards to protect against these risks, there can be no assurance that we will not suffer losses in the future that may be material in amount.

Competition may decrease our growth or profits.

We face substantial competition in all phases of our operations from a variety of different competitors, including commercial banks, savings and loan associations, mutual savings banks, credit unions, consumer finance companies, factoring companies, leasing companies, insurance companies, and money market mutual funds. There is very strong competition among financial services providers in our principal service area. Our competitors may have greater resources, higher lending limits, or larger branch systems than we do. Accordingly, they may be able to offer a broader range of products and services as well as better pricing for those products and services than we can.

In addition, some of the financial services organizations with which we compete are not subject to the same degree of regulation as is imposed on federally insured financial institutions. As a result, those non-bank competitors may be able to access funding and provide various services more easily or at less cost than we can, adversely affecting our ability to compete effectively.

The value of certain investment securities is volatile and future declines or other-than-temporary impairments could materially adversely affect our future earnings and regulatory capital.

Continued volatility in the market value for certain of our investment securities, whether caused by changes in market perceptions of credit risk, as reflected in the expected market yield of the security, or actual defaults in the portfolio could result in significant fluctuations in the value of the securities. This could have a material adverse impact on our accumulated other comprehensive income/loss and shareholders' equity depending on the direction of the fluctuations. Furthermore, future downgrades or defaults in these securities could result in future classifications of investment securities as other than temporarily impaired. This could have a material impact on our future earnings.

We may be adversely affected by government regulation.

The banking industry is heavily regulated. Banking regulations are primarily intended to protect the federal deposit insurance funds and depositors, not shareholders. Changes in the laws, regulations, and regulatory practices affecting the banking industry may increase our costs of doing business or otherwise adversely affect us and create competitive advantages for others. Regulations affecting banks and financial services companies undergo continuous change, and we cannot predict the ultimate effect of these changes, which could have a material adverse effect on our profitability or financial condition.

In response to the financial crisis that commenced in 2008, Congress has taken actions that are intended to strengthen confidence and encourage liquidity in financial institutions, and the FDIC has taken actions to increase insurance coverage on deposit accounts. The Dodd-Frank Act provides for the creation of a consumer protection division at the Board of Governors of the Federal Reserve System that will have broad authority to issue regulations governing the services and products we provide consumers. This additional regulation could increase our compliance costs and otherwise adversely impact our operations. That legislation also contains provisions that, over time, could result in higher regulatory capital requirements (including through the implementation of the capital standards of Basel III) and loan loss provisions for the Banks, and may increase interest expense due to the ability granted in July 2011 to pay interest on all demand deposits. In addition, there have been proposals made by members of Congress and others that would reduce the amount delinquent borrowers are otherwise contractually obligated to pay under their mortgage loans and limit an institution’s ability to foreclose on mortgage collateral. These proposals could result in credit losses or increased expense in pursuing our remedies as a creditor. Recent regulatory changes impose limits on our ability to charge overdraft fees, which may decrease our non-interest income as compared to more recent prior periods.

The potential exists for additional federal or state laws and regulations, or changes in policy, affecting many aspects of our operations, including capital levels, lending and funding practices, and liquidity standards. New laws and regulations may increase our costs of regulatory compliance and of doing business and otherwise affect our operations, and may significantly affect the markets in which we do business, the markets for and value of our loans and investments, the fees we can charge and our ongoing operations, costs and profitability.

We rely on our management and other key personnel, and the loss of any of them may adversely affect our operations.

We are and will continue to be dependent upon the services of our executive management team. In addition, we will continue to depend on our ability to retain and recruit key commercial loan officers. The unexpected loss of services of any key management personnel or commercial loan officers could have an adverse effect on our business and financial condition because of their skills, knowledge of our market, years of industry experience, and the difficulty of promptly finding qualified replacement personnel.

Environmental liability associated with lending activities could result in losses.

In the course of our business, we may foreclose on and take title to properties securing our loans. If hazardous substances were discovered on any of these properties, we could be liable to governmental entities or third parties for the costs of remediation of the hazard, as well as for personal injury and property damage. Many environmental laws can impose liability regardless of whether we knew of, or were responsible for, the contamination. In addition, if we arrange for the disposal of hazardous or toxic substances at another site, we may be liable for the costs of cleaning up and removing those substances from the site even if we neither own nor operate the disposal site. Environmental laws may require us to incur substantial expenses and may materially limit use of properties we acquire through foreclosure, reduce their value or limit our ability to sell them in the event of a default on the loans they secure. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability.

Failure to implement new technologies in our operations may adversely affect our growth or profits.

The market for financial services, including banking services and consumer finance services is increasingly affected by advances in technology, including developments in telecommunications, data processing, computers, automation, Internet-based banking, and telebanking. Our ability to compete successfully in our markets may depend on the extent to which we are able to exploit such technological changes. However, we can provide no assurance that we will be able to properly or timely anticipate or implement such technologies or properly train our staff to use such technologies. Any failure to adapt to new technologies could adversely affect our business, financial condition, or operating results.

An investment in our common stock is not an insured deposit.

Our common stock is not a bank deposit and, therefore, is not insured against loss by the FDIC, any other deposit insurance fund, or by any other public or private entity. Investment in our common stock is subject to the same market forces that affect the price of common stock in any company.

ITEM 1B UNRESOLVED STAFF COMMENTS

None.

ITEM 2 PROPERTIES

The Company owns and leases its properties. Listed herewith are the locations of properties owned or leased as of December 31, 2015, in which the banking offices are located; all properties are in good condition and adequate for the Company's purposes:

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Jersey Shore State Bank & Subsidiaries

Office	Address	Ownership
Main Street	115 South Main Street, PO Box 5098 Jersey Shore, Pennsylvania 17740	Owned
Bridge Street	112 Bridge Street Jersey Shore, Pennsylvania 17740	Owned
DuBoistown	2675 Euclid Avenue Williamsport, Pennsylvania 17702	Owned
Williamsport	300 Market Street P.O. Box 967 Williamsport, Pennsylvania 17703-0967	Owned
Montgomery	9094 Rt. 405 Highway Montgomery, Pennsylvania 17752	Owned
Lock Haven	4 West Main Street Lock Haven, Pennsylvania 17745	Owned
Mill Hall	(Inside Wal-Mart), 173 Hogan Boulevard Mill Hall, Pennsylvania 17751	Under Lease
Spring Mills	3635 Penns Valley Road, P.O. Box 66 Spring Mills, Pennsylvania 16875	Under Lease
Centre Hall	2842 Earlystown Road Centre Hall, Pennsylvania 16828	Land Under Lease
Zion	100 Cobblestone Road Bellefonte, Pennsylvania 16823	Under Lease
State College	2050 North Atherton Street State College, Pennsylvania 16803	Land Under Lease
Montoursville	820 Broad Street Montoursville, Pennsylvania 17754	Under Lease
Danville	606 Continental Boulevard Danville, Pennsylvania 17821	Under Lease
Loyalsock	1720 East Third Street Williamsport, PA 17701	Owned
Lewisburg	550 North Derr Drive Lewisburg, PA 17837	Land Under Lease
The M Group, Inc.	705 Washington Boulevard	Under Lease

D/B/A The Comprehensive Financial Group	Williamsport, Pennsylvania 17701

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Luzerne Bank

Office	Address	Ownership
Dallas	509 Main Road Memorial Highway Dallas, PA 18612	Owned
Lake	Corners of Rt. 118 & 415 Dallas, PA 18612	Owned
Hazle Twp.	10 Dessen Drive Hazle Twp., PA 18202	Owned
Luzerne	118 Main Street Luzerne, PA 18709	Owned
Plains	1077 Hwy. 315 Wilkes Barre, PA 18702	Under Lease
Swoyersville	801 Main Street Swoyersville, PA 18704	Owned
Wilkes-Barre	67 Public Square Wilkes-Barre, PA 18701	Under Lease
Wyoming	324 Wyoming Ave. Wyoming, PA 18644	Owned

ITEM 3 LEGAL PROCEEDINGS

The Company is subject to lawsuits and claims arising out of its business in the ordinary course. In the opinion of management, after review and consultation with counsel, there are no legal proceedings currently pending or threatened that are reasonably likely to have a material adverse effect on the consolidated financial position or results of operations of the Company.

ITEM 4 MINE SAFETY DISCLOSURES

Not applicable.

PART II

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

The Company’s common stock is listed on the NASDAQ Global Select Market under the symbol “PWOD”. The following table sets forth (1) the quarterly high and low closing sale prices for a share of the Company’s Common Stock during the periods indicated, and (2) quarterly dividends on a share of the common stock with respect to each quarter since January 1, 2013.

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	Price Range High	Low	Dividends Declared
2015			
First quarter	$48.91	$44.41	$0.47
Second quarter	48.28	41.84	0.47
Third quarter	44.56	40.41	0.47
Fourth quarter	45.28	40.47	0.47
2014			
First quarter	$50.95	$43.19	$0.47
Second quarter	48.37	43.21	0.47
Third quarter	48.79	42.25	0.47
Fourth quarter	49.26	42.18	0.47
2013			
First quarter	$41.45	$38.50	$0.72
Second quarter	41.86	39.44	0.47
Third quarter	49.89	42.76	0.47
Fourth quarter	53.99	47.03	0.47

The Company has paid dividends since the effective date of its formation as a bank holding company. It is the present intention of the Company's board of directors to continue the dividend payment policy; however, further dividends must necessarily depend upon earnings, financial condition, appropriate legal restrictions, and other factors relevant at the time the board of directors of the Company considers dividend policy. Cash available for dividend distributions to shareholders of the Company primarily comes from dividends paid by Jersey Shore State Bank and Luzerne Bank to the Company. Therefore, the restrictions on the Banks' dividend payments are directly applicable to the Company. See also the information appearing in Note 20 to "Notes to Consolidated Financial Statements" for additional information related to dividend restrictions.

Under the Pennsylvania Business Corporation Law of 1988 a corporation may not pay a dividend, if after giving effect thereto, the corporation would be unable to pay its debts as they become due in the usual course of business and after giving effect thereto the total assets of the corporation would be less than the sum of its total liabilities plus the amount that would be needed, if the corporation were to be dissolved at the time of the distribution, to satisfy the preferential rights upon dissolution of the shareholders whose preferential rights are superior to those receiving the dividend.

As of March 1, 2016, the Company had approximately 1,373 shareholders of record.

Following is a schedule of the shares of the Company's common stock purchased by the Company during the fourth quarter of 2015.

Period	Total Number of Shares (or Units) Purchased	Average Price Paid per Share (or Units) Purchased	Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
Month #1 (October 1 - October 31, 2015)	3,708	$41.13	3,708	404,744
Month #2 (November 1 - November 30, 2015)	—	—	—	404,744
Month #3 (December 1 - December 31, 2015)	—	—	—	404,744

Set forth below is a line graph comparing the yearly dollar changes in the cumulative shareholder return on the Company's common stock against the cumulative total return of the S&P 500 Stock Index, NASDAQ Bank Index, NASDAQ Composite, and Russell 2000 for the period of five fiscal years assuming the investment of $100.00 on December 31, 2010 and assuming the reinvestment of dividends. The shareholder return shown on the graph below is not necessarily indicative of future performance.

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	Period Ending					
Index	12/31/2010	12/31/2011	12/31/2012	12/31/2013	12/31/2014	12/31/2015
Penns Woods Bancorp, Inc.	100.00	102.50	103.81	148.52	149.43	134.47
S&P 500	100.00	102.11	118.45	156.82	178.28	180.75
NASDAQ Composite	100.00	99.21	116.82	163.75	188.03	201.40
NASDAQ Bank	100.00	89.50	106.23	150.55	162.35	171.92
Russell 2000	100.00	95.82	111.49	154.78	162.35	155.18

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ITEM 6 SELECTED FINANCIAL DATA

The following table sets forth certain financial data for each of the years in the five-year period ended December 31, 2015:

(In Thousands, Except Per Share Data Amounts)	2015	2014	2013	2012	2011
Consolidated Statement of Income Data:					
Interest income	$46,124	$45,606	$43,299	$37,107	$36,376
Interest expense	5,219	4,962	5,264	6,211	7,656
Net interest income	40,905	40,644	38,035	30,896	28,720
Provision for loan losses	2,300	2,850	2,275	2,525	2,700
Net interest income after provision for loan losses	38,605	37,794	35,760	28,371	26,020
Non-interest income	12,765	14,508	12,042	10,100	8,219
Non-interest expense	33,736	33,890	30,267	22,023	19,964
Income before income tax provision	17,634	18,412	17,535	16,448	14,275
Income tax provision	3,736	3,804	3,451	2,598	1,913
Net income	$13,898	$14,608	$14,084	$13,850	$12,362
Consolidated Balance Sheet at End of Period:					
Total assets	$1,320,057	$1,245,011	$1,211,995	$856,535	$763,953
Loans	1,045,207	915,579	818,344	512,232	435,959
Allowance for loan losses	(12,044)	(10,579)	(10,144)	(7,617)	(7,154)
Deposits	1,031,880	981,419	973,002	642,026	581,664
Long-term debt	91,025	71,176	71,202	76,278	61,278
Shareholders’ equity	136,279	135,967	127,815	93,726	80,460
Per Share Data:					
Earnings per share - basic	$2.91	$3.03	$3.19	$3.61	$3.22
Earnings per share - diluted	2.91	3.03	3.19	3.61	3.22
Cash dividends declared	1.88	1.88	2.13	1.88	1.84
Book value	28.71	28.30	26.52	24.42	20.97
Number of shares outstanding, at end of period	4,747,132	4,804,815	4,819,333	3,838,516	3,837,081
Weighted average number of shares outstanding - basic and diluted	4,772,239	4,816,149	4,410,626	3,837,751	3,836,036
Selected Financial Ratios:					
Return on average shareholders’ equity	10.11 %	10.79 %	12.36 %	15.36 %	16.60 %
Return on average total assets	1.08 %	1.19 %	1.32 %	1.70 %	1.69 %
Net interest margin	3.61 %	3.81 %	4.13 %	4.45 %	4.70 %
Dividend payout ratio	64.52 %	61.99 %	67.88 %	52.08 %	57.10 %
Average shareholders’ equity to average total assets	10.68 %	11.05 %	10.70 %	11.04 %	10.18 %
Loans to deposits, at end of period	101.29 %	93.29 %	84.11 %	79.78 %	74.95 %

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ITEM 7 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

RESULTS OF OPERATIONS

NET INTEREST INCOME

Net interest income is determined by calculating the difference between the yields earned on interest-earning assets and the rates paid on interest-bearing liabilities. To compare the tax-exempt asset yields to taxable yields, amounts are adjusted to taxable equivalents based on the marginal corporate federal tax rate of 34%. The tax equivalent adjustments to net interest income for 2015, 2014, and 2013 were $2,011,000, $2,219,000, and $2,730,000, respectively.

2015 vs. 2014

Reported net interest income increased $261,000 to $40,905,000 for the year ended December 31, 2015 compared to the year ended December 31, 2014, as the yield on earning assets decreased to 4.04% from 4.25% offsetting the growth in the earning asset portfolio. On a tax equivalent basis, the change in net interest income was an increase of $53,000 to $42,916,000 for the year ended December 31, 2015 compared to the year ended December 31, 2014. Total interest income increased $518,000 as the impact of growth in the average balance of the loan portfolio was limited by a decline in the average balance of the investment portfolio as the portfolio is actively managed to reduce interest rate and market risk. Interest income growth was also limited by the portfolio yields caused by the prolonged low interest rate cycle enacted by the Federal Open Markets Committee ("FOMC"). Interest income on a tax equivalent basis recognized on the loan portfolio increased $2,770,000 due to a $117,317,000 increase in the average balance in the loan portfolio which was partially offset by interest rates repricing downward . Interest and dividend income generated from the investment portfolio on a tax equivalent basis decreased $2,440,000 due to a $46,232,000 decrease in the average balance in the investment portfolio and a 23 basis point ("bp") reduction in the average rate. The decrease in the portfolio was driven by a strategic plan that started in 2014 to sell off long-term municipal bonds with a maturity date of 2025 or later and securities with a call date within the next five years, in order to reduce interest rate risk and market risk.

Interest expense increased $257,000 to $5,219,000 for the year ended December 31, 2015 compared to 2014. The increase in interest expense was driven by growth in total deposits and borrowings that funded the earning asset portfolio growth. The impact of the growth in interest-bearing liabilities was limited by minimal increase of 1 bp in cost of funds. The average rate paid on time deposits increased 13 bp as efforts were undertaken to lengthen the time deposit portfolio in preparation for a rising rate environment.

2014 vs. 2013

Reported net interest income increased $2,609,000 or 6.86% to $40,644,000 for the year ended December 31, 2014 compared to the year ended December 31, 2013, although the yield on earning assets decreased to 4.25% from 4.66%. On a tax equivalent basis, the change in net interest income was an increase of $2,098,000 or 5.15% to $42,863,000 for the year ended December 31, 2014 compared to the year ended December 31, 2013. Total interest income increased $2,307,000 as the impact of growth in the average balance of the loan portfolio was offset by a decline in the average balance of the investment portfolio and in the portfolio yields caused by the prolonged low interest rate cycle enacted by the Federal Open Markets Committee ("FOMC"). Interest income on a tax equivalent basis recognized on the loan portfolio increased $4,223,000 due to a $170,929,000 increase in the average balance in the loan portfolio which was partially offset by interest rates repricing downward. Interest and dividend income generated from the investment portfolio on a tax equivalent basis decreased $2,441,000 due to a $36,794,000 decrease in the average balance in the investment portfolio and a 30 basis point ("bp") reduction in the average rate. The decrease in the portfolio was driven by a strategic plan to sell off long-term municipal bonds with a maturity date of 2025 or later and securities with a call date within the next five years, in order to reduce interest rate risk and market risk.

Interest expense decreased $302,000 to $4,962,000 for the year ended December 31, 2014 compared to 2013. Leading the decrease in interest expense was a decline of 7.02% or $226,000 related to deposits. The FOMC actions noted previously together with a strategic focus on core deposits led to a 8 bp decline in the rate paid on interest-bearing deposits from 0.48% for the year ended December 31, 2013 to 0.40% for the year ended December 31, 2014. The overall growth in average deposit balances of $91,174,000 coupled with the decrease in the average investment portfolio were the primary funding source for the growth in the average loans of $170,929,000.

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AVERAGE BALANCES AND INTEREST RATES

The following tables set forth certain information relating to the Company's average balance sheet and reflect the average yield on assets and average cost of liabilities for the periods indicated and the average yields earned and rates paid. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods presented.

	2015				2014				2013			
(In Thousands)	Average Balance	Interest	Average Rate		Average Balance	Interest	Average Rate		Average Balance	Interest	Average Rate	
Assets:												
Tax-exempt loans	$43,395	$1,679	3.87	%	$29,461	$1,295	4.40	%	$24,934	$1,056	4.24	%
All other loans	932,179	38,026	4.08	%	828,796	35,640	4.30	%	662,394	31,656	4.78	%
Total loans	975,574	39,705	4.07	%	858,257	36,935	4.30	%	687,328	32,712	4.76	%
Fed funds sold	—	—	—	%	170	—	—	%	226	—	—	%
Taxable securities	127,052	4,183	3.29	%	161,889	5,626	3.48	%	176,674	6,326	3.58	%
Tax-exempt securities	83,293	4,235	5.08	%	94,688	5,232	5.53	%	116,697	6,973	5.98	%
Total securities	210,345	8,418	4.00	%	256,577	10,858	4.23	%	293,371	13,299	4.53	%
Interest-bearing deposits	4,238	12	0.28	%	9,318	32	0.34	%	6,946	18	0.26	%
Total interest-earning assets	1,190,157	48,135	4.04	%	1,124,322	47,825	4.25	%	987,871	46,029	4.66	%
Other assets	97,103				100,983				76,593			
Total assets	$1,287,260				$1,225,305				$1,064,464			
Liabilities and shareholders' equity:												
Savings	$143,055	56	0.04	%	$140,575	81	0.06	%	$118,125	140	0.12	%
Super Now deposits	187,396	491	0.26	%	182,229	583	0.32	%	154,131	687	0.45	%
Money market deposits	207,252	554	0.27	%	210,066	561	0.27	%	183,460	548	0.30	%
Time deposits	220,360	2,028	0.92	%	223,537	1,770	0.79	%	209,517	1,846	0.88	%
Total interest-bearing deposits	758,063	3,129	0.41	%	756,407	2,995	0.40	%	665,233	3,221	0.48	%
Short-term borrowings	38,909	116	0.30	%	22,342	54	0.24	%	22,281	81	0.38	%
Long-term borrowings	84,721	1,974	2.30	%	71,195	1,913	2.65	%	72,140	1,962	2.68	%

Total borrowings	123,630	2,090	1.67	%	93,537	1,967	2.07	%	94,421	2,043	2.14	%
Total interest-bearing liabilities	881,693	5,219	0.59	%	849,944	4,962	0.58	%	759,654	5,264	0.69	%
Demand deposits	251,029				225,981				174,909			
Other liabilities	17,047				13,933				15,962			
Shareholders' equity	137,491				135,447				113,939			
Total liabilities and shareholders' equity	$1,287,260				$1,225,305				$1,064,464			
Interest rate spread			3.45	%			3.67	%			3.97	%
Net interest income/margin		$42,916	3.61	%		$42,863	3.81	%		$40,765	4.13	%

· Fees on loans are included with interest on loans as follows: 2015 - $422,000; 2014 - $487,000; 2013 - $610,000.

· Information in this table has been calculated using average daily balance sheets to obtain average balances.

· Nonaccrual loans have been included with loans for the purpose of analyzing net interest earnings.

· Income and rates on a fully taxable equivalent basis include an adjustment for the difference between annual income from tax-exempt obligations and the taxable equivalent of such income at the standard 34% tax rate.

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Reconciliation of Taxable Equivalent Net Interest Income

(In Thousands)	2015	2014	2013
Total interest income	$46,124	$45,606	$43,299
Total interest expense	5,219	4,962	5,264
Net interest income	40,905	40,644	38,035
Tax equivalent adjustment	2,011	2,219	2,730
Net interest income (fully taxable equivalent)	$42,916	$42,863	$40,765

Rate/Volume Analysis

The table below sets forth certain information regarding changes in our interest income and interest expense for the periods indicated. For interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in volume (changes in average volume multiplied by old rate) and (ii) changes in rates (changes in rate multiplied by old average volume). Increases and decreases due to both interest rate and volume, which cannot be separated, have been allocated proportionally to the change due to volume and the change due to interest rate. Income and interest rates are on a taxable equivalent basis.

	Year Ended December 31, 2015 vs. 2014 Increase (Decrease) Due To			2014 vs. 2013 Increase (Decrease) Due To		
(In Thousands)	Volume	Rate	Net	Volume	Rate	Net
Interest income:						
Loans, tax-exempt	$555	$(171)	$384	$197	$42	$239
Loans	4,278	(1,892)	2,386	5,099	(1,115)	3,984
Fed funds sold	—	—	—	—	—	—
Taxable investment securities	(1,151)	(292)	(1,443)	(524)	(176)	(700)
Tax-exempt investment securities	(595)	(402)	(997)	(1,246)	(495)	(1,741)
Interest-bearing deposits	(22)	3	(19)	3	11	14
Total interest-earning assets	3,065	(2,754)	311	3,529	(1,733)	1,796
Interest expense:						
Savings deposits	—	(2)	(2)	3	(62)	(59)
Super Now deposits	17	(109)	(92)	37	(141)	(104)
Money market deposits	(7)	—	(7)	141	(128)	13
Time deposits	(27)	285	258	45	(121)	(76)
Short-term borrowings	47	15	62	—	(27)	(27)
Long-term borrowings	330	(269)	61	(27)	(22)	(49)
Total interest-bearing liabilities	360	(80)	280	199	(501)	(302)
Change in net interest income	$2,705	$(2,674)	$31	$3,330	$(1,232)	$2,098

PROVISION FOR LOAN LOSSES

2015 vs 2014

The provision for loan losses is based upon management’s quarterly review of the loan portfolio. The purpose of the review is to assess loan quality, identify impaired loans, analyze delinquencies, ascertain loan growth, evaluate potential charge-offs and recoveries, and assess general economic conditions in the markets served. An external independent loan review is also performed annually for the Company. Management remains committed to an aggressive program of problem loan identification and resolution.

The allowance is calculated by applying loss factors to outstanding loans by type, excluding loans for which a specific allowance has been determined. Loss factors are based on management's consideration of the nature of the portfolio segments, changes in mix and volume of the loan portfolio, and historical loan loss experience. In addition, management considers industry standards and trends with respect to nonperforming loans and its knowledge and experience with specific lending segments.

Although management believes that it uses the best information available to make such determinations and that the allowance for loan losses is adequate at December 31, 2015, future adjustments could be necessary if circumstances or economic conditions differ substantially from the assumptions used in making the initial determinations. A downturn in the local economy or employment and delays in receiving financial information from borrowers could result in increased levels of nonperforming assets and charge-offs, increased loan loss provisions and reductions in interest income. Additionally, as an integral part of the examination process, bank regulatory agencies periodically review the Banks' loan loss allowance adequacy. The banking regulators could require the recognition of additions to the loan loss allowance based on their judgment of information available to them at the time of their examination.

While determining the appropriate allowance level, management has attributed the allowance for loan losses to various portfolio segments; however, the allowance is available for the entire portfolio as needed.

The allowance for loan losses increased from $10,579,000 at December 31, 2014 to $12,044,000 at December 31, 2015. At December 31, 2015, the allowance for loan losses was 1.15% of total loans compared to 1.16% of total loans at December 31, 2014.

The provision for loan losses totaled $2,300,000 for the year ended December 31, 2015 compared to $2,850,000 for the year ended December 31, 2014. The decrease in the provision was appropriate when considering the gross loan growth offset by the $2,802,000 or 22.88% decrease in non-performing loans and level of net charge-offs. Net charge-offs of $835,000 represented 0.09% of average loans for the year ended December 31, 2015 compared to net charge-offs of $2,451,000 or 0.28% of average loans for the year ended December 31, 2014. The growth in the loan portfolio was driven by home equity product growth which historically is a lower risk product than commercial loans and requires a lower allowance for loan losses. The decrease in nonperforming loans is primarily the result of the payoff of a large commercial real estate loan and the resolution of several smaller commercial real estate loans. The majority of the nonperforming loans are centered on several loans that are either in a secured position and have sureties with a strong underlying financial position and/or a specific allowance within the allowance for loan losses. Internal loan review and analysis, coupled with the ratios noted previously, dictated a decrease in the provision for loan losses. Utilizing both internal and external resources, as noted, senior management has concluded that the allowance for loan losses remains at a level adequate to provide for probable losses inherent in the loan portfolio.

2014 vs 2013

The allowance for loan losses increased from $10,144,000 at December 31, 2013 to $10,579,000 at December 31, 2014. At December 31, 2014, the allowance for loan losses was 1.16% of total loans compared to 1.24% of total loans at December 31, 2013.

The provision for loan losses totaled $2,850,000 for the year ended December 31, 2014 compared to $2,275,000 for the year ended December 31, 2013. The increase in the provision was appropriate when considering the gross loan growth, the increase in the special mention or substandard rated loans, and charge-offs. Net charge-offs of $2,415,000 represented 0.28% of average loans for the year ended December 31, 2014 compared to net recoveries of $251,000 or 0.04% of average loans for the year ended December 31, 2013. In addition, nonperforming loans increased $2,570,000 to $12,248,000 at December 31, 2014 compared to December 31, 2013, which is primarily the result of certain commercial loans becoming non-performing. The majority of the nonperforming loans are in a secured position and have sureties with a strong underlying financial position and/or a specific allowance within the allowance for loan losses. Internal loan review and analysis, coupled with the ratios noted previously, dictated an increase in the provision for loan losses. Utilizing both internal and external resources, as noted, senior management has concluded that the allowance for loan losses remains at a level adequate to provide for probable losses inherent in the loan portfolio.

NON-INTEREST INCOME

2015 vs. 2014

Total non-interest income decreased $1,743,000 from the year ended December 31, 2014 to December 31, 2015. Excluding net security gains, non-interest income decreased $798,000 year over year. Service charges decreased slightly due to decreased level of overdraft income. Bank owned life insurance income decreased as a gain on death benefit was recognized in 2014. Insurance commissions and brokerage commissions decreased due to a shift in product mix and a decreased level of commissions received

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on each sale. Gain on sale of loans decreased due to product mix. The decrease in other income was primarily from a decreased level of debit card income.

(In Thousands)	2015 Amount	% Total	2014 Amount	% Total	Change Amount	%
Service charges	$2,383	18.67 %	$2,419	16.67 %	$(36)	(1.49)%
Net securities gains, available for sale	2,592	20.31	3,515	24.23	(923)	(26.26)
Net securities losses, trading	(22)	(0.17)	—	—	(22)	N/A
Bank owned life insurance	720	5.64	923	6.36	(203)	(21.99)
Gain on sale of loans	1,743	13.65	1,803	12.43	(60)	(3.33)
Insurance commissions	781	6.12	1,146	7.90	(365)	(31.85)
Brokerage commissions	1,064	8.34	1,077	7.42	(13)	(1.21)
Other	3,504	27.44	3,625	24.99	(121)	(3.34)
Total non-interest income	$12,765	100.00 %	$14,508	100.00 %	$(1,743)	(12.01)%

2014 vs. 2013

Total non-interest income increased $2,466,000 from the year ended December 31, 2013 to December 31, 2014. Excluding net security gains, non-interest income increased $1,368,000 year over year. Service charges increased primarily due to the impact of the Luzerne acquisition and the increased number of deposit accounts being serviced, but was partially offset by changes in the Banks' overdraft product that reduced the number of daily overdrafts on a per customer basis. Bank owned life insurance income increased primarily due to a gain on death benefit. Insurance commissions and brokerage commissions increased due in part to the acquisition of Luzerne Bank and a shift in product mix. Gain on sale of loans increased due to an increase in volume that was driven in part by the access to the greater Wilkes-Barre market provided by the acquisition of Luzerne. The increase in other income was impacted by the acquisition of Luzerne Bank as it increased the debit and credit card related income and by an increasing number of merchants that utilize our merchant card services.

(In Thousands)	2014 Amount	% Total	2013 Amount	% Total	Change Amount	%
Service charges	$2,419	16.67 %	$2,307	19.16 %	$112	4.85 %
Securities gains, net	3,515	24.23	2,417	20.07	1,098	45.43
Bank owned life insurance	923	6.36	677	5.62	246	36.34
Gain on sale of loans	1,803	12.43	1,438	11.94	365	25.38
Insurance commissions	1,146	7.90	1,084	9.00	62	5.72
Brokerage commissions	1,077	7.42	1,018	8.45	59	5.80
Other	3,625	24.99	3,101	25.76	524	16.90
Total non-interest income	$14,508	100.00 %	$12,042	100.00 %	$2,466	20.48 %

NON-INTEREST EXPENSE

2015 vs. 2014

Total non-interest expenses decreased $154,000 from the year ended December 31, 2014 to December 31, 2015. The decrease in salaries and employee benefits was attributable to the defined benefit pension plan ceasing to accrue additional benefits as of December 31, 2014. Furniture and equipment expenses increased due to the full year impact of significant upgrades to the core operating system, a new teller system, and various enhancements to other ancillary systems that were undertaken during 2014. Other expenses decreased as the acquisition of Luzerne Bank is allowing for greater purchasing power as various contracts are renewed.

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(In Thousands)	2015 Amount	% Total	2014 Amount	% Total	Change Amount	%
Salaries and employee benefits	$17,023	50.46 %	$17,273	50.97 %	$(250)	(1.45)%
Occupancy	2,248	6.66	2,301	6.79	(53)	(2.30)
Furniture and equipment	2,622	7.77	2,536	7.48	86	3.39
Pennsylvania shares tax	954	2.83	907	2.68	47	5.18
Amortization of investment in limited partnerships	661	1.96	661	1.95	—	—
FDIC deposit insurance	867	2.57	746	2.20	121	16.22
Marketing	612	1.81	532	1.57	80	15.04
Intangible amortization	311	0.92	345	1.02	(34)	(9.86)
Other	8,438	25.02	8,589	25.34	(151)	(1.76)
Total non-interest expense	$33,736	100.00 %	$33,890	100.00 %	$(154)	(0.45)%

2014 vs. 2013

Total non-interest expenses increased $3,623,000 from the year ended December 31, 2013 to December 31, 2014. The increase in salaries and employee benefits was attributable to increases in salaries and health insurance, coupled with the acquisition of Luzerne Bank. Occupancy and furniture and equipment expenses increased due to the additional branches of Luzerne Bank and significant upgrades to the core operating system, a new teller system, and various enhancements to other ancillary systems. Other expenses increased primarily due to increased fees related to providing debit card services and other expenses related to the acquisition of Luzerne Bank.

(In Thousands)	2014 Amount	% Total	2013 Amount	% Total	Change Amount	%
Salaries and employee benefits	$17,273	50.97 %	$15,415	50.93 %	$1,858	12.05 %
Occupancy	2,301	6.79	1,905	6.29	396	20.79
Furniture and equipment	2,536	7.48	1,815	6.00	721	39.72
Pennsylvania shares tax	907	2.68	864	2.85	43	4.98
Amortization of investment in limited partnerships	661	1.95	661	2.18	—	—
FDIC deposit insurance	746	2.20	594	1.96	152	25.59
Marketing	532	1.57	517	1.71	15	2.90
Intangible amortization	345	1.02	213	0.70	132	—
Other	8,589	25.34	8,283	27.38	306	3.69
Total non-interest expense	$33,890	100.00 %	$30,267	100.00 %	$3,623	11.97 %

INCOME TAXES

2015 vs. 2014

The provision for income taxes for the year ended December 31, 2015 resulted in an effective income tax rate of 21.19% compared to 20.66% for 2014. This increase is primarily the result of decreased tax-exempt investment income and bank-owned life insurance income which has resulted in a greater percentage of the pre-tax income being taxable.

The Company currently is in a deferred tax asset position due to the low income housing tax credits earned both currently and previously. Management has reviewed the deferred tax asset and has determined that the asset will be utilized within the appropriate carry forward period and therefore does not require a valuation allowance.

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2014 vs. 2013

The provision for income taxes for the year ended December 31, 2014 resulted in an effective income tax rate of 20.66% compared to 19.68% for 2013. This increase is primarily the result of increased pre-tax income which includes an increase in net securities gains of $1,098,000.

FINANCIAL CONDITION

INVESTMENTS

2015

The fair value of the investment portfolio decreased $55,983,000 from December 31, 2014 to December 31, 2015. The decrease in value is the result of the investment portfolio being actively managed in order to reduce interest rate and market risk. This process began in 2014 and is being undertaken primarily through the sale of long term municipal bonds that have a maturity date of 2025 or later and securities with a call date within the next five years. In addition, the decrease in corporate bond holdings is being undertaken to reduce risk and also in response to the changes in bank regulatory capital calculations per Basel III. The proceeds of the bond sales are primarily being deployed into loans. The strategy to sell a portion of the long-term bond portfolio does negatively impact current earnings, but this action plays a key role in our long-term asset/liability management strategy as the balance sheet is shortened to better prepare for a rising rate environment. The unrealized losses within the debt securities portfolio are the result of market activity, not credit issues/ratings, as approximately 90% of the debt securities portfolio on an amortized cost basis is currently rated A or higher by either S&P or Moody's.

2014

The fair value of the investment portfolio decreased $56,399,000 from December 31, 2013 to December 31, 2014. The decrease in value is the result of the investment portfolio being actively managed in order to reduce interest rate and market risk. This is being undertaken primarily through the sale of long term municipal bonds that have a maturity date of 2025 or later and securities with a call date within the next five years. The proceeds of the bond sales are being deployed into loans and intermediate term corporate bonds and short and intermediate term municipal bonds. The strategy to sell a portion of the long-term bond portfolio does negatively impact current earnings, but this action plays a key role in our long-term asset/liability management strategy as the balance sheet is shortened to better prepare for a rising rate environment. The unrealized losses within the debt securities portfolio are the result of market activity, not credit issues/ratings, as approximately 90% of the debt securities portfolio on an amortized cost basis is currently rated A or higher by either S&P or Moody's.

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The carrying amounts of investment securities are summarized as follows for the years ended December 31, 2015 and 2014:

(In Thousands)	2015 Balance	% Portfolio	2014 Balance	% Portfolio
U.S. Government agency securities:				
Available for sale	$3,549	2.01 %	$3,841	1.65 %
Mortgage-backed securities:				
Available for sale	10,009	5.68	12,697	5.47
Asset-backed securities:				
Available for sale	1,940	1.10	2,492	1.07
State and political securities (tax-exempt):				
Available for sale	73,110	41.49	89,024	38.34
State and political securities (taxable):				
Available for sale	13,445	7.63	19,092	8.22
Other bonds, notes and debentures:				
Available for sale	57,772	32.78	89,463	38.53
Total bonds, notes and debentures	159,825	90.69	216,609	93.28
Financial institution equity securities:				
Available for sale	11,483	6.52	9,915	4.27
Other equity securities:				
Available for sale	4,849	2.75	5,689	2.45
Trading	73	0.04	—	—
Total equity securities	16,405	9.31	15,604	6.72
Total	$176,230	100.00 %	$232,213	100.00 %

The following table shows the maturities and repricing of investment securities, at amortized cost and the weighted average yields (for tax-exempt obligations on a fully taxable basis assuming a 34% tax rate) at December 31, 2015:

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(In Thousands)	Three Months or Less	Over Three Months Through One Year	Over One Year Through Five Years	Over Five Years Through Ten Years	Over Ten Years	Amortized Cost Total
U.S. Government agency securities:						
AFS Amount	$—	$—	$—	$3,586	$—	$3,586
Yield	— %	— %	— %	1.84 %	— %	1.84 %
Mortgage-backed securities:						
AFS Amount	—	—	3,800	564	5,421	9,785
Yield	— %	— %	1.69 %	3.54 %	3.61 %	2.86 %
Asset-backed securities:						
AFS Amount	—	—	—	318	1,642	1,960
Yield	— %	— %	— %	0.75 %	1.70 %	1.54 %
State and political securities (tax-exempt):						
AFS Amount	—	807	9,973	32,371	28,736	71,887
Yield	— %	0.67 %	1.85 %	2.65 %	4.19 %	3.13 %
State and political securities (taxable):						
AFS Amount	150	778	2,538	7,953	1,686	13,105
Yield	2.65 %	3.11 %	3.40 %	4.14 %	5.62 %	4.11 %
Other bonds, notes, and debentures:						
AFS Amount	—	100	15,773	43,763	196	59,832
Yield	— %	1.40 %	2.88 %	2.66 %	6.69 %	2.73 %
Total Amount	$150	$1,685	$32,084	$88,555	$37,681	160,155
Total Yield	2.65 %	1.84 %	2.46 %	2.75 %	4.08 %	3.00 %
Equity Securities						
AFS Amount						15,611
Trading Amount						78
Total Investment Portfolio Value						$175,844
Total Investment Portfolio Yield						2.73 %

All yields represent weighted average yields expressed on a tax equivalent basis. They are calculated on the basis of the cost, adjusted for amortization of premium and accretion of discount, and effective yields weighted for the scheduled maturity of each security. The taxable equivalent adjustment represents the difference between annual income from tax-exempt obligations and the taxable equivalent of such income at the standard 34% tax rate (derived by dividing tax-exempt interest by 66%).

The distribution of credit ratings by amortized cost and estimated fair value for the debt security portfolio at December 31, 2015 follows:

(In Thousands)	A- to AAA Amortized Cost	Fair Value	B- to BBB+ Amortized Cost	Fair Value	C to CCC+ Amortized Cost	Fair Value	Not Rated Amortized Cost	Fair Value	Total Amortized Cost	Fair Value
Available for sale										
U.S. Government and agency securities	$—	$—	$—	$—	$—	$—	$3,586	$3,549	$3,586	$3,549

Mortgage-backed securities	9,785	10,009	—	—	—	—	—	—	9,785	10,009
Asset-backed securities	1,960	1,940	—	—	—	—	—	—	1,960	1,940
State and political securities	82,274	83,813	—	—	—	—	2,718	2,742	84,992	86,555
Other debt securities	49,294	48,460	10,538	9,312	—	—	—	—	59,832	57,772
Total debt securities	$143,313	$144,222	$10,538	$9,312	$—	$—	$6,304	$6,291	$160,155	$159,825

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LOAN PORTFOLIO

2015

Gross loans of $1,045,207,000 at December 31, 2015 represented an increase of $129,628,000 from December 31, 2014. The continued emphasis on well collateralized real estate loans was the primary driver of the overall increase in loans outstanding, with home equity loans and lines of credit leading the way. The emphasis to add home equity lines of credit is part of the overall strategy to shorten the duration of the earning asset portfolio in preparation of a rising interest rate environment. Several successful campaigns to increase home equity, multifamily residential, and auto loans were undertaken during 2015 with the increase in residential and commercial loans being directly correlated to the campaigns.

2014

Gross loans of $915,579,000 at December 31, 2014 represented an increase of $97,235,000 from December 31, 2013. The continued emphasis on well collateralized real estate loans was the primary driver of the overall increase in loans outstanding, with home equity loans and lines of credit leading the way. Successful campaigns to increase home equity, multifamily residential, and auto loans were undertaken during 2014 with the increase in residential and commercial loans being directly correlated to the campaigns.

The amounts of loans outstanding at the indicated dates are shown in the following table according to type of loan at December 31, 2015, 2014, 2013, 2012, and 2011:

(In Thousands)	2015 Amount	% Total	2014 Amount	% Total	2013 Amount	% Total	2012 Amount	% Total	2011 Amount	% Tota
Commercial, financial, and agricultural	$164,072	15.70 %	$124,156	13.56 %	$105,029	12.83 %	$48,455	9.46 %	$53,129	12.19
Real estate mortgage:										
Residential	526,183	50.34	457,760	50.00	399,781	48.86	252,142	49.22	179,383	41.15
Commercial	302,539	28.95	291,348	31.82	282,476	34.52	182,031	35.54	164,288	37.68
Construction	26,824	2.57	21,996	2.40	17,282	2.11	20,067	3.92	29,457	6.76
Installment loans to individuals	27,001	2.58	21,509	2.35	14,647	1.79	10,659	2.08	11,297	2.59
Net deferred loan fees and discounts	(1,412)	(0.14)	(1,190)	(0.13)	(871)	(0.11)	(1,122)	(0.22)	(1,595)	(0.37
Gross loans	$1,045,207	100.00 %	$915,579	100.00 %	$818,344	100.00 %	$512,232	100.00 %	$435,959	100.00

The amounts of domestic loans at December 31, 2015 are presented below by category and maturity:

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(In Thousands)	Commercial, financial, and agricultural	Real Estate Residential	Commercial	Construction	Installment Loans to Individuals	Total
Loans with variable interest rates:						
1 year or less	$ 26,512	$ 11,209	$ 9,540	$ 1,634	$ 1,178	$ 50,073
1 through 5 years	4,240	3,888	12,378	354	74	20,934
5 through 10 years	43,460	18,457	44,632	242	—	106,791
After 10 years	39,228	454,421	216,936	18,967	2,252	731,804
Total floating interest rate loans	113,440	487,975	283,486	21,197	3,504	909,602
Loans with fixed interest rates:						
1 year or less	5,103	1,830	2,851	1,367	487	11,638
1 through 5 years	22,867	6,744	9,123	2,869	18,060	59,663
5 through 10 years	20,099	11,487	3,328	294	3,149	38,357
After 10 years	2,563	18,147	3,751	1,097	1,801	27,359
Total predetermined interest rate loans	50,632	38,208	19,053	5,627	23,497	137,017
Total	$ 164,072	$ 526,183	$ 302,539	$ 26,824	$ 27,001	1,046,619
Net deferred loan fees and discounts						(1,412)
						$ 1,045,207

· The loan maturity information is based upon original loan terms and is not adjusted for "rollovers." In the ordinary course of business, loans maturing within one year may be renewed, in whole or in part, at interest rates prevailing at the date of renewal.

· Scheduled repayments are reported in maturity categories in which the payment is due.

The Banks do not make loans that provide for negative amortization, nor do any loans contain conversion features. The Banks did not have any foreign loans outstanding at December 31, 2015.

The following table shows the amount of accrual and nonaccrual TDRs at December 31, 2015 and 2014:

	2015			2014		
(In Thousands)	Accrual	Nonaccrual	Total	Accrual	Nonaccrual	Total
Commercial, financial, and agricultural	$ 320	$ 149	$ 469	$ 551	$ 440	$ 991
Real estate mortgage:						
Residential	1,428	353	1,781	697	181	878
Commercial	5,085	2,312	7,397	3,267	6,160	9,427
Construction	—	—	—	514	—	514
Installment loans to individuals	—	—	—	—	—	—
	$ 6,833	$ 2,814	$ 9,647	$ 5,029	$ 6,781	$ 11,810

ALLOWANCE FOR LOAN LOSSES

2015

The allowance for loan losses represents the amount which management estimates is adequate to provide for probable losses inherent in its loan portfolio, as of the consolidated balance sheet date. All loan losses are charged to the allowance and all recoveries are credited to it per the allowance method of providing for loan losses. The allowance for loan losses is established through a provision for loan losses charged to operations. The provision for loan losses is based upon management's quarterly review of the loan portfolio. The purpose of the review is to assess loan quality, identify impaired loans, analyze delinquencies, ascertain loan growth, evaluate potential charge-offs and recoveries, and assess general economic conditions in the markets served. An external independent loan review is also performed annually for the Banks. Management remains committed to an aggressive program of problem loan identification and resolution.

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The allowance is calculated by applying loss factors to outstanding loans by type, excluding loans for which a specific allowance has been determined. Loss factors are based on management's consideration of the nature of the portfolio segments, changes in mix and volume of the loan portfolio, and historical loan loss experience. In addition, management considers industry standards and trends with respect to nonperforming loans and its knowledge and experience with specific lending segments.

The allowance for loan losses increased from $10,579,000 at December 31, 2014 to $12,044,000 at December 31, 2015. At December 31, 2015, the allowance for loan losses was 1.15% of total loans compared to 1.16% of total loans at December 31, 2014. The decrease in the allowance for loan losses to total loans was the result of the increased allowance for loan losses that was more than offset by the increase in loan growth. The growth in the loan portfolio was driven by home equity product growth which historically is a lower risk product than commercial loans and requires a lower allowance for loan losses. Net loan charge-offs of $835,000 or 0.09% of average loans for the year ended December 31, 2015 limited the impact of the provision for loan losses of $2,300,000. Management concluded that the allowance for loan losses is adequate to provide for probable losses inherent in its loan portfolio as of the balance sheet date as noted in the provision for loan losses discussion.

Based on management's loan-by-loan review, the past performance of the borrowers, and current economic conditions, including recent business closures and bankruptcy levels, management does not anticipate any current losses related to nonaccrual, nonperforming, or classified loans above those that have already been considered in its overall judgment of the adequacy of the allowance for loan losses.

2014

The allowance for loan losses increased from $10,144,000 at December 31, 2013 to $10,579,000 at December 31, 2014. At December 31, 2014, the allowance for loan losses was 1.16% of total loans compared to 1.24% of total loans at December 31, 2013. The decrease in the allowance for loan losses to total loans was the result of the increased allowance for loan losses that was more than offset by the increase in loan growth. The increase in the allowance for loan losses was appropriate when considering the gross loan growth, level of commercial loans, declining impact of the Marcellus Shale natural gas exploration, and the continued uncertain economic environment. Net loan charge-offs of $2,415,000 limited the impact of the provision for loan losses of $2,850,000.

Allocation of The Allowance For Loan Losses

	December 31, 2015		December 31, 2014		December 31, 2013		December 31, 2012		December 31, 2011	
(In Thousands)	Amount	% Total	Amount	% Total	Amount	% Total	Amount	% Total	Amount	% Total
Balance at end of period applicable to:										
Commercial, financial, and agricultural	$1,532	15.68 %	$1,124	13.54 %	$474	12.82 %	$361	9.44 %	$418	12.14 %
Real estate mortgage:										
Residential	5,116	50.27	3,755	49.93	3,917	48.80	1,954	49.11	939	41.00
Commercial	4,217	28.91	4,205	31.78	4,079	34.48	3,831	35.46	2,651	37.55
Construction	160	2.56	786	2.40	741	2.11	950	3.91	2,775	6.73
Installment loans to	243	2.58	245	2.35	139	1.79	144	2.08	190	2.58

individuals										
Unallocated	776	—	464	—	794	—	377	—	181	—
	$12,044	100.00 %	$10,579	100.00 %	$10,144	100.00 %	$7,617	100.00 %	$7,154	100.00 %

NONPERFORMING LOANS

The decrease in nonperforming loans is primarily the result of the payoff of a large commercial real estate loan and the resolution of several smaller commercial real estate loans. The majority of the nonperforming loans are centered on several loans that are either in a secured position and have sureties with a strong underlying financial position and/or a specific allowance within the allowance for loan losses.

The following table presents information concerning nonperforming loans. The accrual of interest will be discontinued when the principal or interest of a loan is in default for 90 days or more, or as soon as payment is questionable, unless the loan is well secured and in the process of collection. Consumer loans and residential real estate loans secured by 1 to 4 family dwellings are not

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ordinarily subject to those guidelines. The reversal of previously accrued but uncollected interest applicable to any loan placed in a nonaccrual status and the treatment of subsequent payments of either principal or interest is handled in accordance with GAAP. These principles do not require a write-off of previously accrued interest if principal and interest are ultimately protected by sound collateral values. A nonperforming loan may be restored to accruing status when:

1. Principal and interest is no longer due and unpaid;
2. It becomes well secured and in the process of collection; and
3. Prospects for future contractual payments are no longer in doubt.

	Total Nonperforming Loans		
(In Thousands)	90 Days Past Due	Nonaccrual	Total
2015	$979	$8,467	$9,446
2014	387	11,861	12,248
2013	604	9,074	9,678
2012	351	11,355	11,706
2011	384	11,625	12,009

The level of non-accruing loans continues to fluctuate annually and is attributed to the various economic factors experienced both regionally and nationally. Overall, the portfolio is well secured with a majority of the balance making regular payments or scheduled to be satisfied in the near future. Presently, there are no significant amounts of loans where serious doubts exist as to the ability of the borrower to comply with the current loan payment terms which are not included in the nonperforming categories as indicated above.

Management’s judgment in determining the amount of the additions to the allowance charged to operating expense considers the following factors with no single factor being determinative:

1. Economic conditions and the impact on the loan portfolio.
2. Analysis of past loan charge-offs experienced by category and comparison to outstanding loans.
3. Effect of problem loans on overall portfolio quality.
4. Reports of examination of the loan portfolio by the Department and the FDIC.

DEPOSITS

2015 vs. 2014

Total average deposits increased $26,704,000 or 2.72% from 2014 to 2015. The growth is a result of an emphasis to increase and solidify deposit relationships by focusing on core deposits, not time deposits. The actions caused average core deposits, which exclude time deposits, to increase to 78.16% in 2015 from 77.25% for 2014. The level of deposits has been negatively impacted by the Commonwealth of Pennsylvania budget impasse which has resulted in a decreased level of deposits held by the various governmental entities serviced by the Banks.

2014 vs. 2013

Total average deposits increased $142,246,000 or 16.93% from 2013 to 2014. The result of an emphasis to increase and solidify deposit relationships by focusing on core deposits, not time deposits. The actions caused average core deposits, which exclude time deposits, to increase to 77.25% in 2014 from 75.06% for 2013. In addition to the emphasis on growing core deposits by utilizing marketing strategies, the core deposit growth received a lift from the natural gas exploration throughout our market footprint and municipal account gathering efforts.

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The average amount and the average rate paid on deposits are summarized below for the years ended December 31, 2015, 2014, and 2013:

(In Thousands)	2015 Average Amount	Rate		2014 Average Amount	Rate		2013 Average Amount	Rate	
Noninterest-bearing	$251,029	0.00	%	$225,981	0.00	%	$174,909	0.00	%
Savings	143,055	0.04		140,575	0.06		118,125	0.12	
Super Now	187,396	0.26		182,229	0.32		154,131	0.45	
Money Market	207,252	0.27		210,066	0.27		183,460	0.30	
Time	220,360	0.92		223,537	0.79		209,517	0.88	
Total average deposits	$1,009,092	0.31	%	$982,388	0.31	%	$840,142	0.38	%

SHAREHOLDERS' EQUITY

2015

Shareholders' equity increased $312,000 to $136,279,000 at December 31, 2015 compared to December 31, 2014. Since December 31, 2014, treasury stock purchases of $2,603,000 for 60,018 shares were completed as part of the stock repurchase plan. The change in accumulated other comprehensive loss from $1,667,000 at December 31, 2014 to $3,799,000 at December 31, 2015 is a result of a decrease in unrealized gains on available for sale securities from an unrealized gain of $2,930,000 at December 31, 2014 to an unrealized gain of $258,000 at December 31, 2015. The amount of accumulated other comprehensive loss at December 31, 2015 was also impacted by the change in net excess of the projected benefit obligation over the fair value of the plan assets of the defined benefit pension plan resulting in a decrease in the net loss of $540,000 to $4,057,000 at December 31, 2015. The current level of shareholders' equity equates to a book value per share of $28.71 at December 31, 2015 compared to $28.30 at December 31, 2014 and an equity to asset ratio of 10.32% at December 31, 2015 compared to 10.92% at December 31, 2014. Excluding goodwill and intangibles, book value per share was $24.84 at December 31, 2015 compared to $24.44 at December 31, 2014. Dividends declared for each of the three and twelve months ended December 31, 2015 and 2014 were $0.47 and $1.88 per share.

2014

Shareholders' equity increased $8,152,000 to $135,967,000 at December 31, 2014 compared to December 31, 2013. The accumulated other comprehensive loss of $1,667,000 at December 31, 2014 is a result of an increase in unrealized gains on available for sale securities from an unrealized loss of $2,169,000 at December 31, 2013 to an unrealized gain of $2,930,000 at December 31, 2014. The amount of accumulated other comprehensive loss at December 31, 2014 was also impacted by the change in net excess of the projected benefit obligation over the market value of the plan assets of the defined benefit pension plan resulting in an increase in the net loss of $1,872,000 to $4,597,000 at December 31, 2014. The current level of shareholders' equity equates to a book value per share of $28.30 at December 31, 2014 compared to $26.52 at December 31, 2013 and an equity to asset ratio of 10.92% at December 31, 2014 compared to 10.55% at December 31, 2013. Excluding goodwill and intangibles, book value per share was $24.44 at December 31, 2014 compared to $22.60 at December 31, 2013. Dividends declared for the twelve months ended December 31, 2014 were $1.88 per share compared to $2.13, which included a special cash dividend of $0.25 per share declared in the first quarter 2013, for the twelve months ended December 31, 2013.

Bank regulators have risk based capital guidelines. Under these guidelines the Company and each Bank are required to maintain minimum ratios of core capital and total qualifying capital as a percentage of risk weighted assets and certain off-balance sheet items. At December 31, 2015, both the Company's and each Bank's required ratios were well above the minimum ratios as follows:

	Company	Jersey Shore State Bank	Luzerne Bank	Minimum Standards
Common equity tier 1 capital ratio	11.24 %	10.70 %	10.66 %	4.50 %
Tier 1 capital ratio	11.24 %	10.70 %	10.66 %	6.00 %
Total capital ratio	12.38 %	11.91 %	11.61 %	8.00 %

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For a more comprehensive discussion of these requirements, see “Regulation and Supervision” in Item 1 of the Annual Report on Form 10-K. Management believes that the Company will continue to exceed regulatory capital requirements.

RETURN ON EQUITY AND ASSETS

The ratio of net income to average total assets and average shareholders’ equity, and other certain equity ratios are presented as follows:

	2015		2014		2013	
Percentage of net income to:						
Average total assets	1.08	%	1.19	%	1.32	%
Average shareholders’ equity	10.11	%	10.79	%	12.36	%
Percentage of dividends declared to net income	64.52	%	61.99	%	67.88	%
Percentage of average shareholders’ equity to average total assets	10.68	%	11.05	%	10.70	%

LIQUIDITY, INTEREST RATE SENSITIVITY, AND MARKET RISK

The Asset/Liability Committee addresses the liquidity needs of the Company to ensure that sufficient funds are available to meet credit demands and deposit withdrawals as well as to the placement of available funds in the investment portfolio. In assessing liquidity requirements, equal consideration is given to the current position as well as the future outlook.

The following liquidity measures are monitored for compliance and were within the limits cited at December 31, 2015, except for Net Loans to Total Deposits which was 100.12%:

1. Net Loans to Total Assets, 85% maximum
2. Net Loans to Total Deposits, 100% maximum
3. Cumulative 90 day Maturity GAP %, +/- 20% maximum
4. Cumulative 1 Year Maturity GAP %, +/- 25% maximum

Fundamental objectives of the Company’s asset/liability management process are to maintain adequate liquidity while minimizing interest rate risk. The maintenance of adequate liquidity provides the Company with the ability to meet its financial obligations to depositors, loan customers, and shareholders. Additionally, it provides funds for normal operating expenditures and business opportunities as they arise. The objective of interest rate sensitivity management is to increase net interest income by managing interest sensitive assets and liabilities in such a way that they can be repriced in response to changes in market interest rates.

The Company, like other financial institutions, must have sufficient funds available to meet its liquidity needs for deposit withdrawals, loan commitments, and expenses. In order to control cash flow, the Company estimates future flows of cash from deposits and loan payments. The primary sources of funds are deposits, principal and interest payments on loans and mortgage-backed securities, as well as FHLB borrowings. Funds generated are used principally to fund loans and purchase investment securities. Management believes the Company has adequate resources to meet its normal funding requirements.

Management monitors the Company’s liquidity on both a short and long-term basis, thereby, providing management necessary information to react to current balance sheet trends. Cash flow needs are assessed and sources of funds are determined. Funding strategies consider both customer needs and economical cost. Both short and long term funding needs are addressed by maturities and sales of available for sale investment securities, loan repayments and maturities, and liquidating money market investments such as federal funds sold. The use of these resources, in conjunction with access to credit, provides core ingredients to satisfy depositor, borrower, and creditor needs.

Management monitors and determines the desirable level of liquidity. Consideration is given to loan demand, investment opportunities, deposit pricing and growth potential, as well as the current cost of borrowing funds. The Company has a current borrowing capacity at the FHLB of $500,839,000 with $118,929,000 utilized, leaving $381,910,000 available. In addition to this credit arrangement, the Company has additional lines of credit with correspondent banks of $35,413,000. The Company's management believes that it has sufficient liquidity to satisfy estimated short-term and long-term funding needs.

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Interest rate sensitivity, which is closely related to liquidity management, is a function of the repricing characteristics of the Company's portfolio of assets and liabilities. Asset/liability management strives to match maturities and rates between loan and investment security assets with the deposit liabilities and borrowings that fund them. Successful asset/liability management results in a balance sheet structure which can cope effectively with market rate fluctuations. The matching process is affected by segmenting both assets and liabilities into future time periods (usually 12 months, or less) based upon when repricing can be effected. Repriceable assets are subtracted from repriceable liabilities, for a specific time period to determine the "gap", or difference. Once known, the gap is managed based on predictions about future market interest rates. Intentional mismatching, or gapping, can enhance net interest income if market rates move as predicted. However, if market rates behave in a manner contrary to predictions, net interest income will suffer. Gaps, therefore, contain an element of risk and must be prudently managed. In addition to gap management, the Company has an asset liability management policy which incorporates a market value at risk calculation which is used to determine the effects of interest rate movements on shareholders' equity and a simulation analysis to monitor the effects of interest rate changes on the Company's balance sheet.

The Company currently maintains a gap position of being liability sensitive. The Company has taken this position as it has decreased the duration of the time deposit portfolio over the last several years and has increased the use of rate sensitive funding sources such as overnight borrowings and core deposits (non-time deposits), while continuing to maintain a primarily fixed rate earning asset portfolio with a duration greater than the liabilities utilized to fund earning assets. Lengthening of the liability portfolio coupled with the addition of limited short-term assets is being undertaken. These actions are expected to reduce, but not eliminate, the liability sensitive structure of the balance sheet.

A market value at risk calculation is utilized to monitor the effects of interest rate changes on the Company's balance sheet and more specifically shareholders' equity. The Company does not manage the balance sheet structure in order to maintain compliance with this calculation. The calculation serves as a guideline with greater emphasis placed on interest rate sensitivity. Changes to calculation results from period to period are reviewed as changes in results could be a signal of future events.

INTEREST RATE SENSITIVITY

In this analysis the Company examines the result of various changes in market interest rates in 100 basis point increments and their effect on net interest income. It is assumed that the change is instantaneous and that all rates move in a parallel manner. Assumptions are also made concerning prepayment speeds on mortgage loans and mortgage securities.

The following is a rate shock forecast for the twelve month period ended December 31, 2016 assuming a static balance sheet as of December 31, 2015.

	Parallel Rate Shock in Basis Points						
(In Thousands)	(200)	(100)	Static	100	200	300	400
Net interest income	$36,618	$39,141	$41,741	$43,705	$45,491	$46,842	$47,798
Change from static	(5,123)	(2,600)	—	1,964	3,750	5,101	6,057
Percent change from static	-12.27%	-6.23%	—	4.71%	8.98%	12.22%	14.51%

The model utilized to create the report presented above makes various estimates at each level of interest rate change regarding cash flow from principal repayment on loans and mortgage-backed securities and/or call activity on investment securities. Actual results could differ significantly from these estimates which would result in significant differences in the calculated projected change. In addition, the limits stated above do not necessarily represent the level of change under which management would undertake specific measures to realign its portfolio in order to reduce the projected level of change. Generally, management believes the Company is well positioned to respond expeditiously when the market interest rate outlook changes.

INFLATION

The asset and liability structure of a financial institution is primarily monetary in nature; therefore, interest rates rather than inflation have a more significant impact on the Company's performance. Interest rates are not always affected in the same direction or magnitude as prices of other goods and services, but are reflective of fiscal policy initiatives or economic factors that are not measured by a price index.

CRITICAL ACCOUNTING POLICIES

The Company's accounting policies are integral to understanding the results reported. The accounting policies are described in detail in Note 1 of the "Notes to Consolidated Financial Statements." Our most complex accounting policies require management's

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judgment to ascertain the valuation of assets, liabilities, commitments, and contingencies. We have established detailed policies and control procedures that are intended to ensure valuation methods are well controlled and applied consistently from period to period. In addition, the policies and procedures are intended to ensure that the process for changing methodologies occurs in an appropriate manner. The following is a brief description of our current accounting policies involving significant management valuation judgments.

Other Than Temporary Impairment of Debt and Equity Securities

Debt and equity securities are evaluated periodically to determine whether a decline in their value is other than temporary. Management utilizes criteria such as the magnitude and duration of the decline, in addition to the reason underlying the decline, to determine whether the loss in value is other than temporary. The term "other than temporary" is not intended to indicate that the decline is permanent. It indicates that the prospects for a near term recovery of value are not necessarily favorable, or that there is a lack of evidence to support fair values equal to, or greater than, the carrying value of the investment. Once a decline in value is determined to be other than temporary, the value of the security is reduced and a corresponding charge to earnings is recognized. For a full discussion of the Company's methodology of assessing impairment, refer to Note 4 of the "Notes to Consolidated Financial Statements."

Allowance for Loan Losses

Arriving at an appropriate level of allowance for loan losses involves a high degree of judgment. The Company's allowance for loan losses provides for probable losses based upon evaluations of known and inherent risks in the loan portfolio.

Management uses historical information to assess the adequacy of the allowance for loan losses as well as the prevailing business environment; as it is affected by changing economic conditions and various external factors, which may impact the portfolio in ways currently unforeseen. The allowance is increased by provisions for loan losses and by recoveries of loans previously charged-off and reduced by loans charged-off. For a full discussion of the Company's methodology of assessing the adequacy of the reserve for allowance for loan losses, refer to Note 1 of the "Notes to Consolidated Financial Statements."

Goodwill and Other Intangible Assets

As discussed in Note 8 of the "Notes to Consolidated Financial Statements," the Company must assess goodwill and other intangible assets each year for impairment. This assessment involves estimating cash flows for future periods. If the future cash flows were less than the recorded goodwill and other intangible assets balances, we would be required to take a charge against earnings to write down the assets to the lower value.

Deferred Tax Assets

Management uses an estimate of future earnings to support their position that the benefit of their deferred tax assets will be realized. If future income should prove non-existent or less than the amount of the deferred tax assets within the tax years to which they may be applied, the asset may not be realized and the Company's net income will be reduced. The Company's deferred tax assets are described further in Note 12 of the "Notes to Consolidated Financial Statements."

Pension Benefits

Pension costs and liabilities are dependent on assumptions used in calculating such amounts. These assumptions include discount rates, benefits earned, interest costs, expected return on plan assets, mortality rates, and other factors. In accordance with GAAP, actual results that differ from the assumptions are accumulated and amortized over future periods and, therefore, generally affect recognized expense and the recorded obligation of future periods. While management believes that the assumptions used are appropriate, differences in actual experience or changes in assumptions may affect the Company's pension obligations and future expense. Our pension benefits are described further in Note 13 of the "Notes to Consolidated Financial Statements."

CONTRACTUAL OBLIGATIONS

The Company has various financial obligations, including contractual obligations which may require future cash payments. The following table presents, as of December 31, 2015, significant fixed and determinable contractual obligations to third parties by payment date. Further discussion of the nature of each obligation is included in the "Notes to Consolidated Financial Statements."

(In Thousands)	Payments Due In One Year or Less	One to Three Years	Three to Five Years	Over Five Years	Total
Deposits without a stated maturity	$810,504	$—	$—	$—	$810,504
Time deposits	81,010	106,422	31,889	2,056	221,377
Repurchase agreements	18,334	—	—	—	18,334
Short-term borrowings	28,304	—	—	—	28,304
Long-term borrowings	5,027	57,057	25,684	3,257	91,025
Operating leases	482	794	476	823	2,575

The Company's operating lease obligations represent short and long-term lease and rental payments for branch facilities and equipment. The Bank leases certain facilities under operating leases which expire on various dates through 2027. Renewal options are available on the majority of these leases.

CAUTIONARY STATEMENT FOR PURPOSES OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This Report contains certain "forward-looking statements" including statements concerning plans, objectives, future events or performance and assumptions and other statements which are other than statements of historical fact. The Company wishes to caution readers that the following important factors, among others, may have affected and could in the future affect the Company's actual results and could cause the Company's actual results for subsequent periods to differ materially from those expressed in any forward-looking statement made by or on behalf of the Company herein: (i) the effect of changes in laws and regulations, including federal and state banking laws and regulations, with which the Company must comply, and the associated costs of compliance with such laws and regulations either currently or in the future as applicable; (ii) the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies as well as by the Financial Accounting Standards Board, or of changes in the Company's organization, compensation and benefit plans; (iii) the effect on the Company's competitive position within its market area of the increasing consolidation within the banking and financial services industries, including the increased competition from larger regional and out-of-state banking organizations as well as non-bank providers of various financial services; (iv) the effect of changes in interest rates; (v) the effect of changes in the business cycle and downturns in the local, regional or national economies; and (vi) the successful integration of the business and operations of Luzerne with those of the Company.

ITEM 7A QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk for the Company is comprised primarily from interest rate risk exposure and liquidity risk. Interest rate risk and liquidity risk management is performed at the Banks' level as well as the Company level. The Company's interest rate sensitivity is monitored by management through selected interest rate risk measures produced internally. Additional information and details are provided in the Interest Sensitivity section of Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations.

Generally, management believes the Company is well positioned to respond expeditiously when the market interest rate outlook changes.

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ITEM 8 FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
Penns Woods Bancorp, Inc.

We have audited the accompanying consolidated balance sheet of Penns Woods Bancorp, Inc. and subsidiaries as of December 31, 2015 and 2014, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2015. These consolidated financial statements are the responsibility of Penns Woods Bancorp, Inc.'s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Penns Woods Bancorp, Inc. and subsidiaries as of December 31, 2015 and 2014, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2015, in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Penns Woods Bancorp, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2015, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013, and our report dated March 10, 2016, expressed an unqualified opinion on the effectiveness of Penns Woods Bancorp, Inc.'s internal control over financial reporting.

Wexford, Pennsylvania
March 10, 2016

PENNS WOODS BANCORP, INC.
CONSOLIDATED BALANCE SHEET

	December 31,	
(In Thousands, Except Share Data)	2015	2014
ASSETS:		
Noninterest-bearing balances	$22,044	$19,403
Interest-bearing deposits in other financial institutions	752	505
Total cash and cash equivalents	22,796	19,908
Investment securities available for sale, at fair value	176,157	232,213
Investment securities, trading	73	—
Loans held for sale	757	550
Loans	1,045,207	915,579
Allowance for loan losses	(12,044)	(10,579)
Loans, net	1,033,163	905,000
Premises and equipment, net	21,830	21,109
Accrued interest receivable	3,686	3,912
Bank-owned life insurance	26,667	25,959
Investment in limited partnerships	899	1,560
Goodwill	17,104	17,104
Intangibles	1,240	1,456
Deferred tax asset	8,990	8,101
Other assets	6,695	8,139
TOTAL ASSETS	$1,320,057	$1,245,011
LIABILITIES:		
Interest-bearing deposits	$751,797	$738,041
Noninterest-bearing deposits	280,083	243,378
Total deposits	1,031,880	981,419
Short-term borrowings	46,638	40,818
Long-term borrowings	91,025	71,176
Accrued interest payable	426	381
Other liabilities	13,809	15,250
TOTAL LIABILITIES	1,183,778	1,109,044
SHAREHOLDERS' EQUITY:		
Preferred stock, no par value, 3,000,000 shares authorized; no shares issued	—	—
Common stock, par value $8.33, 15,000,000 shares authorized; 5,004,984 and 5,002,649 shares issued	41,708	41,688
Additional paid-in capital	49,992	49,896
Retained earnings	58,038	53,107
Accumulated other comprehensive loss:		
Net unrealized gain on available for sale securities	258	2,930
Defined benefit plan	(4,057)	(4,597)
Treasury stock at cost, 257,852 and 197,834 shares	(9,660)	(7,057)
TOTAL SHAREHOLDERS' EQUITY	136,279	135,967
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$1,320,057	$1,245,011

See accompanying notes to the consolidated financial statements.

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PENNS WOODS BANCORP, INC.
CONSOLIDATED STATEMENT OF INCOME

	Year Ended December 31,		
(In Thousands, Except Per Share Data)	2015	2014	2013
INTEREST AND DIVIDEND INCOME:			
Loans, including fees	$39,134	$36,495	$32,353
Investment securities:			
Taxable	3,426	5,111	6,034
Tax-exempt	2,795	3,453	4,602
Dividend and other interest income	769	547	310
TOTAL INTEREST AND DIVIDEND INCOME	46,124	45,606	43,299
INTEREST EXPENSE:			
Deposits	3,129	2,995	3,221
Short-term borrowings	116	54	81
Long-term borrowings	1,974	1,913	1,962
TOTAL INTEREST EXPENSE	5,219	4,962	5,264
NET INTEREST INCOME	40,905	40,644	38,035
PROVISION FOR LOAN LOSSES	2,300	2,850	2,275
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	38,605	37,794	35,760
NON-INTEREST INCOME:			
Service charges	2,383	2,419	2,307
Securities gains, available for sale	2,592	3,515	2,417
Securities losses, trading	(22)	—	—
Bank-owned life insurance	720	923	677
Gain on sale of loans	1,743	1,803	1,438
Insurance commissions	781	1,146	1,084
Brokerage commissions	1,064	1,077	1,018
Other	3,504	3,625	3,101
TOTAL NON-INTEREST INCOME	12,765	14,508	12,042
NON-INTEREST EXPENSE:			
Salaries and employee benefits	17,023	17,273	15,415
Occupancy	2,248	2,301	1,905
Furniture and equipment	2,622	2,536	1,815
Pennsylvania shares tax	954	907	864
Amortization of investment in limited partnerships	661	661	661
Federal Deposit Insurance Corporation deposit insurance	867	746	594
Marketing	612	532	517
Intangible amortization	311	345	213
Other	8,438	8,589	8,283
TOTAL NON-INTEREST EXPENSE	33,736	33,890	30,267
INCOME BEFORE INCOME TAX PROVISION	17,634	18,412	17,535
INCOME TAX PROVISION	3,736	3,804	3,451

NET INCOME	$13,898	$14,608	$14,084
EARNINGS PER SHARE - BASIC AND DILUTED	$2.91	$3.03	$3.19
WEIGHTED AVERAGE SHARES OUTSTANDING - BASIC AND DILUTED	4,772,239	4,816,149	4,410,626
DIVIDENDS PER SHARE	$1.88	$1.88	$2.13

See accompanying notes to the consolidated financial statements.

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PENNS WOODS BANCORP, INC.
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Year Ended December 31,		
(In Thousands)	2015	2014	2013
Net Income	$13,898	$14,608	$14,084
Other comprehensive (loss) income:			
Change in unrealized gain (loss) on available for sale securities	(1,457)	11,242	(16,270)
Tax effect	495	(3,822)	5,532
Net realized gain included in net income	(2,592)	(3,515)	(2,417)
Tax effect	882	1,195	822
Amortization (accretion) of unrecognized pension and post-retirement items	817	(2,837)	3,155
Tax effect	(277)	964	(1,073)
Total other comprehensive (loss) income	(2,132)	3,227	(10,251)
Comprehensive income	$11,766	$17,835	$3,833

See accompanying notes to the consolidated financial statements.

PENNS WOODS BANCORP, INC.
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(In Thousands, Except Per Share Data)	COMMON STOCK SHARES	COMMON STOCK AMOUNT	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	ACCUMULATED OTHER COMPREHENSIVE (LOSS) INCOME	TREASURY STOCK	TOTAL SHAREHOLDERS' EQUITY
Balance, December 31, 2012	4,019,112	$33,492	$18,157	$43,030	$5,357	$(6,310)	$93,726
Net income				14,084			14,084
Other comprehensive loss					(10,251)		(10,251)
Dividends declared, ($2.13 per share)				(9,560)			(9,560)
Common shares issued for acquisition of Luzerne National Bank Corporation	978,977	8,158	31,578				39,736
Common shares issued for employee stock purchase plan	1,840	15	65				80
Balance, December 31, 2013	4,999,929	41,665	49,800	47,554	(4,894)	(6,310)	127,815
Net income				14,608			14,608
Other comprehensive income					3,227		3,227
Dividends declared, ($1.88 per share)				(9,055)			(9,055)
Common shares issued for employee stock purchase plan	2,720	23	96				119
Purchase of treasury stock (17,238 shares)						(747)	(747)
Balance, December 31, 2014	5,002,649	41,688	49,896	53,107	(1,667)	(7,057)	135,967
Net income				13,898			13,898
Other comprehensive loss					(2,132)		(2,132)
Dividends declared, ($1.88 per share)				(8,967)			(8,967)

Common shares issued for employee stock purchase plan	2,335	20	96				116
Purchase of treasury stock (60,018 shares)						(2,603)	(2,603)
Balance, December 31, 2015	5,004,984	$41,708	$49,992	$58,038	$(3,799)	$(9,660)	$136,279

See accompanying notes to the consolidated financial statements.

PENNS WOODS BANCORP, INC.
CONSOLIDATED STATEMENT OF CASH FLOWS

	Year Ended December 31,		
(In Thousands)	2015	2014	2013
OPERATING ACTIVITIES:			
Net Income	$13,898	$14,608	$14,084
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	3,366	3,078	1,448
Amortization of intangible assets	311	345	213
Provision for loan losses	2,300	2,850	2,275
Accretion and amortization of investment security discounts and premiums	873	672	69
Securities gains, net	(2,592)	(3,515)	(2,417)
Originations of loans held for sale	(56,058)	(51,119)	(51,512)
Proceeds of loans held for sale	57,594	53,998	55,098
Gain on sale of loans	(1,743)	(1,803)	(1,438)
Net securities losses, trading	22	—	—
Proceeds from sales of trading securities	709	—	—
Purchases of trading securities	(804)	—	—
Earnings on bank-owned life insurance	(720)	(923)	(677)
Decrease in deferred tax asset	209	124	123
Other, net	(1,630)	423	61
Net cash provided by operating activities	15,735	18,738	17,327
INVESTING ACTIVITIES:			
Investment securities available for sale:			
Proceeds from sales	65,672	102,145	79,114
Proceeds from calls and maturities	22,859	13,354	16,359
Purchases	(32,776)	(47,902)	(90,179)
Net increase in loans	(130,803)	(101,816)	(55,953)
Acquisition of bank premises and equipment	(2,285)	(2,795)	(4,918)
Proceeds from the sale of foreclosed assets	1,868	1,059	143
Purchase of bank-owned life insurance	(30)	(30)	(981)
Proceeds from bank-owned life insurance death benefit	—	367	—
Proceeds from redemption of regulatory stock	10,790	3,955	3,239
Purchases of regulatory stock	(12,818)	(4,583)	(2,384)
Acquisition, net of cash acquired	—	—	17,487
Net cash used for investing activities	(77,523)	(36,246)	(38,073)
FINANCING ACTIVITIES:			
Net increase (decrease) in interest-bearing deposits	13,756	(17,584)	34,114
Net increase in noninterest-bearing deposits	36,705	26,001	19,906
Proceeds from long-term borrowings	30,625	—	452
Repayment of long-term borrowings	(10,776)	(26)	(5,528)
Net increase (decrease) in short-term borrowings	5,820	14,102	(9,254)
Dividends paid	(8,967)	(9,055)	(9,560)
Issuance of common stock	116	119	80
Purchase of treasury stock	(2,603)	(747)	—
Net cash provided by financing activities	64,676	12,810	30,210
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	2,888	(4,698)	9,464
CASH AND CASH EQUIVALENTS, BEGINNING	19,908	24,606	15,142

CASH AND CASH EQUIVALENTS, ENDING	$22,796	$19,908	$24,606

See accompanying notes to the consolidated financial statements.

	Year Ended December 31,		
(In Thousands)	2015	2014	2013
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:			
Interest paid	$5,174	$4,986	5,225
Income taxes paid	2,933	3,750	3,998
Transfer of loans to foreclosed real estate	340	2,166	470
Acquisition of Luzerne National Bank Corporation			
Non-cash assets acquired:			
Securities available for sale			21,783
Loans			250,377
Premises and equipment, net			8,014
Accrued interest receivable			726
Bank-owned life insurance			7,419
Intangibles			2,015
Other assets			2,636
Goodwill			14,072
			307,042
Liabilities assumed:			
Deferred tax liability			76
Interest-bearing deposits			194,438
Noninterest-bearing deposits			82,518
Short-term borrowings			2,766
Accrued interest payable			103
Other liabilities			4,892
			284,793
Net non-cash assets acquired			22,249
Cash and cash equivalents acquired			$20,363

See accompanying notes to the consolidated financial statements.

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PENNS WOODS BANCORP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 — OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Penns Woods Bancorp, Inc. and its wholly owned subsidiaries, Jersey Shore State Bank ("JSSB"), Luzerne Bank ("Luzerne" collectively with JSSB "Banks"), Woods Real Estate Development Co., Inc., Woods Investment Company, Inc., and The M Group Inc. D/B/A The Comprehensive Financial Group ("The M Group"), a wholly owned subsidiary of JSSB, (collectively, the "Company"). All significant intercompany balances and transactions have been eliminated.

Nature of Business

The Banks engage in a full-service commercial banking business, making available to the community a wide range of financial services including, but not limited to, installment loans, credit cards, mortgage and home equity loans, lines of credit, construction financing, farm loans, community development loans, loans to non-profit entities and local government, and various types of demand and time deposits including, but not limited to, checking accounts, savings accounts, money market deposit accounts, certificates of deposit, and IRAs. Deposits are insured by the Federal Deposit Insurance Corporation ("FDIC") to the extent provided by law.

The financial services are provided by the Banks to individuals, partnerships, non-profit organizations, and corporations through their twenty-three offices located in Clinton, Lycoming, Centre, Montour, Union, and Luzerne Counties, Pennsylvania.

Woods Real Estate Development Co., Inc. engages in real estate transactions on behalf of Penns Woods Bancorp, Inc. and the Banks.

Woods Investment Company, Inc., a Delaware holding company, is engaged in investing activities.

The M Group engages in securities brokerage and financial planning services, which include the sale of life insurance products, annuities, and estate planning services.

Operations are managed and financial performance is evaluated on a corporate-wide basis. Accordingly, all financial service operations are considered by management to be aggregated in one reportable operating segment.

Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, valuation of net deferred tax assets, impairment of goodwill, other than temporary impairment of debt and equity securities, fair value of financial instruments, and the valuation of real estate acquired through, or in lieu of, foreclosure on settlement of debt.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and in banks and federal funds sold. Interest-earning deposits mature within 90 days and are carried at cost. Net cash flows are reported for loan, deposit, and short-term borrowing transactions.

Restrictions on Cash and Cash Equivalents

Based on deposit levels, the Banks must maintain cash and other reserves with the Federal Reserve Bank of Philadelphia (FRB).

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Investment Securities

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

Securities are periodically reviewed for other-than-temporary impairment based upon a number of factors, including, but not limited to, the length of time and extent to which the fair value has been less than cost, the financial condition of the underlying issuer, the ability of the issuer to meet contractual obligations, the likelihood of the security's ability to recover any decline in its fair value, whether it is more likely than not that the Company would be required to sell the security before its anticipated recovery in fair value, and a review of the Company's capital adequacy, interest rate risk position, and liquidity. The assessment of a security's ability to recover any decline in fair value, the ability of the issuer to meet contractual obligations, and management's intent and ability requires considerable judgment. A decline in value that is considered to be other-than-temporary is recorded as a loss within non-interest income in the Consolidated Statement of Income.

Investment securities fair values are based on observed market prices. Certain investment securities do not have observed bid prices and their fair value is based on instruments with similar risk elements. Since regulatory stock is redeemable at par, the Company carries it at cost.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff generally are stated at the principal amount outstanding, net of deferred fees and discounts, unamortized loan fees and costs, and the allowance for loan losses. Interest on loans is recognized as income when earned on the accrual method. The Company's general policy has been to stop accruing interest on loans when it is determined a reasonable doubt exists as to the collectability of additional interest. Income is subsequently recognized only to the extent that cash payments are received provided the loan is not delinquent in payment and, in management's judgment, the borrower has the ability and intent to make future principal payments. Otherwise, payments are applied to the unpaid principal balance of the loan. Loans are restored to accrual status if certain conditions are met, including but not limited to, the repayment of all unpaid interest and scheduled principal due, ongoing performance consistent with the contractual agreement, and the future expectation of continued, timely payments.

Loan origination and commitment fees as well as certain direct loan origination costs are being deferred and amortized as an adjustment to the related loan's yield over the contractual lives of the related loans.

Allowance for Loan Losses

The allowance for loan losses represents the amount which management estimates is adequate to provide for probable losses inherent in its loan portfolio, as of the Consolidated Balance Sheet date. The allowance method is used in providing for loan losses. Accordingly, all loan losses are charged to the allowance and all recoveries are credited to it. The allowance for loan losses is established through a provision for loan losses charged to operations. The provision for loan losses is based upon management’s quarterly review of the loan portfolio. The purpose of the review is to assess loan quality, identify impaired loans, analyze delinquencies, ascertain loan growth, evaluate potential charge-offs and recoveries, and assess general economic conditions in the markets served. An external independent loan review is also performed annually for the Bank. Management remains committed to an aggressive program of problem loan identification and resolution.

The allowance is calculated by applying loss factors to outstanding loans by type, excluding loans for which a specific allowance has been determined. Loss factors are based on management’s consideration of the nature of the portfolio segments, changes in mix and volume of the loan portfolio, historical loan loss experience, and general economic conditions. In addition, management considers industry standards and trends with respect to nonperforming loans and its knowledge and experience with specific lending segments.

Although management believes that it uses the best information available to make such determinations and that the allowance for loan losses is adequate at December 31, 2015, future adjustments could be necessary if circumstances or economic conditions

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differ substantially from the assumptions used in making the initial determinations. A downturn in the local economy, rising unemployment, or negative performance trends in financial information from borrowers could be indicators of subsequent increased levels of nonperforming assets and possible charge-offs, which would normally require increased loan loss provisions. An integral part of the periodic regulatory examination process is the review of the adequacy of the Banks' loan loss allowance. The regulatory agencies could require the Banks, based on their evaluation of information available at the time of their examination, to provide additional loan loss provisions to further supplement the allowance.

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

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

Loan Charge-off Policies

Loans are generally fully or partially charged down to the fair value of collateral securing the asset when:
- management judges the asset to be uncollectible;
- repayment is deemed to be protracted beyond reasonable time frames;
- the asset has been classified as a loss by either the internal loan review process or external examiners;
- the borrower has filed bankruptcy and the loss becomes evident due to a lack of assets; or
- the loan is 180 days past due unless both well secured and in the process of collection.

Troubled Debt Restructurings

In situations where, for economic or legal reasons related to a borrower’s financial difficulties, management may grant a concession for other than an insignificant period of time to the borrower that would not otherwise be considered, the related loan is classified as a troubled debt restructuring (TDR). Management strives to identify borrowers in financial difficulty early and work with them to modify to more affordable terms before their loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance, and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. In cases where borrowers are granted new terms that provide for a reduction of either interest or principal, management measures any impairment on the restructuring as noted above for impaired loans.

In addition to the allowance for the pooled portfolios, management has developed a separate allowance for loans that are identified as impaired through a TDR. These loans are excluded from pooled loss forecasts and a separate reserve is provided under the accounting guidance for loan impairment. Consumer loans whose terms have been modified in a TDR are also individually analyzed for estimated impairment.

Loans Held for Sale

In general, fixed rate residential mortgage loans originated by the Banks are held for sale and are carried at cost due to their short holding period, which can range from less than two weeks to a maximum of thirty days. Sold loans are not serviced by the Banks. Proceeds from the sale of loans in excess of the carrying value are accounted for as a gain. Total gains on the sale of loans are shown as a component of non-interest income within the Consolidated Statement of Income.

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Foreclosed Assets

Foreclosed assets are carried at the lower of cost or fair value less estimated selling costs. Prior to foreclosure, the value of the underlying loan is written down to the fair value of the real estate to be acquired by a charge to the allowance for loan losses, if necessary. Any subsequent write-downs are charged against operating expenses. Net operating expenses and gains and losses realized from disposition are included in non-interest expense and income, respectively, within the Consolidated Statement of Income.

Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed using straight-line and accelerated methods over the estimated useful lives of the related assets, which range from five to ten years for furniture, fixtures, and equipment and fifteen to forty years for buildings and improvements. Costs incurred for routine maintenance and repairs are charged to operations as incurred. Costs of major additions and improvements are capitalized.

Bank-Owned Life Insurance

The Company has purchased life insurance policies on certain officers and directors. Bank-owned life insurance is recorded at its cash surrender value, or the amount that can be realized. Increases in the cash surrender value are recognized as a component of non-interest income within the Consolidated Statement of Income.

Goodwill

The Company performs an annual impairment analysis of goodwill for its purchased subsidiaries, Luzerne and The M Group. Based on the fair value of these reporting units, estimated using the expected present value of future cash flows, no impairment of goodwill was recognized in 2015, 2014, or 2013.

Intangible Assets

At December 31, 2015, the Company had intangible assets of $1,240,000 as a result of the acquisition of Luzerne National Bank Corporation, which is net of accumulated amortization of $774,000. These intangible assets will continue to be amortized using the sum-of-the-years digits method of amortization over ten years.

Investments in Limited Partnerships

The Company is a limited partner in four partnerships at December 31, 2015 that provide low income elderly housing in the Company’s geographic market area. The carrying value of the Company’s investments in limited partnerships was $899,000 at December 31, 2015 and $1,560,000 at December 31, 2014. The investments are being amortized over the ten-year tax credit receipt period utilizing the straight-line method. The partnerships are amortized once the projects reach the level of occupancy needed to begin the ten year tax credit recognition period. Amortization of limited partnership investments amounted to $661,000 in 2015, 2014, and 2013.

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Company enters into off-balance sheet financial instruments. Those instruments consist of commitments to extend credit and standby letters of credit. When those instruments are funded or become payable, the Company reports the amounts in its financial statements.

Marketing Cost

Marketing costs are generally expensed as incurred.

Income Taxes

The Company prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Benefits from tax positions should be recognized in the financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority that would have full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of benefit that is greater than fifty percent likely of being realized

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upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be derecognized in the first subsequent financial reporting period in which that threshold is no longer met.

Deferred tax assets and liabilities result from temporary differences in financial and income tax methods of accounting, and are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. The Company analyzed its deferred tax asset position and determined that there was not a need for a valuation allowance due to the Company's ability to generate future ordinary and capital taxable income.

The Company when applicable recognizes interest and penalties on income taxes as a component of income tax provision.

Earnings Per Share

The Company provides dual presentation of basic and diluted earnings per share. Basic earnings per share is calculated utilizing net income as reported in the numerator and weighted average shares outstanding in the denominator. The computation of diluted earnings per share differs in that the dilutive effects of any stock options are adjusted in the denominator.

Employee Benefits

Pension and employee benefits include contributions, determined actuarially, to a defined benefit retirement plan covering the eligible employees of JSSB. The plan is funded on a current basis to the extent that it is deductible under existing federal tax regulations. Pension and other employee benefits also include contributions to a defined contribution Section 401(k) plan covering eligible employees. Contributions matching those made by eligible employees are funded throughout the year. In addition, an elective contribution may be made annually at the discretion of the board of directors for the employees of JSSB with contributions being made in 2015 and 2014.

The M Group Products and Income Recognition

The M Group product line is comprised primarily of annuities, life insurance, and mutual funds. The revenues generated from life insurance sales are commission only, as The M Group does not underwrite the policies. Life insurance sales include permanent and term policies with the majority of the policies written being permanent. Term life insurance policies are written for 10, 15, 20, and 30 year terms with the majority of the policies being written for 20 years. None of these products are offered as an integral part of lending activities.

Commissions from the sale of annuities are recognized at the time notice is received from the third party broker/dealer or an insurance company that the transaction has been accepted and approved, which is also the time when commission income is received.

Life insurance commissions are recognized at varying points based on the payment option chosen by the customer. Commissions from monthly and annual payment plans are recognized at the start of each annual period for the life insurance, while quarterly and semi-annual premium payments are recognized quarterly and semi-annually when the earnings process is complete. For example, semi-annual payments on the first of January and July would result in commission income recognition on the first of January and July, while payments on the first of January, April, July, and October would result in commission income recognition on those dates. The potential for chargebacks only exists for those policies on a monthly payment plan since income is recognized at the beginning of the annual coverage period versus at the time of each monthly payment. No liability is maintained for chargebacks as these are removed from income at the time of the occurrence.

Accumulated Other Comprehensive Income (Loss)

The Company is required to present accumulated other comprehensive income (loss) in a full set of general-purpose financial statements for all periods presented. Accumulated other comprehensive income (loss) is comprised of unrealized holding gains (losses) on the available for sale securities portfolio and the unrecognized components of net periodic benefit costs of the defined benefit pension plan.

Segment Reporting

The Company has determined that its only reportable segment is Community Banking.

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Reclassification of Comparative Amounts

Certain items previously reported have been reclassified to conform to the current year's reporting format. Such reclassifications did not affect net income or shareholders' equity.

Recent Accounting Pronouncements

In January 2014, FASB issued ASU 2014-01, Investments - Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects. The amendments in this update permit reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). The amendments in this update should be applied retrospectively to all periods presented. A reporting entity that uses the effective yield method to account for its investments in qualified affordable housing projects before the date of adoption may continue to apply the effective yield method for those preexisting investments. The amendments in this update are effective for public business entities for annual periods and interim reporting periods within those annual periods, beginning after December 15, 2014. Early adoption is permitted. This ASU did not have an impact on the Company's financial statements.

In January 2014, the FASB issued ASU 2014-04, Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure. The amendments in this update clarify that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additionally, the amendments require interim and annual disclosure of both (1) the amount of foreclosed residential real estate property held by the creditor, and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to local requirements of the applicable jurisdiction. The amendments in this update are effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. An entity can elect to adopt the amendments in this update using either a modified retrospective transition method or a prospective transition method. The Company has provided the necessary disclosures in Note 6. Loan Credit Quality and Related Allowance for Loan Losses.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (a new revenue recognition standard). The update's core principle is that a company will recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, this update specifies the accounting for certain costs to obtain or fulfill a contract with a customer and expands disclosure requirements for revenue recognition. This update is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. The Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In June 2014, the FASB issued ASU 2014-11, Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures. The amendments in this update change the accounting for repurchase-to-maturity transactions to secured borrowing accounting. For repurchase financing arrangements, the amendments require separate accounting for a transfer of a financial asset executed contemporaneously with a repurchase agreement with the same counterparty, which will result in secured borrowing accounting for the repurchase agreement. The amendments also require enhanced disclosures. The accounting changes in this update are effective for the first interim or annual period beginning after December 15, 2014. An entity is required to present changes in accounting for transactions outstanding on the effective date as a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption. Earlier application is prohibited. The disclosure for certain transactions accounted for as a sale is required to be presented for interim and annual periods beginning after December 15, 2014, and the disclosure for repurchase agreements, securities lending transactions, and repurchase-to-maturity transactions accounted for as secured borrowings is required to be presented for annual periods beginning after December 15, 2014, and for interim periods beginning after March 15, 2015. The disclosures are not required to be presented for comparative periods before the effective date. This update did not have an impact on the Company’s financial statements.

In June 2014, the FASB issued ASU 2014-12, Compensation-Stock Compensation (Topic 718): Accounting for Share-Based Payments when the Terms of an Award Provide that a Performance Target Could Be Achieved After the Requisite Service Period. The amendments require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. The amendments in this update are effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. Earlier adoption is permitted. Entities may apply the amendments in this update either (a) prospectively to all awards granted or modified after the effective date or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. If retrospective transition is adopted, the cumulative effect of applying this update as of the beginning of the earliest annual period presented in the financial statements should be recognized as an adjustment to the opening retained earnings balance at that date. Additionally, if retrospective transition is adopted, an entity may use hindsight in measuring and recognizing the compensation cost. This ASU did not have a significant impact on the Company’s financial statements.

In August 2014, the FASB issued ASU 2014-14, Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40). The amendments in this update require that a mortgage loan be de-recognized and that a separate other receivable be recognized upon foreclosure if the following conditions are met: (1) the loan has a government guarantee that is not separable from the loan before foreclosure, (2) at the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim, and (3) at the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. The amendments in this update are effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. This ASU did not have a significant impact on the Company’s financial statements.

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements - Going Concern (Subtopic 205-40). The amendments in this update provide guidance in accounting principles generally accepted in the United States of America about management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. The amendments in this update are effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. Early application is permitted. This ASU is not expected to have a significant impact on the Company’s financial statements.

In November 2014, the FASB issued ASU 2014-17, Business Combinations (Topic 805): Pushdown Accounting. The amendments in this update apply to the separate financial statements of an acquired entity and its subsidiaries that are a business or nonprofit activity (either public or nonpublic) upon the occurrence of an event in which an acquirer (an individual or an entity) obtains control of the acquired entity. An acquired entity may elect the option to apply pushdown accounting in the reporting period in which the change-in-control event occurs. If pushdown accounting is not applied in the reporting period in which the change-in-control event occurs, an acquired entity will have the option to elect to apply pushdown accounting in a subsequent reporting period to the acquired entity's most recent change-in-control event. The amendments in this update are effective on November 18, 2014. After the effective date, an acquired entity can make an election to apply the guidance to future change-in-control events or to its most recent change-in-control event. This update will not have an impact on the Company’s financial statements.

In January 2015, the FASB issued ASU 2015-01, Income Statement -Extraordinary and Unusual Items, as part of its initiative to reduce complexity in accounting standards. This update eliminates from GAAP the concept of extraordinary items. The amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. A reporting entity may apply the amendments prospectively. A reporting entity also may apply the amendments retrospectively to all prior periods presented in the financial statements. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. This update is not expected to have a significant impact on the Company’s financial statements.

In February 2015, the FASB issued ASU 2015-02, Consolidation (Topic 810). The amendments in this update affect reporting entities that are required to evaluate whether they should consolidate certain legal entities. All legal entities are subject to reevaluation under the revised consolidation model. Specifically, the amendments (1) Modify the evaluation of whether limited partnerships and similar legal entities are variable interest entities (VIEs) or voting interest entities; (2) Eliminate the presumption that a general partner should consolidate a limited partnership; (3) Affect the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships; (4) Provide a scope exception from consolidation guidance for reporting entities with interests in legal entities that are required to comply with or operate in accordance with requirements that are similar to those in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. The amendments in this update are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. The Company is currently evaluating the impact the adoption of the standard will have on the Company’s financial position or results of operations.

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In April 2015, the FASB issued ASU 2015-03, Interest-Imputation of Interest (Subtopic 835-30), as part of its initiative to reduce complexity in accounting standards. To simplify presentation of debt issuance costs, the amendments in this update require 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 recognition and measurement guidance for debt issuance costs are not affected by the amendments in this update. For public business entities, the amendments in this update are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. An entity should apply the new guidance on a retrospective basis, wherein the balance sheet of each individual period presented should be adjusted to reflect the period-specific effects of applying the new guidance. This update is not expected to have a significant impact on the Company’s financial statements.

In April 2015, the FASB issued ASU 2015-04, Compensation-Retirement Benefits (Topic 715), as part of its initiative to reduce complexity in accounting standards. For an entity with a fiscal year-end that does not coincide with a month-end, the amendments in this update provide a practical expedient that permits the entity to measure defined benefit plan assets and obligations using the month-end that is closest to the entity's fiscal year-end and apply that practical expedient consistently from year to year. The practical expedient should be applied consistently to all plans if an entity has more than one plan. The amendments in this update are effective for public business entities for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Earlier application is permitted. This update is not expected to have a significant impact on the Company’s financial statements.

In April 2015, the FASB issued ASU 2015-05, Intangible - Goodwill and Other Internal Use Software (Topic 350-40), as part of its initiative to reduce complexity in accounting standards. This guidance will help entities evaluate the accounting for fees paid by a customer in a cloud computing arrangement. The amendments in this update provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. For public business entities, the Board decided that the amendments will be effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2015. Early adoption is permitted for all entities. This update is not expected to have a significant impact on the Company’s financial statements.

In May 2015, the FASB issued ASU 2015-07, Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent). The update applies to reporting entities that elect to measure the fair value of an investment using the net asset value per share (or its equivalent) practical expedient. Under the amendments in this update, investments for which fair value is measured at net asset value per share (or its equivalent) using the practical expedient should not be categorized in the fair value hierarchy. Removing those investments from the fair value hierarchy not only eliminates the diversity in practice resulting from the way in which investments measured at net asset value per share (or its equivalent) with future redemption dates are classified, but also ensures that all investments categorized in the fair value hierarchy are classified using a consistent approach. Investments that calculate net asset value per share (or its equivalent), but for which the practical expedient is not applied will continue to be included in the fair value hierarchy. A reporting entity should continue to disclose information on investments for which fair value is measured at net asset value (or its equivalent) as a practical expedient to help users understand the nature and risks of the investments and whether the investments, if sold, are probable of being sold at amounts different from net asset value. The amendments in this update are effective for public business entities for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. For all other entities, the amendments in this update are effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. A reporting entity should apply the amendments retrospectively to all periods presented. The retrospective approach requires that an investment for which fair value is measured using the net asset value per share practical expedient be removed from the fair value hierarchy in all periods presented in an entity's financial statements. Earlier application is permitted. This update is not expected to have a significant impact on the Company’s financial statements.

In May 2015, the FASB issued ASU 2015-08, Business Combinations - Pushdown Accounting - Amendment to SEC Paragraphs Pursuant to Staff Accounting Bulletin No. 115. This ASU was issued to amend various SEC paragraphs pursuant to the issuance of Staff Accounting Bulletin No. 115. This update is not expected to have a significant impact on the Company’s financial statements.

In June 2015, the FASB issued ASU 2015-10, Technical Corrections and Improvements. The amendments in this update represent changes to clarify the Codification, correct unintended application of guidance, or make minor improvements to the Codification that are not expected to have a significant effect on current accounting practice or create a significant administrative cost to most entities. Transition guidance varies based on the amendments in this update. The amendments in this update that require transition guidance are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted, including adoption in an interim period. All other amendments will be effective upon the issuance of this update. This update is not expected to have a significant impact on the Company’s financial statements.

In August 2015, the FASB issued ASU 2015-14, Revenue from Contract with Customers (Topic 606). The amendments in this update defer the effective date of ASU 2014-09 for all entities by one year. Public business entities, certain not-for-profit entities, and certain employee benefit plans should apply the guidance in ASU 2014-09 to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. The Company is evaluating the effect of adopting this new accounting update.

In August 2015, the FASB issued ASU 2015-15, Interest-Imputation of Interest (Subtopic 835-30) Presentation and Subsequent
Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting. This ASU adds SEC paragraphs pursuant to the SEC Staff Announcement at the June 18, 2015 Emerging Issues Task Force meeting about the presentation and subsequent measurement of debt issuance costs associated with line-of-credit arrangements. This update is not expected to have a significant impact on the Company’s financial statements.

In September 2015, the FASB issued ASU 2015-16, Business Combinations (Topic 805). The amendments in this update require that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The amendments in this update require that the acquirer record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. The amendments in this update require an entity to present separately on the face of the income statement or disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. For public business entities, the amendments in this update are effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. This update is not expected to have a significant impact on the Company’s financial statements.

In November 2015, the FASB issued ASU 2015-17, Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes. The amendments in this Update require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The amendments in this Update apply to all entities that present a classified statement of financial position. For public business entities, the amendments in this Update are effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. For all other entities, the amendments in this Update are effective for financial statements issued for annual periods beginning after December 15, 2017, and interim periods within annual periods beginning after December 15, 2018. Earlier application is permitted for all entities as of the beginning of an interim or annual reporting period. The amendments in this Update may be applied either prospectively to all deferred tax liabilities and assets or retrospectively to all periods presented. This Update is not expected to have a significant impact on the Company’s financial statements.

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. Among other things, this Update (a) requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income; (b) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (c) eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities; (d) eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (e) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (f) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; (g) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements; and (h) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. 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. For all other entities including not-for-profit entities and employee benefit plans within the scope of Topics 960 through 965 on plan accounting, the amendments in this Update are effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. 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

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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.

NOTE 2 - ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The changes in accumulated other comprehensive income (loss) by component shown net of tax as of December 31, 2015 and 2014 were as follows:

	Twelve Months Ended December 31, 2015			Twelve Months Ended December 31, 2014		
(In Thousands)	Net Unrealized Gain (Loss) on Available for Sale Securities	Defined Benefit Plan	Total	Net Unrealized Gain (Loss) on Available for Sale Securities	Defined Benefit Plan	Total
Beginning balance	$2,930	$(4,597)	$(1,667)	$(2,169)	$(2,725)	$(4,894)
Other comprehensive (loss) income before reclassifications	(962)	435	(527)	7,419	(2,010)	5,409
Amounts reclassified from accumulated other comprehensive (loss) income	(1,710)	105	(1,605)	(2,320)	138	(2,182)
Net current-period other comprehensive income (loss)	(2,672)	540	(2,132)	5,099	(1,872)	3,227
Ending balance	$258	$(4,057)	$(3,799)	$2,930	$(4,597)	$(1,667)

The reclassifications out of accumulated other comprehensive income as of December 31, 2015 and 2014 were as follows:

(In Thousands)	Amount Reclassified from Accumulated Other Comprehensive Income		
	Twelve Months Ended		
Details about Accumulated Other Comprehensive Income Components	December 31, 2015	December 31, 2014	Affected Line Item in the Consolidated Statement of Income
Net realized gain on available for sale securities	$ (2,592)	$ (3,515)	Securities gains, net
Income tax effect	882	1,195	Income tax provision
	(1,710)	(2,320)	Net of tax
Net unrecognized pension costs	159	209	Salaries and employee benefits
Income tax effect	(54)	(71)	Income tax provision
	$ 105	$ 138	Net of tax

NOTE 3 - PER SHARE DATA

There are no convertible securities which would affect the denominator in calculating basic and dilutive earnings per share; therefore, net income as presented on the consolidated statement of income will be used as the numerator. The following table sets forth the composition of the weighted average common shares (denominator) used in the basic and dilutive per share computation.

	Year Ended December 31,		
	2015	2014	2013
Weighted average common shares issued	5,003,691	5,001,171	4,591,222
Average treasury stock shares	(231,452)	(185,022)	(180,596)

Weighted average common shares used to calculate basic and diluted earnings per share	4,772,239	4,816,149	4,410,626

There were 38,750 stock options issued during the third quarter of 2015 with 34,750 outstanding at December 31, 2015. The outstanding stock options did not impact diluted earnings per share as the strike price of the options was greater than the market price. There were no stock options outstanding during 2014 and 2013.

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NOTE 4 - INVESTMENT SECURITIES

The amortized cost and fair values of investment securities at December 31, 2015 and 2014 are as follows:

	2015			
(In Thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale (AFS)				
U.S. Government and agency securities	$3,586	$—	$(37)	$3,549
Mortgage-backed securities	9,785	284	(60)	10,009
Asset-backed securities	1,960	—	(20)	1,940
State and political securities	84,992	1,797	(234)	86,555
Other debt securities	59,832	185	(2,245)	57,772
Total debt securities	160,155	2,266	(2,596)	159,825
Financial institution equity securities	10,397	1,100	(14)	11,483
Other equity securities	5,214	70	(435)	4,849
Total equity securities	15,611	1,170	(449)	16,332
Total investment securities AFS	$175,766	$3,436	$(3,045)	$176,157

	2014			
(In Thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale (AFS)				
U.S. Government and agency securities	$3,953	$—	$(112)	$3,841
Mortgage-backed securities	12,240	485	(28)	12,697
Asset-backed securities	2,468	27	(3)	2,492
State and political securities	104,820	3,885	(589)	108,116
Other debt securities	89,736	1,026	(1,299)	89,463
Total debt securities	213,217	5,423	(2,031)	216,609
Financial institution equity securities	8,823	1,110	(18)	9,915
Other equity securities	5,733	84	(128)	5,689
Total equity securities	14,556	1,194	(146)	15,604
Total investment securities AFS	$227,773	$6,617	$(2,177)	$232,213

The amortized cost and fair values of trading investment securities at December 31, 2015 are as follows. There were no trading securities at December 31, 2014.

	2015			
(In Thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Trading				
Financial institution equity securities	$78	$—	$(5)	$73
Total trading securities	$78	$—	$(5)	$73

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The following tables show the Company’s gross unrealized losses and fair value, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position, at December 31, 2015 and 2014.

	2015					
	Less than Twelve Months		Twelve Months or Greater		Total	
(In Thousands)	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Available for Sale (AFS)						
U.S. Government and agency securities	$—	$—	$3,549	$(37)	$3,549	$(37)
Mortgage-backed securities	6,081	(60)	—	—	6,081	(60)
Asset-backed securities	1,626	(16)	314	(4)	1,940	(20)
State and political securities	7,345	(47)	1,656	(187)	9,001	(234)
Other debt securities	24,381	(530)	22,547	(1,715)	46,928	(2,245)
Total debt securities	39,433	(653)	28,066	(1,943)	67,499	(2,596)
Financial institution equity securities	—	—	53	(14)	53	(14)
Other equity securities	2,363	(277)	1,001	(158)	3,364	(435)
Total equity securities	2,363	(277)	1,054	(172)	3,417	(449)
Total Investment Securities AFS	$41,796	$(930)	$29,120	$(2,115)	$70,916	$(3,045)

	2014					
	Less than Twelve Months		Twelve Months or Greater		Total	
(In Thousands)	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Available for Sale (AFS)						
U.S. Government and agency securities	$—	$—	$3,841	$(112)	$3,841	$(112)
Mortgage-backed securities	6,741	(28)	—	—	6,741	(28)
Asset-backed securities	—	—	519	(3)	519	(3)
State and political securities	8,243	(14)	6,382	(575)	14,625	(589)
Other debt securities	23,174	(718)	29,266	(581)	52,440	(1,299)
Total debt securities	38,158	(760)	40,008	(1,271)	78,166	(2,031)
Financial institution equity securities	407	(18)	—	—	407	(18)
Other equity securities	1,837	(100)	773	(28)	2,610	(128)
Total equity securities	2,244	(118)	773	(28)	3,017	(146)
Total Investment Securities AFS	$40,402	$(878)	$40,781	$(1,299)	$81,183	$(2,177)

At December 31, 2015 there were 44 individual securities in a continuous unrealized loss position for less than twelve months and 21 individual securities in a continuous unrealized loss position for greater than twelve months.

The Company reviews its position quarterly and has asserted that at December 31, 2015 and 2014, the declines outlined in the above table represent temporary declines and the Company does not intend to sell and does not believe they will be required to sell these securities before recovery of their cost basis, which may be at maturity. The Company has concluded that any impairment of its investment securities portfolio is not other than temporary but is the result of interest rate changes that are not expected to result in the non-collection of principal and interest during the period.

The amortized cost and fair value of debt securities at December 31, 2015, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities since borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

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(In Thousands)	Amortized Cost	Fair Value
Due in one year or less	$1,835	$1,843
Due after one year to five years	32,085	31,926
Due after five years to ten years	88,554	87,311
Due after ten years	37,681	38,745
Total	$160,155	$159,825

Total gross proceeds from sales of securities available for sale were $65,672,000, $102,145,000, and $79,114,000 for 2015, 2014, and 2013, respectively. The following table represents gross realized gains and losses on those transactions:

	Year Ended December 31,		
(In Thousands)	2015	2014	2013
Gross realized gains:			
U.S. Government and agency securities	$—	$59	$—
Mortgage-backed securities	—	89	—
State and political securities	1,571	2,327	2,076
Other debt securities	825	622	490
Financial institution equity securities	183	710	241
Other equity securities	132	491	340
Total gross realized gains	$2,711	$4,298	$3,147
Gross realized losses:			
U.S. Government and agency securities	$—	$45	$—
Mortgage-backed securities	—	—	92
State and political securities	22	412	611
Other debt securities	54	209	27
Financial institution equity securities	—	—	—
Other equity securities	43	117	—
Total gross realized losses	$119	$783	$730

There were no impairment charges included in gross realized losses for the years ended December 31, 2015, 2014, and 2013.

Investment securities with a carrying value of approximately $131,089,000 and $128,501,000 at December 31, 2015 and 2014, respectively, were pledged to secure certain deposits, repurchase agreements, and for other purposes as required by law.

There is no concentration of investments that exceed ten percent of shareholders’ equity for any individual issuer, excluding those guaranteed by the U.S. Government.

NOTE 5 - FEDERAL HOME LOAN BANK STOCK

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

Management evaluated the stock and concluded that the stock was not impaired for the periods presented herein. Management considered that the FHLB maintains regulatory capital ratios in excess of all regulatory capital requirements, liquidity appears adequate, new shares of FHLB stock continue to change hands at the $100 par value, and the payment of dividends.

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NOTE 6 - LOAN CREDIT QUALITY AND RELATED ALLOWANCE FOR LOAN LOSSES

Management segments the Banks' loan portfolio to a level that enables risk and performance monitoring according to similar risk characteristics. Loans are segmented based on the underlying collateral characteristics. Categories include commercial, financial,
and agricultural, real estate, and installment loans to individuals. Real estate loans are further segmented into three categories: residential, commercial, and construction.

The following table presents the related aging categories of loans, by segment, as of December 31, 2015 and 2014:

	2015				
(In Thousands)	Current	Past Due 30 To 89 Days	Past Due 90 Days Or More & Still Accruing	Non-Accrual	Total
Commercial, financial, and agricultural	$162,312	$164	$—	$1,596	$164,072
Real estate mortgage:					
Residential	517,753	6,827	714	889	526,183
Commercial	295,784	720	265	5,770	302,539
Construction	26,545	67	—	212	26,824
Installment loans to individuals	26,572	429	—	—	27,001
	1,028,966	$8,207	$979	$8,467	1,046,619
Net deferred loan fees and discounts	(1,412)				(1,412)
Allowance for loan losses	(12,044)				(12,044)
Loans, net	$1,015,510				$1,033,163

	2014				
(In Thousands)	Current	Past Due 30 To 89 Days	Past Due 90 Days Or More & Still Accruing	Non-Accrual	Total
Commercial, financial, and agricultural	$122,624	$773	$—	$759	$124,156
Real estate mortgage:					
Residential	450,503	6,078	332	847	457,760
Commercial	279,731	1,819	54	9,744	291,348
Construction	21,485	—	—	511	21,996
Installment loans to individuals	21,125	383	1	—	21,509
	895,468	$9,053	$387	$11,861	916,769
Net deferred loan fees and discounts	(1,190)				(1,190)
Allowance for loan losses	(10,579)				(10,579)
Loans, net	$883,699				$905,000

Purchased loans acquired are recorded at fair value on their purchase date without a carryover of the related allowance for loan losses.

Upon acquisition, the Company evaluated whether each acquired loan (regardless of size) was within the scope of ASC 310-30. Purchased credit-impaired loans are loans that have evidence of credit deterioration since origination and it is probable at the date of acquisition that the Company will not collect all contractually required principal and interest payments. The fair value of purchased credit-impaired loans, on the acquisition date, was determined, primarily based on the fair value of loan collateral. The carrying value of purchased loans acquired with deteriorated credit quality was $341,000 at December 31, 2015.

On the acquisition date, the preliminary estimate of the unpaid principal balance for all loans evidencing credit impairment acquired in the Luzerne acquisition was $1,211,000 and the estimated fair value of the loans was $878,000. Total contractually required payments on these loans, including interest, at the acquisition date was $1,783,000. However, the Company’s preliminary estimate of expected cash flows was $941,000. At such date, the Company established a credit risk related non-accretable discount (a discount representing amounts which are not expected to be collected from the customer nor liquidation of collateral) of $842,000 relating to these impaired loans, reflected in the recorded net fair value. Such amount is reflected as a non-accretable fair value

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adjustment to loans. The Company further estimated the timing and amount of expected cash flows in excess of the estimated fair value and established an accretable discount of $63,000 on the acquisition date relating to these impaired loans.

The carrying value of the loans acquired and accounted for in accordance with ASC 310-30, was determined by projecting discounted contractual cash flows. The table below presents the components of the purchase accounting adjustments related to the purchased impaired loans acquired in the Luzerne acquisition as of June 1, 2013:

(In Thousands)	June 1, 2013
Unpaid principal balance	$1,211
Interest	572
Contractual cash flows	1,783
Non-accretable discount	(842)
Expected cash flows	941
Accretable discount	(63)
Estimated fair value	$878

The amortizable yield for purchased credit-impaired loans was fully amortized during 2014. Changes in the amortizable yield for purchased credit-impaired loans were as follows for the twelve months ended December 31, 2014

(In Thousands)	December 31, 2014
Balance at beginning of period	$35
Accretion	(35)
Balance at end of period	$—

The following table presents additional information regarding loans acquired with specific evidence of deterioration in credit quality under ASC 310-30:

(In Thousands)	December 31, 2015	December 31, 2014
Outstanding balance	$441	$449
Carrying amount	341	349

The following table presents the interest income if interest had been recorded based on the original loan agreement terms and rate of interest for non-accrual loans and interest income recognized on a cash basis for non-accrual loans as of December 31, 2015, 2014, and 2013:

	Year Ended December 31,					
	2015		2014		2013	
(In Thousands)	Interest Income That Would Have Been Recorded Based on Original Term and Rate	Interest Income Recorded on a Cash Basis	Interest Income That Would Have Been Recorded Based on Original Term and Rate	Interest Income Recorded on a Cash Basis	Interest Income That Would Have Been Recorded Based on Original Term and Rate	Interest Income Recorded on a Cash Basis
Commercial, financial, and agricultural	$48	$ 53	$42	$ 33	$7	$ 3
Real estate mortgage:						
Residential	53	38	63	34	41	20
Commercial	281	54	600	264	447	251

Construction	16	—	63	2	88	56
	$398	$ 145	$768	$ 333	$583	$ 330

Impaired Loans

Impaired loans are loans for which it is probable the Banks will not be able to collect all amounts due according to the contractual terms of the loan agreement. The Banks individually evaluate such loans for impairment and do not aggregate loans by major

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risk classifications. The definition of "impaired loans" is not the same as the definition of "non-accrual loans," although the two categories overlap. The Banks may choose to place a loan on non-accrual status due to payment delinquency or uncertain collectability, while not classifying the loan as impaired. Factors considered by management in determining impairment include payment status and collateral value. The amount of impairment for these types of loans is determined by the difference between the present value of the expected cash flows related to the loan, using the original interest rate, and its recorded value, or as a practical expedient in the case of collateralized loans, the difference between the fair value of the collateral and the recorded amount of the loan. When foreclosure is probable, impairment is measured based on the fair value of the collateral.

Management evaluates individual loans in all of the commercial segments for possible impairment if the loan is greater than $100,000 and if the loan is either on non-accrual status or has a risk rating of substandard or worse. Management may also elect to measure an individual loan for impairment if less than $100,000 on a case by case basis.

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

The following table presents the recorded investment, unpaid principal balance, and related allowance of impaired loans by segment as of December 31, 2015 and 2014:

	2015		
(In Thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:			
Commercial, financial, and agricultural	$319	$319	$—
Real estate mortgage:			
Residential	1,142	1,142	—
Commercial	1,735	1,785	—
Construction	212	212	—
	3,408	3,458	—
With an allowance recorded:			
Commercial, financial, and agricultural	150	150	75
Real estate mortgage:			
Residential	1,573	1,703	376
Commercial	10,752	10,752	1,653
Construction	—	—	—
	12,475	12,605	2,104
Total:			
Commercial, financial, and agricultural	469	469	75
Real estate mortgage:			
Residential	2,715	2,845	376
Commercial	12,487	12,537	1,653
Construction	212	212	—

	$15,883	$16,063	$2,104

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(In Thousands)	2014 Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:			
Commercial, financial, and agricultural	$439	$ 439	$—
Real estate mortgage:			
Residential	139	139	—
Commercial	3,228	3,228	—
Construction	716	716	—
	4,522	4,522	—
With an allowance recorded:			
Commercial, financial, and agricultural	673	673	298
Real estate mortgage:			
Residential	1,327	1,449	147
Commercial	10,745	10,889	1,581
Construction	309	309	67
	13,054	13,320	2,093
Total:			
Commercial, financial, and agricultural	1,112	1,112	298
Real estate mortgage:			
Residential	1,466	1,588	147
Commercial	13,973	14,117	1,581
Construction	1,025	1,025	67
	$17,576	$ 17,842	$2,093

The following table presents the average recorded investment in impaired loans and related interest income recognized for December 31, 2015, 2014, and 2013:

(In Thousands)	2015 Average Investment in Impaired Loans	Interest Income Recognized on an Accrual Basis on Impaired Loans	Interest Income Recognized on a Cash Basis on Impaired Loans
Commercial, financial, and agricultural	$1,031	$21	$10
Real estate mortgage:			
Residential	2,570	72	47
Commercial	17,529	342	80
Construction	865	1	53
	$21,995	$436	$190

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(In Thousands)	2014 Average Investment in Impaired Loans	Interest Income Recognized on an Accrual Basis on Impaired Loans	Interest Income Recognized on a Cash Basis on Impaired Loans
Commercial, financial, and agricultural	$763	$26	$25
Real estate mortgage:			
Residential	1,245	46	20
Commercial	10,987	130	101
Construction	1,086	17	89
	$14,081	$219	$235

(In Thousands)	2013 Average Investment in Impaired Loans	Interest Income Recognized on an Accrual Basis on Impaired Loans	Interest Income Recognized on a Cash Basis on Impaired Loans
Commercial, financial, and agricultural	$538	$26	$—
Real estate mortgage:			
Residential	1,581	62	25
Commercial	8,605	183	95
Construction	2,651	1	569
	$13,375	$272	$689

Additional funds totaling $20,000 are committed to be advanced in connection with impaired loans.

Modifications

The loan portfolio also includes certain loans that have been modified in a Troubled Debt Restructuring (TDR), where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance, or other actions. Certain TDRs are classified as nonperforming at the time of restructure and may only be returned to performing status after considering the borrower's sustained repayment performance for a reasonable period, generally six months.

Loan modifications that are considered TDRs completed during the twelve months ended December 31, 2015 and 2014 were as follows:

	Year Ended December 31,					
	2015			2014		
(In Thousands, Except Number of Contracts)	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial, financial, and agricultural	4	$ 213	$ 213	3	$ 620	$ 620
Real estate mortgage:						
Residential	11	962	962	3	392	392
Commercial	6	1,013	1,013	3	636	636
Construction	1	398	398	—	—	—

Total	22	$ 2,586	$ 2,586	9	$ 1,648	$ 1,648

Of the twenty-two new troubled debt restructurings granted for the year ended December 31, 2015, seven loans totaling $1,008,000 were granted payment concessions, four loans totaling $183,000 were granted term concessions, two loans totaling $287,000 were granted rate concessions, and nine loans totaling 1,108,000 were granted concessions due to other default.

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Of the nine new troubled debt restructurings granted for the year ended December 31, 2014, five loans totaling $1,142,000 were granted term concessions, three loans totaling $288,000 were granted payment concessions, and one loan totaling 218,000 was granted a rate concession.

Loan modifications considered troubled debt restructurings made during the twelve months previous to December 31, 2015, that have defaulted during the twelve month period ending December 31, 2015 were as follows:

	Year Ended December 31, 2015	
(In Thousands, Except Number of Contracts)	Number of Contracts	Recorded Investment
Commercial, financial, and agricultural	1	$106
Real estate mortgage:		
Residential	6	374
Commercial	1	242
Total	8	$722

There was one commercial real estate loan modifications considered a troubled debt restructurings made during the twelve months previous to December 31, 2014 that defaulted during the twelve month period ending December 31, 2014. However, that loan was paid off in the fourth quarter of 2014.

Internal Risk Ratings

Management uses a ten point internal risk rating system to monitor the credit quality of the overall loan portfolio. The first six categories are considered not criticized, and are aggregated as “Pass” rated. 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 are evaluated for Substandard classification. Loans in the Doubtful category exhibit the same weaknesses found in the Substandard loans, however, the weaknesses are more pronounced. Such loans are static and collection in full is improbable. However, these loans are not yet rated as loss because certain events may occur which would salvage the debt. Loans classified Loss are considered uncollectible and charge-off is imminent.

To help ensure that risk ratings are accurate and reflect the present and future capacity of borrowers to repay a loan as agreed, the Banks have a structured loan rating process with several layers of internal and external oversight. Generally, consumer and residential mortgage loans are included in the pass category unless a specific action, such as bankruptcy, repossession, or death occurs to raise awareness of a possible credit event. An external annual loan review of large commercial relationships is performed, as well as a sample of smaller transactions. During 2015, the threshold for the annual loan review was commercial relationships $1,100,000 or greater for JSSB and $1,450,000 or greater for Luzerne. Confirmation of the appropriate risk category is included in the review. Detailed reviews, including plans for resolution, are performed on loans classified as Substandard, Doubtful, or Loss on a quarterly basis.

The following table presents the credit quality categories identified above as of December 31, 2015 and 2014:

	2015					
	Commercial and	Real Estate Mortgages			Installment Loans	
(In Thousands)	Agricultural	Residential	Commercial	Construction	to Individuals	Totals

Pass	$160,734	$522,853	$277,248	$26,612	$ 27,001	$1,014,448
Special Mention	1,669	823	8,625	—	—	11,117
Substandard	1,669	2,507	16,666	212	—	21,054
Total	$164,072	$526,183	$302,539	$26,824	$ 27,001	$1,046,619

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	2014					
	Commercial and	Real Estate Mortgages			Installment Loans	
(In Thousands)	Agricultural	Residential	Commercial	Construction	to Individuals	Totals
Pass	$118,210	$454,885	$256,444	$20,927	$ 21,509	$871,975
Special Mention	3,186	2,384	16,262	445	—	22,277
Substandard	2,760	491	18,642	624	—	22,517
Total	$124,156	$457,760	$291,348	$21,996	$ 21,509	$916,769

Allowance for Loan Losses

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 future loss experience, and the amount of non-performing loans.

The Banks' methodology for determining the ALL is based on the requirements of ASC Section 310-10-35 for loans individually evaluated for impairment (previously discussed) and ASC Subtopic 450-20 for loans collectively evaluated for impairment, as well as the Interagency Policy Statements on the Allowance for Loan and Lease Losses and other bank regulatory guidance. The total of the two components represents the Banks' ALL.

Loans that are collectively evaluated for impairment are analyzed with general allowances being made as appropriate. Allowances are segmented based on collateral characteristics previously disclosed, and consistent with credit quality monitoring. Loans that are collectively evaluated for impairment are grouped into two classes for evaluation. A general allowance is determined for “Pass” rated credits, while a separate pool allowance is provided for “Criticized” rated credits that are not individually evaluated for impairment.

For the general allowances historical loss trends are used in the estimation of losses in the current portfolio. These historical loss amounts are modified by other qualitative factors. A historical charge-off factor is calculated utilizing a twelve quarter moving average. However, management may adjust the moving average time frame by up to four quarters to adjust for variances in the economic cycle. Management has identified a number of additional qualitative factors which it uses to supplement the historical charge-off factor because these factors are likely to cause estimated credit losses associated with the existing loan pools to differ from historical loss experience. The additional factors that are evaluated quarterly and updated using information obtained from internal, regulatory, and governmental sources are: national and local economic trends and conditions; levels of and trends in delinquency rates and non-accrual loans; trends in volumes and terms of loans; effects of changes in lending policies; experience, ability, and depth of lending staff; value of underlying collateral; and concentrations of credit from a loan type, industry, and/or geographic standpoint.

Loans in the criticized pools, which possess certain qualities or characteristics that may lead to collection and loss issues, are closely monitored by management and subject to additional qualitative factors. Management also monitors industry loss factors by loan segment for applicable adjustments to actual loss experience.

Management reviews the loan portfolio on a quarterly basis 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.

Activity in the allowance is presented for the twelve months ended December 31, 2015 and 2014:

2015

(In Thousands)	Commercial and Agricultural	Real Estate Mortgages Residential	Commercial	Construction	Installment Loans to Individual	Unallocated	Totals
Beginning Balance	$1,124	$3,755	$4,205	$786	$ 245	$464	$10,579
Charge-offs	(283)	(49)	(743)	(46)	(240)	—	(1,361)
Recoveries	176	81	182	23	64	—	526
Provision	515	1,329	573	(603)	174	312	2,300
Ending Balance	$1,532	$5,116	$4,217	$160	$ 243	$776	$12,044

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(In Thousands)	2014 Commercial and Agricultural	Real Estate Mortgages Residential	Commercial	Construction	Installment Loans to Individuals	Unallocated	Totals
Beginning Balance	$474	$3,917	$4,079	$741	$139	$794	$10,144
Charge-offs	(289)	(65)	(2,038)	—	(142)	—	(2,534)
Recoveries	18	15	—	22	64	—	119
Provision	921	(112)	2,164	23	184	(330)	2,850
Ending Balance	$1,124	$3,755	$4,205	$786	$245	$464	$10,579

The Company grants commercial, industrial, residential, and installment loans to customers throughout north-central and north-eastern Pennsylvania. Although the Company has a diversified loan portfolio at December 31, 2015 and 2014, a substantial portion of its debtors' ability to honor their contracts is dependent on the economic conditions within this region.

The Company has a concentration of loans at December 31, 2015 and 2014 as follows:

	2015	2014
Owners of residential rental properties	16.21 %	16.01 %
Owners of commercial rental properties	14.22 %	14.67 %

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31, 2015 and 2014:

(In Thousands)	2015 Commercial and Agricultural	Real Estate Mortgages Residential	Commercial	Construction	Installment Loans to Individuals	Unallocated	Totals
Allowance for Loan Losses:							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$75	$376	$ 1,653	$—	$—	$—	$2,104
Collectively evaluated for impairment	1,457	4,740	2,564	160	243	776	9,940
Total ending allowance balance	$1,532	$5,116	$ 4,217	$ 160	$ 243	$ 776	$12,044
Loans:							
Individually evaluated for impairment	$469	$2,374	$ 12,487	$ 212	$—		$15,542
Loans acquired with deteriorated credit quality	—	341	—	—	—		341
Collectively evaluated for impairment	163,603	523,468	290,052	26,612	27,001		1,030,736
Total ending loans balance	$164,072	$526,183	$ 302,539	$ 26,824	$ 27,001		$1,046,619

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	2014						
		Real Estate Mortgages			Installment Loans		
(In Thousands)	Commercial and Agricultural	Residential	Commercial	Construction	to Individuals	Unallocated	Totals
Allowance for Loan Losses:							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$298	$147	$ 1,581	$ 67	$ —	$ —	$2,093
Collectively evaluated for impairment	826	3,608	2,624	719	245	464	8,486
Total ending allowance balance	$1,124	3,755	$ 4,205	$ 786	$ 245	$ 464	$10,579
Loans:							
Individually evaluated for impairment	$1,112	$1,117	$ 13,973	$ 1,025	$ —		$17,227
Loans acquired with deteriorated credit quality	—	349	—	—	—		349
Collectively evaluated for impairment	123,044	456,294	277,375	20,971	21,509		899,193
Total ending loans balance	$124,156	457,760	$ 291,348	$ 21,996	$ 21,509		$916,769

NOTE 7 - PREMISES AND EQUIPMENT

Major classifications of premises and equipment are summarized as follows at December 31, 2015 and 2014:

(In Thousands)	2015	2014
Land	$5,764	$5,759
Premises	16,074	14,767
Furniture and equipment	8,231	7,435
Leasehold improvements	1,462	1,351
Total	31,531	29,312
Less accumulated depreciation and amortization	9,701	8,203
Net premises and equipment	$21,830	$21,109

Depreciation and amortization related to premises and equipment for the years ended 2015, 2014, and 2013 was $1,564,000, $1,494,000, and $1,054,000, respectively.

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NOTE 8 - GOODWILL AND OTHER INTANGIBLES

As of December 31, 2015 and 2014 goodwill had a gross carrying value of $17,380,000 and accumulated amortization of $276,000 resulting in a net carrying amount of $17,104,000.

The gross carrying amount of goodwill is tested for impairment in the third quarter of each fiscal year. Based on the fair value of the reporting unit, estimated using the expected present value of future cash flows, there was no evidence of impairment of the carrying amount at December 31, 2015 or 2014.

Identifiable intangibles are amortized to their estimated residual values over the expected useful lives. Such lives are also periodically reassessed to determine if any amortization period adjustments are required. Since the acquisition, no such adjustments were recorded. The identifiable intangible assets consist of a core deposit intangible and a trade name intangible which are being amortized on an accelerated basis, and also book of business intangible that is being amortized on a straightline basis over the useful life of such assets. The gross carrying amount of the core deposit intangible, the trade name intangible, and the book of business intangible at December 31, 2015 was $1,072,000, $76,000, and $92,000 respectively, with $521,000, $37,000, and $3,000 accumulated amortization as of that date.

As of December 31, 2015, the estimated future amortization expense for the core deposit and trade name intangible was:

(In Thousands)	Core Deposit Intangible	Trade Name Intangible	Book of Business Intangible
2016	254	18	10
2017	220	15	10
2018	185	13	10
2019	151	11	10
2020	117	8	10
2021	83	6	10
2022	48	4	10
2023	14	1	10
2024	—	—	10
2025	—	—	2
	$ 1,072	$ 76	$ 92

NOTE 9 - TIME DEPOSITS

Time deposits of $250,000 or more totaled approximately $28,953,000 on December 31, 2015 and $26,468,000 on December 31, 2014. Interest expense on time deposits of $100,000 or more was approximately $1,112,000, $875,000, and $841,000, for the years ended December 31, 2015, 2014, and 2013, respectively.

At December 31, 2015, the scheduled maturities on time deposits of $100,000 or more are as follows:

(In Thousands)	2015
Three months or less	$12,006
Three months to six months	5,863
Six months to twelve months	17,036
Over twelve months	71,687

Total	$106,592

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Total time deposit maturities are as follows at December 31, 2015:

(In Thousands)	2015
2016	$81,010
2017	55,318
2018	51,104
2019	24,796
2020	7,093
Thereafter	2,056
Total	$221,377

NOTE 10 - SHORT-TERM BORROWINGS

Short-term borrowings consist of securities sold under agreements to repurchase and primarily FHLB advances, which generally represent overnight or less than six month borrowings. In addition to the outstanding balances noted below, the Banks also have additional lines of credit totaling $35,413,000 available from correspondent banks other than the FHLB. The outstanding balances and related information for short-term borrowings are summarized as follows at December 31, 2015, 2014, and 2013:

(In Thousands)	2015		2014		2013	
Repurchase Agreements:						
Balance at year end	$18,334		$13,987		$12,391	
Maximum amount outstanding at any month end	18,614		18,801		16,632	
Average balance outstanding during the year	15,834		16,350		16,839	
Weighted-average interest rate:						
At year end	0.21	%	0.23	%	0.28	%
Paid during the year	0.21	%	0.22	%	0.40	%
Overnight:						
Balance at year end	$28,304		$26,831		$14,325	
Maximum amount outstanding at any month end	42,760		26,831		21,350	
Average balance outstanding during the year	23,075		5,992		5,508	
Weighted-average interest rate:						
At year end	0.43	%	0.27	%	0.25	%
Paid during the year	0.36	%	0.30	%	0.31	%

We utilize securities sold under agreements to repurchase to facilitate the needs of our customers and to facilitate secured short-term funding needs. Securities sold under agreements to repurchase are stated at the amount of cash received in connection with the transaction. We monitor collateral levels on a continuous basis. We may be required to provide additional collateral based on the fair value of the underlying securities. Securities pledged as collateral under repurchase agreements are maintained with our safekeeping agents.

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The remaining contractual maturity of repurchase agreements in the consolidated balance sheets as of December 31, 2015 and December 31, 2014 is presented in the following tables.

	2015	2014
	Remaining Contractual Maturity of the Agreements	
(In Thousands)	Overnight and Continuous	Overnight and Continuous
Repurchase Agreements:		
U.S. Government and agency securities	$3,586	$3,953
Mortgage-back securities	8,368	4,526
Asset-backed securities	1,960	2,468
State and political securities	8,015	7,070
Other debt securities	2,155	2,218
Total carrying value of collateral pledged	$24,084	$20,235
Total liability recognized for repurchase agreements	$18,334	$13,987

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NOTE 11 - LONG-TERM BORROWINGS

The following represents outstanding long-term borrowings with the FHLB by contractual maturities at December 31, 2015 and 2014:

(In Thousands)		Weighted Average Interest Rate		Stated Interest Rate Range			
Description	Maturity	2015	2014	From	To	2015	2014
Variable	2015	— %	3.97 %	3.97 %	3.97 %	$—	$10,000
Variable	2017	4.22 %	4.22 %	4.15 %	4.28 %	20,000	20,000
Variable	2018	3.18 %	3.18 %	3.18 %	3.18 %	10,000	10,000
Total Variable		3.87 %	3.90 %			30,000	40,000
Fixed	2015	— %	6.92 %	6.92 %	6.92 %	—	750
Fixed	2016	0.75 %	0.75 %	0.75 %	0.75 %	5,000	5,000
Fixed	2017	0.91 %	0.91 %	0.90 %	0.97 %	25,000	25,000
Fixed	2018	1.13 %	— %	1.13 %	1.13 %	2,000	—
Fixed	2019	1.55 %	— %	1.54 %	1.55 %	7,292	—
Fixed	2020	1.70 %	— %	1.62 %	1.79 %	18,333	—
Fixed	2022	2.04 %	— %	2.04 %	2.04 %	3,000	—
Total Fixed		1.28 %	1.03 %			60,625	30,750
Total		2.14 %	2.65 %			$90,625	$70,750

(In Thousands) Year Ending December 31,	Amount	Weighted Average Rate
2016	5,000	0.75 %
2017	45,000	2.38 %
2018	12,000	2.84 %
2019	7,292	1.55 %
Thereafter	21,333	1.75 %
	$90,625	2.14 %

The terms of the convertible borrowings allow the FHLB to convert the interest rate to an adjustable rate based on the three month London Interbank Offered Rate ("LIBOR") at a predetermined anniversary date of the borrowing's origination, ranging from three months to five years. If the FHLB converts the interest rate on one of the predetermined dates, the Bank has the ability to pay off the debt on the conversion date and quarterly thereafter without incurring the customary pre-payment penalty.

The Banks maintain a credit arrangement which includes a revolving line of credit with the FHLB. Under this credit arrangement, at December 31, 2015 JSSB has a remaining borrowing capacity of $236,434,000 and Luzerne has a remaining capacity of $145,476,000, which are subject to annual renewal and typically incur no service charges. Under terms of a blanket agreement, collateral for the FHLB borrowings must be secured by certain qualifying assets of each Bank which consist principally of first mortgage loans and mortgage-backed securities.

In December 2012, JSSB entered in to a capital lease on a piece of land in Lewisburg, Pennsylvania. The carrying amount of the land as of December 31, 2015 and 2014 was $827,000. The present value of minimum lease payments at December 31, 2015 and 2014 was $400,000 and $426,000. The following is a schedule showing the future minimum lease payments under the capital lease by years and the present value of the minimum lease payments as of

December 31, 2015. The interest rate related to the lease obligation is 2.75% and the maturity date is October 2023.

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(In Thousands)	Lease Payment	Interest	Present Value of Minimum Lease Payment
2016	$38	$11	$27
2017	38	10	28
2018	38	9	29
2019	38	9	29
2020	38	8	30
Thereafter	276	19	257
	$466	$66	$400

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NOTE 12 - INCOME TAXES

The following temporary differences gave rise to the net deferred tax asset position at December 31, 2015 and 2014:

(In Thousands)	2015	2014
Deferred tax assets:		
Allowance for loan losses	$3,976	$3,380
Deferred compensation	1,696	1,579
Defined Pension	1,525	2,172
Deferred Loan fees and discounts	272	256
Investment securities allowance	517	487
Low income housing credit carryforward	1,181	2,034
Capital loss carryforward	—	98
Other	1,696	1,578
Total	10,863	11,584
Deferred tax liabilities:		
Unrealized gain on available for sale securities	133	1,510
Investment security accretion	231	262
Depreciation	478	734
Amortization	1,031	977
Total	1,873	3,483
Deferred tax asset, net	$8,990	$8,101

The current low income housing credit carryforward will expire in 2031. The Company fully anticipates being able to use the carry-forward.

No valuation allowance was established at December 31, 2015 and 2014, because of the Company's ability to carry back capital losses to recover taxes paid in previous years and certain tax strategies, together with the anticipated future taxable income as evidenced by the Company's earning potential. The Corporation is no longer subject to federal, state, and local examinations by tax authorities for years before 2012.

The provision or benefit for income taxes is comprised of the following for the year ended December 31, 2015, 2014, and 2013:

(In Thousands)	2015	2014	2013
Currently payable	$3,527	$3,680	$3,328
Deferred benefit	209	124	123
Total provision	$3,736	$3,804	$3,451

A reconciliation between the expected income tax or benefit and the effective income tax rate on income before income tax provision or benefit follows for the year ended December 31, 2015, 2014, and 2013:

	2015		2014		2013	
(In Thousands)	Amount	%	Amount	%	Amount	%
Provision at expected rate	$5,996	34.00 %	$6,260	34.00 %	$5,962	34.00 %
(Decrease) increase in tax resulting from:						
Tax-exempt income	(1,492)	(8.46)	(1,673)	(9.09)	(1,933)	(11.02)
Tax credits	(737)	(4.17)	(737)	(4.00)	(737)	(4.20)
Other, net	(31)	(0.18)	(46)	(0.25)	159	0.90

Effective income tax provision and rate	$3,736	21.19	%	$3,804	20.66	%	$3,451	19.68	%

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NOTE 13 - EMPLOYEE BENEFIT PLANS

Defined Benefit Pension Plan

The Company has a noncontributory defined benefit pension plan (the "Plan") for all employees meeting certain age and length of service requirements that were hired prior to January 1, 2004, at which time entrance into the Plan was frozen. The benefit accrual for the Plan was subsequently frozen at December 31, 2014. Benefits are based primarily on years of service and the average annual compensation during the highest five consecutive years within the final ten years of employment - up until December 31, 2014 when the benefit accrual was frozen.

The following table sets forth the obligation and funded status as of December 31, 2015 and 2014:

(In Thousands)	2015	2014
Change in benefit obligation:		
Benefit obligation at beginning of year	$23,450	$18,186
Service cost	—	484
Interest cost	757	859
Actuarial gain	(144)	277
Benefits paid	(639)	(1,660)
Curtailment gain	(3,155)	—
Other, change in actuarial assumptions	(1,322)	5,304
Benefit obligation at end of year	$18,947	$23,450
Change in plan assets:		
Fair value of plan assets at beginning of year	$13,906	$14,258
Actual return on plan assets	25	487
Employer contribution	965	850
Benefits paid	(704)	(1,736)
Adjustment to fair value of plan assets	31	47
Fair value of plan assets at end of year	14,223	13,906
Funded status	$(4,724)	$(9,544)
Accounts recognized on balance sheet as:		
Total liabilities	$(4,724)	$(9,544)
Amounts not yet recognized as a component of net periodic pension cost:		
Amounts recognized in accumulated other comprehensive income (loss) consist of:		
Net loss	$6,267	$6,965

The accumulated benefit obligation for the Plan was $18,947,000 and $20,296,000 at December 31, 2015 and 2014, respectively.

Components of Net Periodic Cost and Other Amounts Recognized in Other Comprehensive Income (loss) as of December 31, 2015, 2014, and 2013 are as follows:

(In Thousands)	2015	2014	2013
Net periodic pension cost:			
Service cost	$64	$560	$638
Interest cost	757	859	770
Expected return on plan assets	(983)	(1,153)	(985)

Amortization of prior service cost	—	—	25
Amortization of unrecognized net loss	159	209	479
Net periodic benefit cost	$(3)	$475	$927

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Assumptions

Weighted-average assumptions used to determine benefit obligations at December 31, 2015, 2014, and 2013:

	2015		2014		2013	
Discount rate	4.17	%	3.83	%	4.75	%
Rate of compensation increase	N/A		3.00	%	3.00	%

Weighted-average assumptions used to determine net periodic cost for years ended December 31, 2015, 2014, and 2013:

	2015		2014		2013	
Discount rate	3.83	%	4.75	%	4.00	%
Expected long-term return on plan assets	7.00	%	8.00	%	8.00	%
Rate of compensation increase	N/A		3.00	%	3.00	%

The expected long-term rate of return was estimated using market benchmarks by which the plan assets would outperform the market value in the future, based on historical experience adjusted for changes in asset allocation and expectations for overall lower future returns on similar investments compared to past periods.

Plan Assets

The Plan's weighted-average asset allocations at December 31, 2015 and 2014 by asset category are as follows:

Asset Category	2015		2014	
Cash	8.56	%	11.54	%
Fixed income securities	10.33	%	12.46	%
Equity	61.73	%	76.00	%
Inflation Hedges/Real Assets	5.03	%	—	%
Hedged Strategies	14.35	%	—	%
Total	100.00	%	100.00	%

The investment objective for the Plan is to maximize total return with tolerance for slightly above average risk, meaning the fund is able to tolerate short-term volatility to achieve above-average returns over the long term.

Asset allocation favors equities, with target allocation of approximately 62% equity securities, 15.0% fixed income securities, 10% inflation hedges/real assets, 10% hedged strategies, and 2.5% cash. Due to volatility in the market, the target allocation is not always desirable and asset allocations will fluctuate between the acceptable ranges. The equity portfolio's exposure is primarily in mid and large capitalization domestic equities with limited exposure to small capitalization and international stocks.

It is management's intent to give the investment managers flexibility, within the overall guidelines, with respect to investment decisions and their timing. However, certain investments require specific review and approval by management. Management is also informed of anticipated, significant modifications of any previously approved investment, or anticipated use of derivatives to execute investment strategies.

The following table sets forth by level, within the fair value hierarchy detailed in Note 21 - Fair Value Measurements, the Plan's assets at fair value as of December 31, 2015 and 2014:

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(In Thousands)	2015 Level I	Level II	Level III	Total
Assets:				
Cash and cash equivalents	$1,218	$—	$—	$1,218
Mutual funds - taxable fixed income	1,467	—	—	1,467
Mutual funds - domestic equity	8,150	—	—	8,150
Mutual funds - international equity	631	—	—	631
Inflation Hedges/Real Assets	715	—	—	715
Hedged Strategies	2,042	—	—	2,042
Total assets at fair value	$14,223	$—	$—	$14,223

(In Thousands)	2014 Level I	Level II	Level III	Total
Assets:				
Cash and cash equivalents	$1,606	$—	$—	$1,606
Mutual funds - taxable fixed income	1,732	—	—	1,732
Mutual funds - domestic equity	8,372	—	—	8,372
Mutual funds - international equity	2,196	—	—	2,196
Total assets at fair value	$13,906	$—	$—	$13,906

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

(In Thousands)	
2016	$783
2017	799
2018	812
2019	848
2020	882
Thereafter	4,734
	$8,858

The company expects to contribute a minimum of $500,000 to its Pension Plan in 2016.

401(k) Savings Plan

The Company also offers a 401(k) savings plan in which eligible participating employees may elect to contribute up to a maximum percentage allowable not to exceed the limits of Code Sections 401(k), 404, and 415. The Company may make matching contributions equal to a discretionary percentage that is determined by the Board of Directors. Participants are at all times fully vested in their contributions and vest over a period of five years regarding the employer contribution. Contribution expense was approximately $230,000, $171,000, and $132,000 for the years ended December 31, 2015, 2014, and 2013, respectively.

Deferred Compensation Plan

The Company has a deferred compensation plan whereby participating directors elect to forego directors' fees paid in cash. Under this plan, the Company will make payments for a ten-year period beginning at the later of age 65 or ceasing to be a director in most cases or at death, if earlier, at which time payments would be made to their designated beneficiaries.

To fund benefits under the deferred compensation plan, the Company has acquired bank-owned life insurance policies on the lives of the participating directors for which insurance benefits are payable to the Company. The Company incurred expenses related to the plan of $252,000, $235,000, and $169,000 for the years ended December 31, 2015, 2014, and 2013, respectively. Benefits paid under the plan were approximately $103,000, $88,000, and $57,000 in 2015, 2014, and 2013, respectively.

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NOTE 14 - STOCK OPTIONS

In 2014, the Company adopted the 2014 Equity Incentive Plan designed to help the Company attract, retain, and motivate employees and non-employee directors. Incentive stock options, non-qualified stock options, and restricted stock may be granted as part of the plan.

On August 27, 2015, the Company issued 38,750 stock options to a group of employees. Each option granted has a strike price of $42.03 and is exercisable after five years following the date of the grant of such options. The options expire ten years following the date of the grant of such options.

A summary of stock option activity is presented below:

	2015	
	Shares	Weighted Average Exercise Price
Outstanding, beginning of year	—	—
Granted	38,750	$42.03
Exercised	—	—
Forfeited	(4,000)	42.03
Outstanding, end of year	34,750	$42.03

The estimated fair value of options, including the effect of estimated forfeitures, is recognized as expense on a straightline basis over the options' vesting periods while ensuring that the cumulative amount of compensation cost recognized at least equals the value of the vested portion of the award at that date. The Company determines the fair value of options granted using the Black-Scholes option-pricing model. The risk-free interest rate is based on the United States Treasury bond with a similar term to the expected life of the options at the grant date. Expected volatility was estimated based on the adjusted historic volatility of the Company's shares. The expected life was estimated to equal the contractual life of the options. The dividend yield rate was based upon recent historical dividends paid on shares.

The following assumptions were used in determining the fair value of share options granted:

	2015	
Risk-free interest rate	1.63	%
Expected volatility	31.58	%
Expected dividend yield	4.22	%
Expected life	7.51 years	
Weighted average grant date fair value per option	$3.96	

For the year ended December 31, 2015, recorded $19,000 in total share-based compensation expense. The compensation expense is recorded as part of the non-interest expenses in the Consolidated Statement of Income.

As at December 31, 2015, total unrecognized compensation costs related to non-vested options was $119,000 which is expected to be recognized over a period of 4.66 years.

NOTE 15 - EMPLOYEE STOCK PURCHASE PLAN

The Company maintains a Penns Woods Bancorp, Inc. Employee Stock Purchase Plan (“Plan”). The Plan is intended to encourage employee participation in the ownership and economic progress of the Company. The Plan allows for up to 1,000,000 shares to be purchased by employees. The purchase price of the shares is 95% of market value with an employee eligible to purchase up to the lesser of 15% of base compensation or $12,000 in market value annually. There were 2,335 and 2,720 shares issued under the plan for the years ended December 31, 2015 and 2014, respectively.

NOTE 16 - RELATED PARTY TRANSACTIONS

Certain directors and executive officers of the Company and the Bank, including their immediate families and companies in which they are principal owners (more than ten percent), are indebted to the Company. Such indebtedness was incurred in the ordinary course of business on the same terms and at those rates prevailing at the time for comparable transactions with others.

A summary of loan activity with executive officers, directors, principal shareholders, and associates of such persons is listed below for the years ended December 31, 2015 and 2014:

(In Thousands)	Beginning Balance	New Loans	Repayments	Ending Balance
2014	$10,955	$7,920	$(9,929)	$8,946
2015	$8,946	$8,693	$(8,381)	$9,258

Deposits from related parties held by the Banks amounted to $13,330,000 at December 31, 2015 and $10,703,000 at December 31, 2014.

NOTE 17 - COMMITMENTS AND CONTINGENT LIABILITIES

The following schedule shows future minimum rental payments under operating leases with noncancellable terms in excess of one year as of December 31, 2015:

(In Thousands)	
2016	$482
2017	429
2018	365
2019	248
2020	228
Thereafter	823
Total	$2,575

The Company’s operating lease obligations represent short and long-term lease and rental payments for facilities and equipment. Total rental expense for all operating leases for the years ended December 31, 2015, 2014, and 2013 were $591,000, $523,000 and $493,000.

The Company is subject to lawsuits and claims arising out of its business. There are no such legal proceedings or claims currently pending or threatened other than those encountered during the normal course of business.

NOTE 18 - OFF-BALANCE SHEET RISK

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit, interest rate, or liquidity risk in excess of the amount recognized in the Consolidated Balance Sheet. The contract amounts of these instruments express the extent of involvement the Company has in particular classes of financial instruments.

The Company's exposure to credit loss from nonperformance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual amount of these instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The Company may require collateral or other security to support financial instruments with off-balance sheet credit risk.

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Financial instruments whose contract amounts represent credit risk are as follows at December 31, 2015 and 2014:

(In Thousands)	2015	2014
Commitments to extend credit	$241,936	$235,940
Standby letters of credit	4,786	7,490

Commitments to extend credit are legally binding agreements to lend to customers. Commitments generally have fixed expiration dates or other termination clauses and may require payment of fees. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future liquidity requirements. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company, on an extension of credit is based on management's credit assessment of the counterparty.

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

NOTE 19 - CAPITAL REQUIREMENTS

Federal regulations require the Company and the Banks to maintain minimum amounts of capital. Specifically, each is required to maintain certain minimum dollar amounts and ratios of Common Equity Tier 1, Total, and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average total assets.

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

As of December 31, 2015 and 2014, the FDIC categorized the Banks as well capitalized under the regulatory framework for prompt corrective action. To be classified as a well capitalized financial institution, common equity tier I risk-based, tier I risked-based, total risk-based, and tier I leverage capital ratios must be at least 6.5%, 8%, 10%, and 5%, respectively.

The Company's and the Banks' actual capital ratios are presented in the following tables, which shows that the Company and both Banks met all regulatory capital requirements.

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Consolidated Company

(In Thousands)	2015 Amount	Ratio		2014 Amount	Ratio
Common Equity Tier I Capital (to Risk-weighted Assets)					
Actual	$121,665	11.24	%	N/A	N/A
For Capital Adequacy Purposes	48,722	4.50	%	N/A	N/A
To Be Well Capitalized	70,377	6.50	%	N/A	N/A
Total Capital (to Risk-weighted Assets)					
Actual	$134,067	12.38	%	$123,371	