FIRST NATIONAL COMMUNITY BANCORP INC
Form 10-K
March 11, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

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

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission File No. 000-53869

FIRST NATIONAL COMMUNITY BANCORP, INC.

(Exact Name of Registrant as Specified in Its Charter)

Pennsylvania	**23-2900790**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
102 E. Drinker St., Dunmore, PA	**18512**
(Address of Principal Executive Offices)	(Zip Code)

Registrant’s telephone number, including area code **(570) 346-7667**

Securities registered pursuant to Section 12(b) of the Act: **NONE**

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

Common Stock, $1.25 par value

(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes 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. Yes 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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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	Accelerated Filer
Non-Accelerated Filer (Do not check if a smaller reporting company)	Smaller reporting company

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

The aggregate market value of the voting and non-voting common stock of the registrant, held by non-affiliates was $86,331,852 at June 30, 2015.

APPLICABLE ONLY TO CORPORATE REGISTRANTS

State the number of shares outstanding of each of the registrant’s classes of common stock, as of the latest practicable date: 16,530,432 shares of common stock as of March 11, 2016.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information required by Items 10, 11, 12, 13 and 14 is incorporated by reference into Part III hereof from portions of the Proxy Statement for the registrant’s 2016 Annual Meeting of Shareholders.

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PART I

Item 1. Business

Overview

The Company

First National Community Bancorp, Inc., incorporated in 1997, is a Pennsylvania business corporation and a registered bank holding company headquartered in Dunmore, Pennsylvania. In this report the terms "Company," "we," "us," and "our" refer to First National Community Bancorp, Inc. and its subsidiaries, unless the context requires otherwise. In certain circumstances, however, First National Community Bancorp, Inc. uses the term "Company" to refer to itself.

The Company became an active bank holding company on July 1, 1998 when it acquired ownership of First National Community Bank (the "Bank"). The Bank is a wholly-owned subsidiary of the Company. The Company's primary activity consists of owning and operating the Bank, which provides practically all of the Company's earnings as a result of its banking services.

The Company had net income of $35.8 million, $13.4 million and $6.4 million in 2015, 2014 and 2013, respectively. Total assets were $1.1 billion at December 31, 2015 and $1.0 billion at both December 31, 2014 and 2013.

The Bank

Established as a national banking association in 1910, as of December 31, 2015 the Bank operated 19 full-service branch offices within three contiguous counties, Lackawanna, Luzerne and Wayne, its primary market area located in the Northeast section of the state.

Products and Services

Retail Banking

The Bank provides a wide variety of traditional banking products and services to individuals and businesses, including Debit Cards, Online Banking, Mobile Banking, Image Checking and E-Statements. Deposit products include various checking, savings and certificate of deposit products, as well as a line of preferred products for higher-balance customers. The Bank is a member of the Promontory Interfinancial Network and participates in their Certificate of Deposit Account Registry ("CDARs") and Insured Cash Sweep ("ICS") programs, which allow customers to secure Federal Deposit Insurance Corporation ("FDIC") insurance on balances in excess of the standard limitations.

The Bank also offers customers the convenience of 24-hour banking, seven days a week, through FNCB Online Banking ("FNCB Online") via a secure website, https://www.fncb.com. FNCB Online's product suite includes Bill Payment, Finance Works, Funds Transfer and POP Money (person to person transfers), and Purchase Rewards. FNCB Online can also be accessed through the Bank's mobile application. Customers can also access money from their deposit accounts by using their debit card to make purchases or cash withdrawals from any automated teller machines ("ATMs") including ATMs located in each of the Bank's branch offices as well as additional locations. FNCB's mobile deposit, available to personal banking customers with access to FNCB Online Banking and an eligible deposit account, allows customers to deposit checks, electronically from start to finish, from anywhere at any time.

Through FNCB Online, customers can directly access their accounts, open new accounts and apply for a mortgage or obtain a pre-qualification approval through the Bank's mortgage center. Telephone banking (Account Link), a service that provides customers with the ability to access account information and perform related account transfers through the use of a touch tone telephone, is also available. The Bank offers Bounce Protection, Savings Overdraft Protection and Instant Money loans which provide customers with an added level of protection against unanticipated overdrafts due to cash flow emergencies and account reconciliation errors. The Bank offers its customers an identity theft protection plan through a strategic partnership with an independent vendor. Subscribers select which coverage package they desire by visiting the Bank's secure website and choosing "Identity Protection" from the Resources menu.

FNCB Business Online Banking is a menu driven product that provides the Bank's business customers direct access to their account information and the ability to perform internal and external transfers, wire transfers and payments through ACH transactions, and process Direct Deposit payroll transactions for employees, 24 hours a day, 7 days a week, from their place of business. Remote Deposit Capture allows business customers the ability to process daily check deposits to their accounts through an online image capture environment. Business customers can access money from their deposit account by using their "business" debit card, providing a faster, more convenient way to make purchases, track business expenses and manage finances.

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Lending Activities

The Bank offers a variety of loans, including residential real estate loans, construction, land acquisition and development loans, commercial real estate loans, commercial and industrial loans, loans to state and political subdivisions, and consumer loans, generally to individuals and businesses in its primary market area. These lending activities are described in further detail below.

Residential Mortgage Loans

The Bank offers a variety of fixed-rate one- to four-family residential loans including First Time Homebuyer mortgages and Home Possible® mortgages to meet the home financing needs of customers with low downpayments. The Bank also offers a "WOW" mortgage, a first-lien, fixed-rate mortgage product with maturity terms of 7.5, 10 and 14.5 years. At December 31, 2015, one- to four-family residential mortgage loans totaled $130.7 million, or 17.9%, of the total loan portfolio. Except for the WOW mortgage, one- to four-family mortgage loans are originated generally for sale in the secondary market. However, management may portfolio one- to four-family residential mortgage loans as deemed necessary according to current asset/liability management strategies. During the year ended December 31, 2015, the Bank sold $7.9 million of one- to four-family mortgages. The Bank retains servicing rights on these mortgages.

Construction, Land Acquisition and Development Loans

The Bank offers interim construction financing secured by residential property for the purpose of constructing one- to four-family homes. The Bank also offers interim construction financing for the purpose of constructing residential developments and various commercial properties including shopping centers, office complexes and single purpose owner-occupied structures and for land acquisition. At December 31, 2015, construction, land acquisition and development loans amounted to $30.8 million and represented 4.2% of the total loan portfolio.

Commercial Real Estate Loans

At December 31, 2015, commercial real estate loans totaled $245.2 million, or 33.5%, of the total loan portfolio. Commercial real estate mortgage loans represent the largest portion of the Bank's total loan portfolio and loans in this portfolio generally have larger loan balances. The commercial real estate loan portfolio is secured by a broad range of real estate, including but not limited to, office complexes, shopping centers, hotels, warehouses, gas stations, convenience markets, residential care facilities, nursing care facilities, restaurants, multifamily housing, farms and land subdivisions.

Commercial and Industrial Loans

The Bank generally offers commercial loans to individuals and businesses located in its primary market area. The commercial loan portfolio includes, but is not limited to, lines of credit, dealer floor plan lines, equipment loans, vehicle loans and term loans. These loans are primarily secured by vehicles, machinery and equipment, inventory, accounts receivable, marketable securities, deposit accounts and real estate. At December 31, 2015, commercial and industrial loans totaled $149.8 million, or 20.5%, of the total loan portfolio.

Consumer Loans

Consumer loans include both secured and unsecured installment loans, lines of credit and overdraft protection loans. The Bank is also in the business of underwriting indirect auto loans which are originated through various auto dealers in northeastern Pennsylvania and dealer floor plan loans. Generally, the Bank also offers home equity loans and lines of credit with a maximum combined loan-to-value ratio of 90%, based on the appraised value of the property. Home equity loans have fixed rates of interest and are for terms up to 15 years. Home equity lines of credit have adjustable interest rates and are based off of the prime interest rate. At December 31, 2015, consumer loans totaled $128.6 million, or 17.6%, of the total loan portfolio.

State and Political Subdivision Loans

The Bank originates state and political subdivision loans, including general obligation and tax anticipation notes, primarily to municipalities in the Bank's market area. At December 31, 2015, state and political subdivision loans totaled $46.1 million, or 6.3%, of the total loan portfolio.

For more information regarding the loan portfolio and lending policies, please refer to Note 2 "Summary of Significant Accounting Policies" to the consolidated financial statements included in Item 8 of this Annual Report on Form 10-K.

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Wealth Management

The Company offers customers wealth management services through a third party provider. Customers are able to access alternative deposit products such as mutual funds, annuities, stocks, and bonds directly for purchase from an outside provider.

Deposit Activities

In general, deposits, borrowings and loan repayments are the major sources of the Bank's funds for lending and other investment purposes. The Bank grows its deposits within its market area primarily by offering a wide selection of deposit accounts. Deposit account terms vary according to the minimum balance required, the time periods the funds must remain on deposit and the interest rate, among other factors. In determining the terms of the Bank's deposit accounts, the Bank considers the interest rates offered by its competitors, the interest rates available on borrowings, its liquidity needs and customer preferences. The Bank regularly reviews its deposit mix and deposit pricing as part of its asset/liability management, taking into consideration rates offered by competitors in its market area.

Competition

The Company faces substantial competition in originating loans and in attracting deposits from a significant number of financial institutions operating in its market area, many with a statewide or regional presence, and in some cases, a national presence, as well as other financial institutions outside of its market area through online loan and deposit product offerings. The competition comes principally from other banks, savings institutions, credit unions, mortgage banking companies and, with respect to deposits, institutions offering investment alternatives, including money market funds and online savings accounts. The increased competition has resulted from changes in the legal and regulatory guidelines, as well as from economic conditions. The cost of regulatory compliance remains high for community banks as compared to their larger competitors that are able to achieve economies of scale.

As a result of consolidation in the banking industry, some of the Bank's competitors and their respective affiliates are larger and may enjoy advantages such as greater financial resources, a wider geographic presence, a wider array of services, or more favorable pricing alternatives and lower origination and operating costs. The Company considers its major competition to be local commercial banks as well as other commercial banks with branches in the Company's market area. Competitors may offer deposits at higher rates and loans with lower fixed rates, more attractive terms and less stringent credit structures than the Company has been able to offer. The growth and profitability of the Company depend on its continued ability to successfully compete.

Supervision and Regulation

The Company participates in a highly regulated industry and is subject to a variety of statutes, regulations and policies, as well as ongoing regulatory supervision and review. These laws, regulations and policies are subject to frequent change and the Company takes measures to comply with applicable requirements.

Supervisory Actions

The Bank was under a Consent Order (the "Order") from the Office of the Comptroller of the Currency ("OCC") dated September 1, 2010. On March 25, 2015, after meeting all of the requirements of the Order, the Bank was fully and completely released from the Order. The Company was also subject to a Written Agreement (the "Agreement") with the Federal Reserve Bank of Philadelphia (the "Reserve Bank") dated November 24, 2010. On September 8, 2015, the Company was notified by the Reserve Bank that, effective September 2, 2015, it had been fully and completely released from the Written Agreement.

The Company

The Company is a bank holding company registered with, and subject to regulation by, the Reserve Bank and the Board of Governors of the Federal Reserve System ("FRB"). The Bank Holding Company Act of 1956, as amended (the "BHCA"), and other federal laws subject bank holding companies to restrictions on the types of activities in which they may engage, and to a range of supervisory requirements and activities, including regulatory enforcement actions for violations of laws and regulations and unsafe and unsound banking practices.

The BHCA requires approval of the FRB for, among other things, the acquisition by a proposed bank holding company of control of more than five percent (5%) of the voting shares, or substantially all the assets, of any bank or the merger or consolidation by a bank holding company with another bank holding company. The BHCA also generally permits the acquisition by a bank holding company of control or substantially all the assets of any bank located in a state other than the home state of the bank holding company, except where the bank has not been in existence for the minimum period of time required by state law; but if the bank is at least 5 years old, the FRB may approve the acquisition.

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With certain limited exceptions, a bank holding company is prohibited from acquiring control of any voting shares of any company which is not a bank or bank holding company and from engaging directly or indirectly in any activity other than banking or managing or controlling banks or furnishing services to or performing services for its authorized subsidiaries. A bank holding company may, however, engage in, or acquire an interest in a company that engages in, activities that the FRB has determined by order or regulation to be so closely related to banking or managing or controlling banks as to be properly incident thereto. In making such a determination, the FRB is required to consider whether the performance of such activities can reasonably be expected to produce benefits to the public, such as convenience, increased competition or gains in efficiency, which outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest or unsound banking practices. The FRB is also empowered to differentiate between activities commenced *de novo* and activities commenced by the acquisition, in whole or in part, of a going concern. Some of the activities that the FRB has determined by regulation to be closely related to banking include making or servicing loans, performing certain data processing services, acting as a fiduciary or investment or financial advisor, and making investments in corporations or projects designed primarily to promote community welfare.

Subsidiary banks of a bank holding company are subject to certain restrictions imposed by the Federal Reserve Act on any extensions of credit to the bank holding company or any of its subsidiaries, or investments in the stock or other securities thereof, and on the taking of such stock or securities as collateral for loans to any borrower. Further, a holding company and any subsidiary bank are prohibited from engaging in certain tie-in arrangements in connection with the extension of credit. A subsidiary bank may not extend credit, lease or sell property, or furnish any services, or fix or vary the consideration for any of the foregoing on the condition that: (i) the customer obtain or provide some additional credit, property or services from or to such bank other than a loan, discount, deposit or trust service; (ii) the customer obtain or provide some additional credit, property or service from or to the bank holding company or any other subsidiary of the bank holding company; or (iii) the customer not obtain some other credit, property or service from competitors, except for reasonable requirements to assure the soundness of credit extended.

The Gramm Leach-Bliley Act of 1999 (the “GLB Act”) allows a bank holding company or other company to certify status as a financial holding company, which allows such company to engage in activities that are financial in nature, that are incidental to such activities, or are complementary to such activities without further approval. The Company is not a financial holding company. The GLB Act enumerates certain activities that are deemed financial in nature, such as underwriting insurance or acting as an insurance principal, agent or broker, underwriting, dealing in or making markets in securities, and engaging in merchant banking under certain restrictions. It also authorizes the FRB to determine by regulation what other activities are financial in nature, or incidental or complementary thereto.

The Bank

The Bank, as a national bank, is a member of the Federal Reserve System and its accounts are insured up to the maximum legal limit by the Deposit Insurance Fund of the FDIC. The Bank is subject to regulation, supervision and regular examination by the OCC. The regulations of these agencies and the FDIC govern most aspects of the Bank’s

business, including required reserves against deposits, loans, investments, mergers and acquisitions, borrowings, dividends and location and number of branch offices. State laws may also apply to the Bank to the extent that federal law does not preempt the state law. The laws and regulations governing the Bank generally have been promulgated to protect depositors and the Deposit Insurance Fund, and not for the purpose of protecting shareholders.

On February 26, 2016, the Bank filed an application with the Pennsylvania Department of Banking and Securities to convert from an OCC-chartered banking institution to a Pennsylvania state-chartered banking institution and has notified the OCC and the FDIC of the same. If and when the conversion application is approved, the primary banking regulators of the Bank would become the Pennsylvania Department of Banking and Securities and the FDIC. The Company would continue to be regulated by the Federal Reserve. There can be no assurance as to the ability and timing to obtain the requisite approvals of the foregoing conversion application.

Branching and Interstate Banking. The federal banking agencies are authorized to approve interstate bank merger transactions without regard to whether such transactions are prohibited by the law of any state, unless the home state of one of the banks has opted out of the interstate bank merger provisions of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the “Riegle-Neal Act”) by adopting a law after the date of enactment of the Riegle-Neal Act and before June 1, 1997 that applies equally to all out-of-state banks and expressly prohibits merger transactions involving out-of-state banks. Interstate bank mergers are also subject to the nationwide and statewide insured deposit concentration limitations described in the Riegle-Neal Act.

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”) permits national and state banks to establish *de novo* branches in other states to the same extent as a bank chartered by that state would be so permitted. Previously, banks could only establish branches in other states if the host state expressly permitted out-of-state banks to establish branches in that state. Pennsylvania law had previously permitted banks chartered in Pennsylvania to branch in other states without limitation, thereby permitting national banks in Pennsylvania to establish branches anywhere in the state, but only permitted out of state banks to branch in Pennsylvania if the home state of the out of state bank permits Pennsylvania banks to establish *de novo* branches. The branching provisions of the Dodd-Frank Act could result in more banks from other states establishing *de novo* branches in the Bank’s market area.

USA Patriot Act and BSA. Under the BSA, a financial institution is required to have systems in place to detect certain transactions, based on the size and nature of the transaction. Financial institutions are generally required to report cash transactions involving more than $10,000 to the United States Treasury. In addition, financial institutions are required to file suspicious activity reports for transactions that involve more than $5,000 and that the financial institution knows, suspects or has reason to suspect, involves illegal funds, is designed to evade the requirements of the BSA or has no lawful purpose. Under the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act, commonly referred to as the "USA Patriot Act" or the "Patriot Act," financial institutions are subject to prohibitions against specified financial transactions and account relationships, as well as enhanced due diligence standards intended to detect, and prevent, the use of the United States financial system for money laundering and terrorist financing activities. The Patriot Act requires financial institutions, including banks, to establish anti-money laundering programs, including employee training and independent audit requirements, meet minimum standards specified by the act, follow minimum standards for customer identification and maintenance of customer identification records, and regularly compare customer lists against lists of suspected terrorists, terrorist organizations and money launderers.

Capital Adequacy Requirements. The FRB and OCC have adopted risk based capital adequacy and leverage capital adequacy requirements pursuant to which they assess the adequacy of capital in examining and supervising banks and bank holding companies and in analyzing bank regulatory applications. Risk-based capital requirements determine the adequacy of capital based on the risk inherent in various classes of assets and off-balance sheet items.

In December 2010, the Basel Committee on Banking Supervision released its final framework for strengthening international capital and liquidity regulation ("Basel III"). The regulations adopted by the U.S. federal bank regulatory agencies, when fully phased-in, will require bank holding companies and their bank subsidiaries to maintain more capital, with a greater emphasis on common equity. The Basel III final capital framework, among other things, (i) introduces as a new capital measure "Common Equity Tier I" ("CET I"), (ii) specifies that Tier I capital consists of CET I and "Additional Tier I capital" instruments meeting specified requirements, (iii) defines CET I narrowly by requiring that most adjustments to regulatory capital measures be made to CET I and not to the other components of capital and (iv) expands the scope of the adjustments as compared to existing regulations.

When fully phased-in, Basel III requires banks to maintain (i) as a newly adopted international standard, a minimum ratio of CET I to risk-weighted assets of at least 4.50%, plus a "capital conservation buffer" of 2.50 %; (ii) a minimum ratio of Tier I capital to risk-weighted assets of at least 6.00%, plus the capital conservation buffer, or 8.50%; (iii) a minimum ratio of total (Tier I plus Tier 2) capital to risk-weighted assets of at least 8.00% plus the capital conservation buffer, or 10.50%; and (iv) as a newly adopted international standard, a minimum leverage ratio of 3.00%, calculated as the ratio of Tier I capital to balance sheet exposures plus certain off-balance sheet exposures (computed as the average for each quarter of the month-end ratios for the quarter).

Basel III also provides for a "countercyclical capital buffer," generally to be imposed when national regulators determine that excess aggregate credit growth becomes associated with a buildup of systemic risk that would be a

CET I add-on to the capital conservation buffer in the range of 0.00% to 2.50% when fully implemented. The capital conservation buffer is designed to absorb losses during periods of economic stress.

Banking institutions with a ratio of CET I to risk-weighted assets above the minimum but below the conservation buffer (or below the combined capital conservation buffer and countercyclical capital buffer, when the latter is applied) may face constraints on their ability to pay dividends, to effect equity repurchases and pay discretionary bonuses to executive officers, which constraints vary based on the amount of the shortfall.

The Basel III final framework provides for a number of new deductions from and adjustments to CET I. These include, for example, the requirement that mortgage servicing rights, deferred tax assets dependent upon future taxable income and significant investments in non-consolidated financial entities be deducted from CET I to the extent that any one such category exceeds 10.00% of CET I or all such categories in the aggregate exceed 15.00% of CET I.

The federal banking regulators issued a final rulemaking in July 2013 (the “Basel III Rule”) to implement Basel III under regulations substantially consistent with the above. The Basel III Rule also includes, as part of the definition of CET I capital, a requirement that banking institutions include the amount of Accumulated Other Comprehensive Income (“AOCI,” which primarily consists of unrealized gains and losses on available-for-sale securities, that are not required to be treated as OTTI, net of tax) in calculating regulatory capital, unless the institution makes a one-time opt-out election from this provision in connection with the filing of its first regulatory reports after applicability of the Basel III Rule to that institution. The Basel III Rule also imposes a 4.00% minimum Tier I leverage ratio.

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The Basel III Rule also makes changes to the manner of calculating risk-weighted assets. It imposes methodologies for determining risk weighted assets, including revisions to recognition of credit risk mitigation, such as a greater recognition of financial collateral and a wider range of eligible guarantors. They also include risk weighting of equity exposures and past due loans; and higher (greater than 100%) risk weighting for certain commercial real estate exposures that have higher credit risk profiles, including higher loan to value and equity components.

As discussed below, the Basel III Rule also integrates the new capital requirements into the prompt corrective action provisions under Section 38 of the FDIA.

In general, the Basel III Rule became applicable to the Company and Bank on January 1, 2015. The Company and Bank elected to exclude AOCI in calculating regulatory capital with the filing of their respective first regulatory reports after applicability of the Basel III Rule to them. Additionally, the Company's outstanding subordinated notes are subject to phase out and will cease to qualify as capital for regulatory purposes. Overall, the Company believes that implementation of the Basel III Rule did not have a material adverse effect on the Company's or Bank's capital ratios, earnings, shareholder's equity, or its ability to pay discretionary bonuses to executive officers.

Prompt Corrective Action. Under Section 38 of the FDIA, each federal banking agency is required to implement a system of prompt corrective action for institutions which it regulates. The federal banking agencies have promulgated substantially similar regulations to implement the system of prompt corrective action established by Section 38 of the FDIA.

The following are the capital requirements under the Basel III Rules integrated into the prompt corrective action category definitions. As of December 31, 2015, the following capital requirements were applicable to the Bank for purposes of Section 38 of the FDIA.

Capital Category	**Total Risk-Based Capital Ratio**	**Tier I Risk-Based Capital Ratio**	**Common Equity Tier I Capital Ratio**	**Leverage Ratio**	**Tangible Equity to Assets**
Well capitalized	>/= 10.0%	>/= 8.0%	>/= 6.5%	>/= 5.0%	N/A
Adequately capitalized	>/= 8.0%	>/= 6.0%	>/= 4.5%	>/= 4.0%	N/A
Undercapitalized	< 8.0%	< 6.0%	< 4.5%	< 4.0%	N/A
Significantly undercapitalized	< 6.0%	< 4.0%	< 3.0%	< 3.0%	N/A
Critically undercapitalized	N/A	N/A	N/A	N/A	Less than 2.0%

The Company's total capital to risk-weighted assets ratio at December 31, 2015 and 2014 were 11.79% and 13.67%, respectively. The same ratio for the Bank was 13.83% and 15.42% at December 31, 2015 and 2014, respectively. The Tier I capital to risk-weighted assets ratio for the Company at December 31, 2015 and 2014 was 9.42% and 8.76%, respectively. The Bank's Tier I Capital to risk-weighted assets ratio was 12.69% at December 31, 2015 and 14.16% at December 31, 2014. The Tier I capital to average assets ratio for the Company was 7.27% and 6.05%, at December 31, 2015 and 2014, respectively. This ratio for the Bank was 9.79% and 9.78% at December 31, 2015 and 2014, respectively. At December 31, 2015, the Company's and the Bank's common equity Tier I capital to risk-weighted assets ratios were 9.42% and 12.69%, respectively.

Regulatory Enforcement Authority. Federal banking law grants substantial enforcement powers to federal banking regulators. This enforcement authority includes, among other things, the ability to assess civil money penalties, to issue cease-and-desist or removal orders and to initiate injunctive actions against banking organizations and institution-affiliated parties. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with regulatory authorities.

The Bank and its "institution-affiliated parties," including its management, employees, agents, independent contractors, consultants such as attorneys and accountants and others who participate in the conduct of the financial institution's affairs, are subject to potential civil and criminal penalties for violations of law, regulations or written orders of a governmental agency. In addition, regulators are provided with greater flexibility to commence enforcement actions against institutions and institution-affiliated parties. Possible enforcement actions include the termination of deposit insurance and cease-and-desist orders. Such orders may, among other things, require affirmative action to correct any harm resulting from a violation or practice, including restitution, reimbursement, indemnifications or guarantees against loss. A financial institution may also be ordered to restrict its growth, dispose of certain assets, rescind agreements or contracts, or take other actions as determined by the ordering agency to be appropriate.

Under provisions of the federal securities laws, a determination by a court or regulatory agency that certain violations have occurred at a company or its affiliates can result in fines, restitution, a limitation of permitted activities, disqualification to continue to conduct certain activities and an inability to rely on certain favorable exemptions. Certain types of infractions and violations can also affect a public company in its timing and ability to expeditiously issue new securities into the capital markets.

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The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss allowances for regulatory purposes.

As a result of the previous volatility and instability in the financial system, Congress, the bank regulatory authorities and other government agencies have called for or proposed additional regulation and restrictions on the activities, practices and operations of banks and their holding companies. While many of these proposals relate to institutions that have accepted investments from, or sold troubled assets to, the Department of the Treasury or other government agencies, or otherwise participate in government programs intended to promote financial stabilization, Congress and the federal banking agencies have broad authority to require all banks and holding companies to adhere to more rigorous or costly operating procedures, corporate governance procedures, or to engage in activities or practices which they might not otherwise elect. Any such requirement could adversely affect the Company’s business and results of operations. The Company did not accept an investment by the Treasury Department in its preferred stock or warrants to purchase common stock, and except for the temporary increases in deposit insurance for customer accounts, has not participated in any of the programs adopted by the Treasury Department, FDIC or Federal Reserve.

The Dodd-Frank Act. The Dodd-Frank Act made significant changes to the bank regulatory structure and affects the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act has required a number of federal agencies to adopt a broad range of new rules and regulations, and to prepare various studies and reports for Congress. The federal agencies have been given significant discretion in drafting these rules and regulations. To date, the following provisions of the Dodd-Frank Act are considered to be of greatest significance to the Company:

expands the authority of the FRB to examine bank holding companies and their subsidiaries, including insured depository institutions;

requires a bank holding company to be well capitalized and well managed to receive approval of an interstate bank acquisition;

changes standards for federal preemption of state laws related to national banks and their subsidiaries;

provides mortgage reform provisions regarding a customer’s ability to pay and making more loans subject to provisions for higher-cost loans and new disclosures;

creates the Consumer Financial Protection Bureau (the “CFPB”) that has rulemaking authority for a wide range of consumer protection laws that apply to all banks and has broad powers to supervise and enforce consumer protection laws;

- creates the Financial Stability Oversight Council with authority to identify institutions and practices that might pose a systemic risk;

- introduces additional corporate governance and executive compensation requirements on companies subject to the Securities and Exchange Act of 1934, as amended;

- permits FDIC-insured banks to pay interest on business demand deposits;

- requires that holding companies and other companies that directly or indirectly control an insured depository institution serve as a source of financial strength;

- makes permanent the $250 thousand limit for federal deposit insurance at all insured depository institutions; and

- permits national and state banks to establish interstate branches to the same extent as the branch host state allows establishment of in-state branches.

Consumer Financial Protection Bureau. The Dodd-Frank Act created the CFPB, a new independent federal agency within the Federal Reserve System, having broad rulemaking, supervisory and enforcement powers under various federal consumer financial protection laws, including the Equal Credit Opportunity Act, Truth in Lending Act, Real Estate Settlement Procedures Act, Fair Credit Reporting Act, Fair Debt Collection Practices Act, the consumer financial privacy provisions of the Gramm-Leach-Bliley Act and certain other statutes. The CFPB, which began operations on July 21, 2011, has examination and primary enforcement authority with respect to depository institutions with $10 billion or more in assets. Smaller institutions, including the Bank, are subject to rules promulgated by the CFPB but continue to be examined and supervised by federal banking regulators for compliance with federal consumer protection laws and regulations. The CFPB also has authority to prevent unfair, deceptive or abusive practices in connection with the offering of consumer financial products. The Dodd-Frank Act permits states to adopt consumer protection laws and standards that are more stringent than those adopted at the federal level and, in certain circumstances, permits state attorneys general to enforce compliance with both the state and federal laws and regulations.

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A focus of the CFPB's rulemaking efforts has been on reforms related to residential mortgage transactions. In 2013, the CFPB issued final rules related to a borrower's ability to repay and qualified mortgage standards, mortgage servicing standards, loan originator compensation standards, requirements for high-cost mortgages, appraisal and escrow standards and requirements for higher-priced mortgages. Several of the CFPB's rulemakings became effective in January 2014. In November 2013, the CFPB issued final rules establishing integrated disclosure requirements for lenders and settlement agents in connection with most closed end, real estate secured consumer loans. These rules became effective in August 2015. During 2015, the CFPB issued additional rulemaking expanding the scope of information lenders must report in connection with mortgage and other housing-related loan applications under the Home Mortgage Disclosure Act.

The final rule implementing the Dodd-Frank Act requirement that lenders determine whether a consumer has the ability to repay a mortgage loan, which went into effect on January 10, 2014, establishes certain minimum requirements for creditors when making ability to pay determinations, and establishes certain protections from liability for mortgages meeting the definition of "qualified mortgages." The rule affords greater legal protections for lenders making qualified mortgages that are not "higher priced." Qualified mortgages must generally satisfy detailed requirements related to product features, underwriting standards, and a points and fees requirement whereby the total points and fees on a mortgage loan cannot exceed specified amounts or percentages of the total loan amount. Mandatory features of a qualified mortgage include: (1) a loan term not exceeding 30 years and (2) regular periodic payments that do not result in negative amortization, deferral of principal repayment, or a balloon payment. The rule creates special categories of qualified mortgages originated by certain smaller creditors. The Bank's current business strategy, product offerings, and profitability may change as the rule is interpreted by the regulators and courts.

The final rules adopting new mortgage servicing standards, which took effect on January 10, 2014, impose new requirements regarding force-placed insurance, mandate certain notices prior to rate adjustments on adjustable-rate mortgages, and establish requirements for periodic disclosures to borrowers. These requirements will affect notices to be given to consumers as to delinquency, foreclosure alternatives, modification applications, interest rate adjustments and options for avoiding "force-placed" insurance. Servicers will be prohibited from processing foreclosures when a loan modification is pending, and must wait until a loan is more than 120 days delinquent before initiating a foreclosure action. Servicers must provide direct and ongoing access to its personnel, and provide prompt review of any loss mitigation application. Servicers must maintain accurate and accessible mortgage records for the life of a loan and until one year after the loan is paid off or transferred.

FDIC Insurance Premiums. The FDIC maintains a risk-based assessment system for determining deposit insurance premiums. Four risk categories (I-IV), each subject to different premium rates, are established based upon an institution's status as well capitalized, adequately capitalized or undercapitalized, and the institution's supervisory rating.

The Dodd-Frank Act permanently increased the maximum deposit insurance amount for banks, savings institutions and credit unions to $250,000 per depositor. The Dodd-Frank Act also broadened the base for FDIC insurance

assessments. Assessments are now based on a financial institution's average consolidated total assets less tangible equity capital. The Dodd-Frank Act requires the FDIC to increase the reserve ratio of the Deposit Insurance Fund from 1.15% to 1.35% of insured deposits by 2020 and eliminates the requirement that the FDIC pay dividends to insured depository institutions when the reserve ratio exceeds certain thresholds. The Dodd-Frank Act eliminated the statutory prohibition against the payment of interest on business checking accounts.

An insured institution is required to pay deposit insurance premiums on its assessment base in accordance with its risk category. There are three adjustments that can be made to an institution's initial base assessment rate: (1) a potential decrease for long-term unsecured debt, including senior and subordinated debt and, for small institutions, a portion of Tier I capital; (2) a potential increase for secured liabilities above a threshold amount; and (3) for non-Risk Category I institutions, a potential increase for brokered deposits above a threshold amount. The FDIC may also impose special assessments from time to time.

Effective February 2, 2015 and for the remainder of the year ended December 31, 2015, the Bank was considered risk category I for deposit insurance assessments and paid an annual assessment rate ranging from 0.0005 basis points to 0.0006 basis points on the assessment base of average consolidated total assets less the average tangible equity during the assessment period.

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Dividend Restrictions

The Company is a legal entity separate and distinct from the Bank. The Company's revenues (on a parent company only basis) result almost entirely from dividends paid by its subsidiary, the Bank, to the Company. The right of the Company, and consequently the right of creditors and shareholders of the Company, to participate in any distribution of the assets or earnings of any subsidiary through the payment of such dividends or otherwise is necessarily subject to the prior claims of creditors of the subsidiary (including depositors) except to the extent that claims of the Company, in its capacity as a creditor, may be recognized. Additionally, the ability of the Bank to pay dividends to the Company is subject to various regulatory restrictions.

The declaration of cash dividends on the Company's common stock is at the discretion of its board of directors, and any decision to declare a dividend is based on a number of factors, including, but not limited to, earnings, prospects, financial condition, regulatory capital levels, applicable covenants under any credit agreements, notes and other contractual restrictions, Pennsylvania law, federal bank regulatory law, and other factors deemed relevant.

Employees

As of December 31, 2015, the Company and the Bank employed 269 persons, including 39 part-time employees.

Available Information

The Company files reports, proxy and information statements and other information electronically with the Securities and Exchange Commission ("SEC"). You may read and copy any materials that the Company files with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. Information may be obtained on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The SEC's website site address is http://www.sec.gov. The Company's website address is http://www.fncb.com. The Company makes its Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K and amendments thereto available through its website at www.fncb.com. They may also be obtained free of charge as soon as practicable after filing or furnishing them to the SEC upon request by sending an email to corporatesecretary@fncb.com. Information may also be obtained via written request to First National Community Bancorp, Inc. Attention: Chief Financial Officer, 102 East Drinker Street, Dunmore, PA 18512.

Item 1A. Risk Factors.

The risk factors discussed below, which could materially affect the Company's business, operating results or financial condition, should be considered in addition to the other information about the Company presented in this Annual Report on Form 10-K. However, the risk factors described below are not meant to be all inclusive. Additional risks and uncertainties not currently known or that the Company currently deems to be insignificant may also materially adversely affect the business, operating results or financial condition of the Company.

Risks Related to the Company and its Business

The Company may not be able to successfully compete with others for business.

The Company competes for loans, deposits and investment dollars with numerous regional and national banks and other community banking institutions, online divisions of banks located in other markets as well as other kinds of financial institutions and enterprises, such as securities firms, insurance companies, savings associations, credit unions, mortgage brokers, and private lenders. There is also competition for banking business from competitors outside of its market area. As noted above, the Company and the Bank are subject to extensive regulations and supervision, including, in many cases, regulations that limit the type and scope of activities. Many competitors have substantially greater resources than the Company, may offer certain services that the Bank does not provide, and operate under less stringent regulatory environments. The differences in available resources and applicable regulations may make it harder for the Company to compete profitably, reduce the rates that it can earn on loans and investments, increase the rates it must offer on deposits and other funds, and adversely affect its overall financial condition and earnings. For additional discussion of the Company's competitive environment, see the section entitled "Business – Competition" included in Item 1 to this Annual Report on Form 10-K.

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The economic environment continues to pose significant challenges for the Company and could adversely affect its financial condition and results of operations.

The Company is operating in a challenging economic environment, including uncertain national and local conditions. Additionally, concerns from some of the countries in the European Union, Asia and elsewhere have also strained the financial markets both abroad and domestically. Financial institutions continue to be affected by softness in the real estate market and constrained financial markets. While conditions appear to have improved since the depths of the financial crisis, generally and in the Company's market area, should declines in real estate values, home sales volumes, and financial stress on borrowers as a result of the uncertain economic environment re-emerge, such events could have an adverse effect on our borrowers or their customers, which could adversely affect our financial condition and results of operations. A worsening of these conditions would likely exacerbate the adverse effects on us and others in the financial institutions industry. Deterioration in economic conditions in our markets could drive loan losses beyond that which is provided for in the Company's ALLL, which would necessitate further increases in the provision for loan and lease losses, and, in turn, reduce the Company's earnings and capital. The Company may also face the following risks in connection with the economic environment:

economic conditions that negatively affect housing prices and the job market have resulted in the past, and may continue to result, in a deterioration in credit quality of our loan portfolios, and such deterioration in credit quality has had, and could continue to have, a negative impact on our business;

market developments may affect consumer confidence levels and may reduce loan demand and cause adverse changes in payment patterns, leading to a reduced asset base, as well as increases in delinquencies and default rates on loans and other credit facilities;

the methodologies the Company uses to establish the ALLL rely on complex judgments, including forecasts of economic conditions, that are inherently uncertain and may be inadequate;

the continuation of low market interest rates, may further pressure our interest margins as interest-earning assets, such as loans and investments, are reinvested or reprice at lower rates;

volatility in the market, and lower level of confidence in the banking system, could require the Bank to pay higher interest rates to obtain deposits to meet the needs of its depositors and borrowers, resulting in reduced margin and net interest income. If conditions worsen, it is possible that banks such as the Bank may be unable to meet the needs of their depositors and borrowers, which could, in the worst case, result in the Bank being placed into receivership; and

compliance with increased regulation of the banking industry may increase our costs, limit our ability to pursue business opportunities, and divert management efforts.

If these conditions or similar ones continue to exist or worsen, the Company could experience adverse effects on its financial condition.

The Company is subject to lending risk.

As of December 31, 2015, approximately 37.8% of the Company's loan portfolio consisted of commercial real estate loans and construction, land acquisition and development loans. These types of loans are generally viewed as having more risk of default than residential real estate loans or consumer loans. These types of loans are also typically larger than residential real estate loans and consumer loans. Because the Company's loan portfolio contains a significant number of commercial real estate loans with relatively large balances, the deterioration of one or a few of these loans could cause a significant increase in non-performing loans. All non-performing loans totaled $3.8 million, or 0.5% of total gross loans, as of December 31, 2015, and $5.5 million, or 0.8% of total gross loans, as of December 31, 2014. Although non-performing asset levels decreased from the prior year, an increase in non-performing loans could result in an increase in the provision for loan and lease losses and an increase in loan charge-offs, both of which could have a material adverse effect on the Company's financial condition and results of operations. The lending activities in which the Bank engages carry the risk that the borrowers will be unable to perform on their obligations. As such, general economic conditions, nationally and in the Company's primary market area, will have a significant impact on its results of operations. To the extent that economic conditions deteriorate, business and individual borrowers may be less able to meet their obligations to the Bank in full, in a timely manner, resulting in decreased earnings or losses to the Bank. To the extent that loans are secured by real estate, adverse conditions in the real estate market may reduce the ability of the borrower to generate the necessary cash flow for repayment of the loan, and reduce the ability to collect the full amount of the loan upon a default. To the extent that the Bank makes fixed-rate loans, general increases in interest rates will tend to reduce its spread as the interest rates the Company must pay for deposits would increase while interest income is flat. Economic conditions and interest rates may also adversely affect the value of property pledged as security for loans.

The Company's concentrations of loans, including those to insiders and related parties, may create a greater risk of loan defaults and losses.

A substantial portion of the Company's loans are secured by real estate in the Northeastern Pennsylvania market, and substantially all of its loans are to borrowers in that area. The Company also has a significant amount of commercial real estate, commercial and industrial, construction, land acquisition and development loans and land-related loans for residential and commercial developments. At December 31, 2015, $433.7 million, or 59.3%, of gross loans were secured by real estate, primarily commercial real estate. Management has taken steps to mitigate the Company's commercial real estate concentration risk by diversification among the types and characteristics of real estate collateral properties, sound underwriting practices, and ongoing portfolio monitoring and market analysis. Of total gross loans, $30.8 million, or 4.2%, were construction, land acquisition and development loans. Construction, land acquisition and development loans have the highest risk of uncollectability. An additional $149.8 million, or 20.5%, of portfolio loans were commercial and industrial loans not secured by real estate. Historically, commercial and industrial loans generally have had a higher risk of default than other categories of loans, such as single family residential mortgage loans. The repayments of these loans often depend on the successful operation of a business and are more likely to be adversely affected by adverse economic conditions. While the Company believes that its loan portfolio is well diversified in terms of borrowers and industries, these concentrations expose the Company to the risk that adverse developments in the real estate market, or in the general economic conditions in the Company's general market area, could increase the levels of non-performing loans and charge-offs, and reduce loan demand. In that event, the Company would likely experience lower earnings or losses. Additionally, if, for any reason, economic conditions in its market area deteriorate, or there is significant volatility or weakness in the economy or any significant sector of the area's economy, the Company's ability to develop business relationships may be diminished, the quality and collectability of its loans may be adversely affected, the value of collateral may decline and loan demand may be reduced.

Commercial real estate, commercial and industrial and construction, land acquisition and development loans tend to have larger balances than single family mortgage loans and other consumer loans. Because the loan portfolio contains a significant number of commercial and industrial loans, commercial real estate loans and construction, land acquisition and development loans with relatively large balances, the deterioration of one or a few of these loans may cause a significant increase in non-performing assets. An increase in non-performing loans could result in a loss of earnings from these loans, an increase in the provision for loan and lease losses, or an increase in loan charge-offs, which could have an adverse impact on the Company's results of operations and financial condition.

Guidance adopted by federal banking regulators provides that banks having concentrations in construction, land development or commercial real estate loans are expected to have and maintain higher levels of risk management and, potentially, higher levels of capital, which may adversely affect shareholder returns, or require the Company to obtain additional capital sooner than the Company otherwise would. Excluded from the scope of this guidance are loans secured by non-farm nonresidential properties where the primary source of repayment is the cash flow from the ongoing operations and activities conducted by the party, or affiliate of the party, who owns the property.

Outstanding loans and line of credit balances to directors, officers and their related parties totaled $52.7 million as of December 31, 2015. At December 31, 2015, there were no loans to directors, officers and their related parties that were categorized as criticized loans within the Bank's risk rating system, meaning they are not considered to present a higher risk of collection than other loans. For more information regarding loans to officers and directors and/or their related parties, please refer to Note 14 — "Related Party Transactions" to the consolidated financial statements included in Item 8 and Item 13, "Certain Relationships and Related Transactions, and Director Independence" to this Annual Report on Form 10-K.

The Company's financial condition and results of operations would be adversely affected if the ALLL is not sufficient to absorb actual losses or if increases to ALLL were required.

The lending activities in which the Bank engages carry the risk that the borrowers will be unable to perform on their obligations, and that the collateral securing the payment of their obligations may be insufficient to assure repayment. The Company may experience significant credit losses, which could have a material adverse effect on its operating results. The Company makes various assumptions and judgments about the collectability of its loan portfolio, including the creditworthiness of its borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of its loans, which it uses as a basis to estimate and establish its reserves for losses. In determining the amount of the ALLL, the Company reviews its loans, its loss and delinquency experience, and evaluates current economic conditions. If these assumptions prove to be incorrect, the ALLL may not cover inherent losses in its loan portfolio at the date of its financial statements. Material additions to the Company's allowance or extensive charge-offs would materially decrease its net income. At December 31, 2015, the ALLL totaled $8.8 million, representing 1.2% of total loans.

Although the Company believes it has underwriting standards to manage normal lending risks, it is difficult to assess the future performance of its loan portfolio due to the ongoing economic environment and the state of the real estate market. The assessment of future performance of the loan portfolio is inherently uncertain. The Company can give no assurance that non-performing loans will not increase or that non-performing or delinquent loans will not adversely affect the Company's future performance.

In addition, federal regulators periodically review the Company's ALLL and may require increases to the ALLL or further loan charge-offs. Any increase in ALLL or loan charge-offs as required by these regulatory agencies could have a material adverse effect on the Company's results of operations and financial condition.

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If the Company concludes that the decline in value of any of its investment securities is other-than-temporary, the Company is required to write-down the security, to reflect credit-related impairments through a charge to earnings.

The Company reviews its investment securities portfolio at each quarter-end reporting period to determine whether the fair value is below the current carrying value. When the fair value of any of the Company's debt investment securities has declined below its carrying value, the Company is required to assess whether the decline is an OTTI. If the Company concludes that the decline is other-than-temporary, it is required to write down the value of that security to reflect the credit-related impairments through a charge to earnings. Changes in the expected cash flows of securities in its portfolio and/or prolonged price declines in future periods may result in impairment of the Company's investment securities that is other-than-temporary, which would require a charge to earnings. Due to the complexity of the calculations and assumptions used in determining whether an asset is impaired, any impairment disclosed may not accurately reflect the actual impairment in the future. In addition, to the extent that the value of any of the Company's investment securities is sensitive to fluctuations in interest rates, any increase in interest rates may result in a decline in the value of such investment securities.

The Company held approximately $6.3 million in capital stock of the Federal Home Loan Bank of Pittsburgh ("FHLB") as of December 31, 2015. The Company must own such capital stock to qualify for membership in the Federal Home Loan Bank system which enables it to borrow funds under the FHLB advance program. If FHLB were to cease operations, the Company's business, financial condition, liquidity, capital and results of operations may be materially and adversely affected.

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

The Company's earnings and cash flows are largely dependent upon its net interest income. Net interest income is the difference between interest income earned on interest-earning assets such as loans and securities and interest expense paid on interest-bearing liabilities such as deposits and borrowed funds. Interest rates are highly sensitive to many factors that are beyond the Company's control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the FRB. Changes in monetary policy, including changes in interest rates, could influence not only the interest the Company receives on loans and securities and the amount of interest it pays on deposits and borrowings, but such changes could also affect (i) the Company's ability to originate loans and obtain deposits, (ii) the fair value of the Company's financial assets and liabilities, and (iii) the average duration of the Company's mortgage-backed securities portfolio.

If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and investments, the Company's net interest income, and therefore earnings, could be adversely affected. Earnings could also be adversely affected if the interest rates received on loans and investments fall more quickly than the interest rates paid on deposits and other borrowings. Any substantial, unexpected, prolonged change in market

interest rates could have a material adverse effect on the Company’s financial condition and results of operations.

The Company may need to raise additional capital in the future, but that capital may not be available when it is needed and on terms favorable to current shareholders.

Laws, regulations and banking regulators require the Company and Bank to maintain adequate levels of capital to support its operations. In addition, capital levels are determined by the Company’s management and Board of Directors based on capital levels that they believe are necessary to support the Company’s business operations. The Company regularly evaluates its present and future capital requirements and needs and analyzes capital raising alternatives and options. Although the Company succeeded in meeting its current regulatory capital requirements, it may need to raise additional capital in the future to support possible loan losses or potential OTTI during future periods, to meet future regulatory capital requirements or for other reasons.

The Board of Directors may determine from time to time that the Company needs to raise additional capital by issuing additional common shares or other securities. The Company is not restricted from issuing additional common shares, including securities that are convertible into or exchangeable for, or that represent the right to receive, common shares. Because the Company’s decision to issue securities in any future offering will depend on market conditions and other factors beyond its control, the Company cannot predict or estimate the amount, timing or nature of any future offerings, or the prices at which such offerings may be affected. Such offerings will likely be dilutive to common shareholders from ownership, earnings and book value perspectives. New investors also may have rights, preferences and privileges that are senior to, and that adversely affect, its then current common shareholders. Additionally, if the Company raises additional capital by making additional offerings of debt or preferred equity securities, upon liquidation, holders of the Company’s debt securities and shares of preferred shares, and lenders with respect to other borrowings, will receive distributions of the Company’s available assets prior to the holders of the Company’s common shares. Additional equity offerings may dilute the holdings of existing shareholders or reduce the market price of the Company’s common shares, or both. Holders of the Company’s common shares are not entitled to preemptive rights or other protections against dilution.

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The Company cannot assure that additional capital will be available on acceptable terms or at all. Any occurrence that may limit the Company's access to the capital markets may adversely affect the Company's capital costs and its ability to raise capital and, in turn, its liquidity. Moreover, if the Company needs to raise capital, it may have to do so when many other financial institutions are also seeking to raise capital and would have to compete with those institutions for investors. An inability to raise additional capital on acceptable terms when needed could have a material adverse effect on the Company's business, financial condition and results of operations.

Interruptions or security breaches of the Company's information systems could negatively affect its financial performance or reputation.

In conducting its business, the Company relies heavily on its information systems. The Company collects and stores sensitive data, including proprietary business information and personally identifiable information of its customers and employees, in its data centers and on its networks. The secure processing, maintenance and transmission of this information is critical to the Company's operations and business strategy. Maintaining and protecting those systems is difficult and expensive, as is dealing with any failure, interruption or breach of those systems. Despite security measures, the Company's information technology and infrastructure may be vulnerable to security breaches, cyber attacks by hackers or breaches due to employee error, malfeasance or other disruptions. Any damage, failure or breach could cause an interruption in the Company's operations. Computer break-ins, phishing and other disruptions could also jeopardize the security of information stored in and transmitted through the Company's computer systems and network infrastructure. The occurrence of any failures, interruptions or breaches could damage the Company's reputation, disrupt operations and the services provided to customers, cause a loss of confidence in the products and the services provided, cause the Company to incur additional expenses, result in a loss of customer business and data, result in legal claims or proceedings, result in liability under laws that protect the privacy of personal information, result in regulatory penalties, or expose the Company to other liability, any of which could have a material adverse effect on the Company's business, financial condition and results of operations and the Company's competitive position.

If the Company's information technology is unable to keep pace with growth or industry developments or if technological developments result in higher costs or less advantageous pricing, financial performance may suffer.

Effective and competitive delivery of the Company's products and services increasingly depends on information technology resources and processes, both those provided internally as well as those provided through third party vendors. In addition to better serving customers, the effective use of technology can improve efficiency and help reduce costs. The Company's future success will depend, in part, upon its ability to address the needs of its customers by using technology to provide products and services to enhance customer convenience, as well as to create efficiencies in its operations. There is increasing pressure to provide products and services at lower prices. This can reduce net interest income and noninterest income from fee-based products and services. In addition, the widespread adoption of new technologies could require the Company to make substantial capital expenditures to modify or adapt existing products and services or develop new products and services. The Company may not be successful in

introducing new products and services in response to industry trends or developments in technology, or those new products may not achieve market acceptance. Many of the Company's competitors have greater resources to invest in technological improvements. Additionally, as technology in the financial services industry changes and evolves, keeping pace becomes increasingly complex and expensive. There can be no assurance that the Company will be able to effectively implement new technology-driven products and services, which could reduce its ability to compete effectively. As a result, the Company could lose business, be forced to price products and services on less advantageous terms to retain or attract customers, or be subject to cost increases.

The Company's profitability depends significantly on economic conditions in the Commonwealth of Pennsylvania, specifically in Lackawanna, Luzerne and Wayne Counties.

The Company's success depends primarily on the general economic conditions in the Commonwealth of Pennsylvania and the specific local markets in which the Company operates. Unlike larger national or other regional banks that are more geographically diversified, the Company provides banking and financial services to customers primarily in the Lackawanna, Luzerne and Wayne County markets. The local economic conditions in these areas have a significant impact on the demand for the Company's products and services as well as the ability of the Company's customers to repay loans, the value of the collateral securing loans, and the stability of the Company's deposit funding sources. A significant decline in general economic conditions, caused by inflation, recession, acts of terrorism, severe weather or natural disasters, outbreak of hostilities or other international or domestic occurrences, unemployment, changes in securities markets or other factors could impact these local economic conditions and, in turn, have a material adverse effect on the Company's financial condition and results of operations.

The Company relies on management and other key personnel and the loss of any of them may adversely affect its operations.

The Company believes each member of the senior management team is important to the Company's success and the unexpected loss of any of these persons could impair day-to-day operations as well as its strategic direction.

The Company's success depends, in large part, on its ability to attract and retain key people. Competition for the best people in most activities engaged in by the Company can be intense and the Company may not be able to hire people or retain them. The unexpected loss of services of one or more of the Company's key personnel could have a material adverse impact on the Company's business due to the loss of their skills, knowledge of the Company's market, years of industry experience and to the difficulty of promptly finding qualified replacement personnel.

The Company may be a defendant from time to time in a variety of litigation and other actions, which could have a material adverse effect on its financial condition, results of operations and cash flows.

The Company has been and may continue to be involved from time to time in a variety of litigation matters arising out of its business. An increased number of lawsuits, including purported class action lawsuits and other consumer driven litigation, have been filed and will likely continue to be filed against financial institutions, which may involve substantial compensatory and/or punitive damages. The Company believes the risk of litigation generally increases during downturns in the national and local economies. The Company's insurance may not cover all claims that may be asserted against it, and any claims asserted against it, regardless of merit or eventual outcome, may harm the Company's reputation and may cause it to incur significant expense. Should the ultimate judgments or settlements in any litigation exceed the Company's insurance coverage, they could have a material adverse effect on its financial condition, results of operations and cash flows. In addition, the Company may not be able to obtain appropriate types or levels of insurance in the future, nor may the Company be able to obtain adequate replacement policies with acceptable terms, if at all. For additional discussion of the Company's current legal matters, refer to Item 3, "Legal Proceedings" to this Annual Report on Form 10-K.

The Company's disclosure controls and procedures and internal controls over financial reporting may not achieve their intended objectives.

The Company maintains disclosure controls and procedures designed to ensure the timely filing of reports as specified in the rules and forms of the Securities and Exchange Commission. The Company also maintains a system of internal control over financial reporting. These controls may not achieve their intended objectives. Control processes that involve human diligence and compliance, such as its disclosure controls and procedures and internal controls over

financial reporting, are subject to lapses in judgment and breakdowns resulting from human failures. Controls can also be circumvented by collusion or improper management override. Because of such limitations, there are risks that material misstatements due to error or fraud may not be prevented or detected and that information may not be reported on a timely basis. If the Company’s controls are not effective, it could have a material adverse effect on its financial condition, results of operations, and market for its common stock, and could subject the Company to additional regulatory scrutiny.

Risks Related to the Company’s Common Stock

The price of the Company’s common shares may fluctuate significantly, which may make it difficult for investors to resell common shares at a time or price they find attractive.

The Company’s share price may fluctuate significantly as a result of a variety of factors, many of which are beyond its control. These factors include, in addition to those described above:

- actual or anticipated quarterly fluctuations in operating results and financial condition;
- changes in financial estimates or publication of research reports and recommendations by financial analysts or actions taken by rating agencies with respect to the Company or other financial institutions;
- speculation in the press or investment community generally or relating to the Company’s reputation or the financial services industry;
- strategic actions by the Company or its competitors, such as acquisitions, restructurings, dispositions or financings;
- fluctuations in the stock price and operating results of the Company’s competitors;
- future sales of the Company’s equity or equity-related securities;
- proposed or adopted regulatory changes or developments;
- anticipated or pending investigations, proceedings, audits or litigation that involve or affect the Company;
- domestic and international economic factors unrelated to the Company’s performance; and
- general market conditions and, in particular, developments related to market conditions for the financial services industry.

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In addition, in recent years, the stock market in general has experienced extreme price and volume fluctuations. This volatility has had a significant effect on the market price of securities issued by many companies, including for reasons unrelated to their operating performance. These broad market fluctuations may adversely affect the Company's share price, notwithstanding the Company's operating results. The Company expects that the market price of its common shares will continue to fluctuate and there can be no assurances about the levels of the market prices for its common shares.

An active public market for the Company's common stock does not currently exist. As a result, shareholders may not be able to quickly and easily sell their common shares.

The Company's common shares are currently quoted on OTC Markets Group, Inc. During the year ended December 31, 2015, an average of 1817 shares traded on a daily basis. There can be no assurance that an active and liquid market for the Company's common shares will develop, or if one develops that it can be maintained. The absence of an active trading market may make it difficult to subsequently sell the Company's common shares at the prevailing price, particularly in large quantities. For a further discussion, see Item 5- "Market for Registrant's Common Equity, Related Shareholder Matters, and Issuer Purchases of Equity Securities" to this Annual Report on Form 10-K.

The Company's ability to pay dividends or repurchase shares is subject to limitiations.

The Company conducts its principal business operations through the Bank and the cash that it uses to pay dividends is derived from dividends paid to the Company by the Bank; therefore, its ability to pay dividends is dependent on the performance of the Bank and on the Bank's capital requirements. The Bank's ability to pay dividends to the Company and the Company's ability to pay dividends to its shareholders are also limited by certain legal and regulatory restrictions.

Risks Related to Government Regulation and Accounting Pronouncements

The Company is subject to extensive government regulation, supervision and possible regulatory enforcement actions, which may subject it to higher costs and lower shareholder returns.

The banking industry is subject to extensive regulation and supervision that govern almost all aspects of its operations. The extensive regulatory framework is primarily intended to protect the federal deposit insurance fund and depositors, not shareholders. The Company and Bank are regulated and supervised by the FRB and the OCC. Compliance with

applicable laws and regulations can be difficult and costly and, in some instances, may put banks at a competitive disadvantage compared to less regulated competitors such as finance companies, mortgage banking companies and leasing companies. The Company's regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including with respect to the imposition of restrictions on the operation of a bank or a bank holding company, the imposition of significant fines, the ability to delay or deny merger or other regulatory applications, the classification of assets by a bank, and the adequacy of a bank's allowance for loan losses, among other matters. The Company's industry is facing increased regulation and scrutiny; for instance, areas such as BSA compliance (including BSA and related anti-money laundering regulations) and real estate-secured consumer lending (such as Truth-in-Lending regulations, changes in Real Estate Settlement Procedures Act regulations, implementation of licensing and registration requirements for mortgage originators and more recently, heightened regulatory attention to mortgage and foreclosure-related activities and exposures) are being confronted with escalating regulatory expectations and scrutiny. Non-compliance with laws and regulations such as these, even in cases of inadvertent non-compliance, could result in litigation, significant fines and/or sanctions. Any failure to comply with, or any change in, any applicable regulation and supervisory requirement, or change in regulation or enforcement by such authorities, whether in the form of policies, regulations, legislation, rules, orders, enforcement actions, or decisions, could have a material impact on the Company, the Bank and other affiliates, and its operations. Federal economic and monetary policy may also affect the Company's ability to attract deposits and other funding sources, make loans and investments, and achieve satisfactory interest spreads. Any failure to comply with such regulation or supervision could result in sanctions by regulatory agencies, civil money penalties and/or reputation damage, which could have a material adverse effect on the Company's business, financial condition and results of operations. In addition, compliance with any such action could distract management's attention from the Company's operations, cause the Company to incur significant expenses, restrict it from engaging in potentially profitable activities and limit its ability to raise capital.

The impact of recent legislation, proposed legislation, and government programs designed to stabilize the financial markets cannot be predicted at this time, and such legislation is subject to change. In addition, the failure of financial markets to stabilize and a continuation or worsening of current financial market conditions could materially and adversely affect the Company's business, financial condition, results of operations and access to capital.

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New or changed legislation or regulation and regulatory initiatives could adversely affect the Company through increased regulation and increased costs of doing business.

Changes in federal and state legislation and regulation may affect the Company's operations. New and modified regulation, such as the Dodd-Frank Act and Basel III, may have unforeseen or unintended consequences on the banking industry. The Dodd-Frank Act has implemented significant changes to the U.S. financial system, including the creation of new regulatory agencies (such as the Financial Stability Oversight Council to oversee systemic risk and the CFPB to develop and enforce rules for consumer financial products), changes in retail banking regulations, and changes to deposit insurance assessments. For example, the Dodd-Frank Act has implemented new requirements with respect to "qualified mortgages" and new mortgage servicing standards that may increase costs associated with this business. For a more detailed description, see the section entitled "Business – The Bank – *Consumer Financial Protection Bureau*" included in Item 1 to this Annual Report on Form 10-K.

Additionally, final rules to implement Basel III adopted in July 2013 revise risk-based and leverage capital requirements and also limit capital distributions and certain discretionary bonuses if a banking organization does not hold a "capital conservation buffer." The rule became effective for the Company on January 1, 2015, with some additional transition periods. This additional regulation could increase compliance costs and otherwise adversely affect operations. For a more detailed description of the final rules, see the description in Item 1 of this Annual Report on Form 10-K under the heading "Capital Adequacy Requirements". The potential also exists for additional federal or state laws or regulations, or changes in policy or interpretations, affecting many of the Company's operations, including capital levels, lending and funding practices, insurance assessments, and liquidity standards. The effect of any such changes and their interpretation and application by regulatory authorities cannot be predicted, may increase the Company's cost of doing business and otherwise affect the Company's operations, may significantly affect the markets in which the Company does business, and could have a materially adverse effect on the Company.

The Company is also subject to the guidelines under the Gramm-Leach-Bliley Act ("GLBA"). The GLBA guidelines require, among other things, that each financial institution develop, implement and maintain a written, comprehensive information security program containing safeguards that are appropriate to the financial institution's size and complexity, the nature and scope of the financial institution's activities and the sensitivity of any customer information at issue. In recent years there also has been increasing enforcement activity in the areas of privacy, information security and data protection in the United States, including at the federal level. Compliance with these laws, rules and regulations regarding the privacy, security and protection of customer and employee data could result in higher compliance and technology costs. In addition, non-compliance could result in potentially significant fines, penalties and damage to the Company's reputation and brand.

Changes in accounting standards could impact reported earnings.

From time to time there are changes in the financial accounting and reporting standards that govern the preparation of financial statements. These changes can materially impact how the Company records and reports its financial condition and results of operations. In some instances, the Company could be required to apply a new or revised standard retroactively, resulting in the restatement of prior period financial statements.

Item 1B. Unresolved Staff Comments.

None.

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Item 2. Properties.

The Company currently conducts business from its main office located at 102 East Drinker Street, Dunmore, Pennsylvania, 18512 and from its additional 18 branches located throughout Lackawanna, Luzerne and Wayne counties. At December 31, 2015, aggregate net book value of premises and equipment was $11.2 million. With the exception of potential remodeling of certain facilities to provide for the efficient use of work space and/or to maintain an appropriate appearance, each property is considered reasonably adequate for current and anticipated needs.

Property	Location	Ownership	Type of Use
1	102 East Drinker Street Dunmore, PA	Own	Main Office/Branch
2	419-421 Spruce Street Scranton, PA	Own	Scranton Branch
3	934 Main Street Dickson City, PA	Own	Dickson City Branch
4	1743 North Keyser Avenue Scranton, PA	Lease	Keyser Village Branch
5	1 North Main Street Wilkes-Barre, PA	Lease	Wilkes-Barre Branch
6	1700 North Township Blvd. Pittston, PA	Lease	Pittston Plaza Branch
7	754 Wyoming Avenue Kingston, PA	Lease	Kingston Branch
8	1625 Wyoming Avenue Exeter, PA	Lease	Exeter Branch
9	Route 502 & 435 Daleville, PA	Lease	Daleville Branch
10	27 North River Road Plains, PA	Lease	Plains Branch

11	1919 Memorial Highway Shavertown, PA	Lease	Back Mountain Branch
12	269 East Grove Street Clarks Green, PA	Own	Clarks Green Branch
13	734 Sans Souci Parkway Hanover Township, PA	Lease	Hanover Township Branch
14	194 South Market Street Nanticoke, PA	Own	Nanticoke Branch
15	330-352 West Broad Street Hazleton, PA	Own	Hazleton Branch

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Property	Location	Ownership	Type of Use
15	330-352 West Broad Street Hazleton, PA	Own	Hazleton Branch
16	3 Old Boston Road Pittston, PA	Lease	Route 315 Branch
17	1001 Main Street Honesdale, PA	Own	Honesdale Branch
18	1127 Texas Palmyra Highway Honesdale, PA	Lease	Honesdale Route 6 Branch
19	200 South Blakely Street Dunmore, PA	Lease	Administrative Center
20	107-109 South Blakely Street Dunmore, PA	Own	Parking Lot
21	114-116 South Blakely Street Dunmore, PA	Own	Parking Lot
22	1708 Tripp Avenue Dunmore, PA	Own	Parking Lot
23	119-123 South Blakely Street Dunmore, PA	Own	Parking Lot
24	Main Street Taylor, PA	Own	Land
25	1219 Wheeler Avenue Dunmore, PA	Lease	Wheeler Ave. Branch
26	124 South Blakely Street Dunmore, PA	Own	Bank Offices
27	100 Commerce Boulevard Wilkes-Barre, PA	Lease	Commercial Lending Office

Item 3. Legal Proceedings.

On August 8, 2011, the Company announced that it had received document subpoenas from the SEC. The information requested generally related to disclosure and financial reporting by the Company and the restatement of the Company's financial statements for the year ended December 31, 2009, and the quarters ended March 31, 2010 and June 30, 2010. On January 28, 2015, the Company and the SEC entered into a settlement agreement resolving these issues related to disclosure and financial reporting and the restatements of the Company's financial statements for the year ended December 31, 2009 and the quarters ended March 31, 2010 and June 30, 2010. As part of this settlement agreement, on January 30, 2015 the Company paid a civil money penalty of $175 thousand to the SEC. The Company accrued for the $175 thousand civil money penalty in its 2014 results of operations.

On May 24, 2012, a putative shareholder filed a complaint in the Court of Common Pleas for Lackawanna County ("Shareholder Derivative Suit") against certain present and former directors and officers of the Company (the "Individual Defendants") alleging, inter alia, breach of fiduciary duty, abuse of control, corporate waste, and unjust enrichment. The Company was named as a nominal defendant. The parties to the Shareholder Derivative Suit commenced settlement discussions and on December 18, 2013, the Court entered an Order Granting Preliminary Approval of Proposed Settlement subject to notice to shareholders. On February 4, 2014, the Court issued a Final Order and Judgment for the matter granting approval of a Stipulation of Settlement (the "Settlement") and dismissing all claims against the Company and the Individual Defendants. As part of the Settlement, there was no admission of liability by the Individual Defendants. Pursuant to the Settlement, the Individual Defendants, without admitting any fault, wrongdoing or liability, agreed to settle the derivative litigation for $5.0 million. The $5.0 million Settlement payment was made to the Company on March 28, 2014. The Individual Defendants reserved their rights to indemnification under the Company's Articles of Incorporation and Bylaws, resolutions adopted by the Board, the Pennsylvania Business Corporation Law and any and all rights they have against the Company's and the Bank's insurance carriers. In addition, in conjunction with the Settlement, the Company accrued $2.5 million related to fees and costs of the plaintiff's attorneys, which was included in non-interest expense in the Consolidated Statements of Income for the year ended December 31, 2013. On April 1, 2014, the Company paid the $2.5 million related to fees and costs of the plaintiff's attorneys and partial indemnification of the Individual Defendants in the amount of $2.5 million, and as such, as of December 31, 2015 $2.5 million plus accrued interest remains accrued in other liabilities related to the potential indemnification of the Individual Defendants. The Company settled any and all claims it had or may have had against Demetrius & Company, LLC, John Demetrius and Robert L. Rossi & Company in connection with the Shareholder Derivative Suit in 2014.

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On September 5, 2012, Fidelity and Deposit Company of Maryland ("F&D") filed an action against the Company and the Bank, as well as several current and former officers and directors of the Company, in the United States District Court for the Middle District of Pennsylvania. F&D has asserted a claim for the rescission of a directors' and officers' insurance policy and a bond that it had issued to the Company. On November 9, 2012, the Company and the Bank answered the claim and asserted counterclaims for the losses and expenses already incurred by the Company and the Bank. The Company and the other defendants are defending the claims and have opposed F&D's requested relief by way of counterclaims, breaches of contract and bad faith claims against F&D for its failure to fulfill its obligations to the Company and the Bank under the insurance policy. At this time, the matter is in the discovery stage and the Company cannot reasonably determine the outcome or potential range of loss in connection with this matter.

On August 13, 2013, Steven Antonik, individually, as Administrator of the Estate of Linda Kluska, William R. Howells, and Louise A. Howells, on behalf of themselves and others similarly situated, filed a consumer protection class action against the Company and Bank in the Lackawanna County Court of Common Pleas, seeking equitable, injunction and monetary relief to address an alleged pattern and practice of wrong doing by the Bank relating to the repossession and sale of the Plaintiffs' and class members' financed motor vehicles. On December 17, 2015 the Honorable Margaret Moyle entered an Order outlining the primary terms of a tentative agreement to settle this matter, pending a finalized, more-detailed settlement agreement, class notice and a class fairness hearing, said Order covering both this matter and the matter involving Plaintiff Charles Saxe, II individually and on behalf of all others similarly situated. The primary terms of the tentative agreement to settle are 1) Defendants to pay the Plaintiffs' class members, which the Defendants have stated are approximately 430 members, the total sum of $750,000; 2) Plaintiffs will release all claims against Defendants; 3) Defendants will remove to vacate any judgements against any class members arising from the vehicle loans that are the subject of these actions; 4) Defendants will remove the trade line on each class member's credit report associated with the subject vehicle loans that are at issue in these actions for Experian, Equifax and TransUnion, providing Plaintiffs' counsel with verification of such; 5) Defendants will verify that the aggregate amount received from class members by Defendants and its agents during the alleged unjust enrichment class period does not exceed $45,000; and 6) Defendants will waive the disputed deficiency balances relating to the subject loans of each class member and agree not to issue IRS Forms 1099-C in connection with these deficiency waivers or to sell, assign , or otherwise collect on the alleged deficiencies.

On September 17, 2013, Charles Saxe, III individually and on behalf of all others similarly situated filed a consumer class action against the Bank in the Lackawanna County Court of Common Pleas alleging violations of the Pennsylvania Uniform Commercial Code in connection with the repossession and resale of financed vehicles. On December 17, 2015 the Honorable Margaret Moyle entered an Order outlining the primary terms of a tentative agreement to settle this matter, pending a finalized, more-detailed settlement agreement, class notice and a class fairness hearing, said Order covering both this matter and the matter involving Plaintiffs Steven Antonik, individually, as Administrator of the Estate of Linda Kluska, William R. Howells, and Louise A. Howells, on behalf of themselves and all others similarly situated. The primary terms of the tentative agreement to settle are 1) Defendants to pay the Plaintiffs' class members, which the Defendants have stated are approximately 430 members, the total sum of $750,000; 2) Plaintiffs will release all claims against Defendants; 3) Defendants will remove to vacate any judgements against any class members arising from the vehicle loans that are the subject of these actions; 4) Defendants will remove the trade line on each class member's credit report associated with the subject vehicle loans that are at issue in these actions for Experian, Equifax and TransUnion, providing Plaintiffs' counsel with verification of such; 5) Defendants will verify that the aggregate amount received from class members by Defendants and its agents during

the alleged unjust enrichment class period does not exceed $45,000; and 6) Defendants will waive the disputed deficiency balances relating to the subject loans of each class member and agree not to issue IRS Forms 1099-C in connection with these deficiency waivers or to sell, assign , or otherwise collect on the alleged deficiencies.

On January 22, 2014, the Bank was advised by the Department of Treasury's Financial Crimes Enforcement Network ("FinCEN") that FinCEN was investigating the Bank for alleged violations of the Bank Secrecy Act ("BSA"). On May 28, 2014 the Bank was advised by the OCC that the OCC was investigating allegations that the Bank failed to file timely SARS. On November 18, 2014 both FinCEN and OCC advised the Bank that they intended on assessing civil money penalties against the Bank. Subsequent to November 18, 2014, the Bank had been in discussions with both regulatory agencies about the alleged BSA violations. On February 27, 2015, the Bank reached a comprehensive settlement with FinCEN and OCC to resolve the BSA allegations. In order to settle the matter, the Bank consented to an aggregate civil money penalty assessment of $1.5 million which was accrued for at December 31, 2014 and included in non-interest expense for the year ended December 31, 2014. The Company paid the $1.5 million civil money penalty on February 27, 2015.

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The Company has been subject to tax audits and is also a party to routine litigation involving various aspects of its business, such as employment practice claims, claims to enforce liens, condemnation proceedings on properties in which the Company holds security interests, claims involving the making and servicing of real property loans and other issues incident to its business, none of which has or is expected to have a material adverse impact on the consolidated financial condition, results of operations or liquidity of the Company.

Item 4. Mine Safety Disclosures.

Not Applicable.

PART II

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

Market Prices of Stock and Dividends Paid

Effective February 17, 2015, the Company's common shares are quoted on the OTCQX Marketplace operated by the OTC Markets Group, Inc. under the sysmbol "FNCB." Previous to this date, the Company's common shares were quoted on the OTCQB Venture Marketplace operated by the OTC Markets Group, Inc. The principal market area for the Company's shares is northeastern Pennsylvania, although shares are held by residents of other states across the country. Quarterly market highs and lows and dividends paid for each of the past two years are presented below. These prices represent actual transactions.

	Market Price		**Dividends Paid**
	High	**Low**	**Per Share**
Quarter	**2015**		**2015**
First	$6.10	$5.12	$ 0.00
Second	6.55	5.15	0.00
Third	6.05	5.02	0.00
Fourth	5.50	5.06	0.00
Quarter	**2014**		**2014**

First	$9.90	$5.91	$0.00
Second	6.85	5.15	0.00
Third	6.85	5.75	0.00
Fourth	6.65	5.60	0.00

Holders

As of February 29, 2016 there were approximately 1,778 holders of record of the Company's common shares. Because many of the Company's shares are held by brokers and other institutions on behalf of shareholders, the Company is unable to estimate the total number of shareholders represented by these record holders.

Dividends

From February 26, 2010 through September 2, 2015, as a result of the Order and Agreement, the Company suspended paying dividends For a further discussion of the Company's dividend limitations, refer to the section entitled "Capital Analysis" included in Item 7 "Management's Discussion and Analysis" to this Annual Report on Form 10-K.

Equity Compensation Plans

For more information regarding the Company's equity compensation plans, see Part III, Item 12 "Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters" to this Annual Report on Form 10-K.

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Performance Graph

The following graph compares the cumulative total shareholder return (i.e. price change, reinvestment of cash dividends and stock dividends received) on the Company's common shares against the cumulative total return of the NASDAQ Stock Market (U.S. Companies) Index, the SNL Bank Index for banks with $500 million to $1 billion in assets and the SNL U.S. Bank Pink for banks traded on the OTC with total assets greater than $500 million. The stock performance graph assumes that $100 was invested on December 31, 2010. The graph further assumes the reinvestment of dividends into additional shares of the same class of equity securities at the frequency with which dividends are paid on such securities during the relevant fiscal year. The yearly points marked on the horizontal axis correspond to December 31 of that year. The Company calculates each of the referenced indices in the same manner. All are market-capitalization-weighted indices, so companies judged by the market to be more important (i.e. more valuable) count for more in all indices.

First National Community Bancorp, Inc.

	Period Ending					
Index	**12/31/10**	**12/31/11**	**12/31/12**	**12/31/13**	**12/31/14**	**12/31/15**
First National Community Bancorp, Inc.	100.00	83.06	100.66	289.04	199.34	174.42
NASDAQ Composite	100.00	99.21	116.82	163.75	188.03	201.40
SNL Bank $500M-$1B	100.00	87.98	112.79	146.26	160.46	181.11
SNL Bank Pink > $500M	100.00	98.32	108.42	131.77	154.48	171.37

(*) Source: SNL Financial LC, Charlottesville, VA © 2011. SNL Securities is a research and publishing firm specializing in the collection and dissemination of data on the banking, thrift and financial services industries.

Purchase of Equity Securities by the Issuer or Affiliates Purchasers

None.

Recent Sales of Unregistered Securities

On November 25, 2015, the Board of Directors adopted the 2015 Employee Stock Grant Plan (the “2015 Stock Grant Plan”) under which shares of common stock not to exceed 13,550 were authorized to be granted to employees. On the same date the Company granted 50 shares of the Company’s common stock to each active full and part time employee. There were 13,300 shares issued under this grant at a fair value of $5.15 per share on the date of the grant. The total cost of these grants, which was included in salary expense in the Consolidated Statements of Income, amounted to $68 thousand for the year ended December 31, 2015. No additional shares were granted under this plan. This share grant was effected without registration under the Securities Act in reliance upon Section 2(a)(3) of the Securities Act, as a non-sale distribution of securities by the Company. These shares were given to all employees of the Company as a share bonus and not as individual incentive compensation or in lieu of a cash payment, with no investment decision on the part of the recipients or receipt of value by the Company in return. There were no underwriters employed in the issuance of the securities or in connection with this transaction, and no proceeds were received by the Company for this stock grant. There have been no sales of unregistered securities during 2015.

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Item 6. Selected Financial Data

The selected consolidated financial and other data and management's discussion and analysis of financial condition and results of operations set forth below and in Item 7 hereof is derived in part from, and should be read in conjunction with, the consolidated financial statements and notes thereto contained elsewhere herein. Certain reclassifications have been made to prior years' consolidated financial statements to conform to the current year's presentation. Those reclassifications did not impact net income.

	For the Years Ended December 31,				
(dollars in thousands, except per share data)	2015	2014	2013	2012	2011
Balance Sheet Data:					
Total assets	$1,090,618	$970,029	$1,003,808	$968,274	$1,102,639
Securities, available-for-sale	253,773	218,989	203,867	185,361	185,475
Securities, held-to-maturity	-	-	2,308	2,198	2,094
Net loans	724,926	658,747	629,880	579,396	659,044
Total deposits	821,546	795,336	884,698	854,613	957,136
Borrowed funds	160,112	96,504	62,433	53,903	83,571
Shareholders' equity	86,178	51,398	33,578	36,925	39,925
Income Statement Data:					
Interest income	$32,201	$32,673	$32,953	$37,027	$42,936
Interest expense	4,801	6,147	7,176	9,218	13,867
Net interest income before (credit) provision for loan and lease losses	27,400	26,526	25,777	27,809	29,069
(Credit) provision for loan and lease losses	(1,345)	(5,869)	(6,270)	4,065	523
Non-interest income	7,800	14,920	9,283	4,283	12,949
Non-interest expense	28,464	33,569	34,948	41,738	41,830
Income (loss) before income taxes	8,081	13,746	6,382	(13,711)	(335)
Income tax (benefit) expense	(27,759)	326	-	-	-
Net income (loss)	35,840	13,420	6,382	(13,711)	(335)
Earnings (loss) per share, basic and diluted	2.17	0.81	0.39	(0.83)	(0.02)
Capital and Related Ratios:					
Cash dividends declared per share	$-	$-	$-	$-	$-
Book value per share	5.22	3.12	2.04	2.24	2.43
Tier I leverage ratio	7.27%	6.05%	4.71%	4.07%	4.72%
Total risk-based capital to risk-adjusted assets	11.79%	13.67%	11.58%	10.20%	11.35%
Average equity to average total assets (1)	5.64%	4.66%	3.60%	3.97%	3.04%
Tangible equity to tangible assets	7.89%	5.27%	3.30%	3.75%	3.55%
Selected Performance Ratios:					
Return on average assets (1)	3.57%	1.38%	0.67%	(1.35%)	(0.03%)
Return on average equity (1)	68.24%	29.50%	18.65%	(34.09%)	(0.98%)

Net interest margin (2)	2.99	%	3.08	%	3.21	%	3.26	%	3.10	%
Noninterest income/operating income (2)	18.73	%	30.30	%	20.79	%	9.71	%	21.82	%
Asset Quality Ratios:										
Allowance for loan and lease losses/total loans	1.20	%	1.72	%	2.18	%	3.10	%	3.07	%
Nonperforming loans/total loans	0.52	%	0.82	%	0.99	%	1.62	%	2.93	%
Allowance for loan and lease losses/nonperforming loans	232.05	%	208.62	%	219.87	%	190.92	%	104.60	%
Net charge-offs/average loans	0.20	%	(0.51%	)	(0.28%	)	0.97	%	0.31	%
Loan loss provision/net charge-offs	***		***		***		63.88	%	23.10	%

*** Ratio is not meaningful for 2015, 2014 and 2013.

(1) Average balances were calculated using average daily balances. Average balances for loans include non-accrual loans.

(2) Tax-equivalent adjustments were calculated using the prevailing statutory rate of 34.0 percent.

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

Management's discussion and analysis ("MD&A") represents an overview of the financial condition and results of operations and should be read in conjunction with our consolidated financial statements and notes thereto included in Item 8 and Risk Factors detailed in Item 1A of Part I to this Annual Report on Form 10-K.

The Company is in the business of providing customary retail and commercial banking services to individuals and businesses. The Company's core market is Northeastern Pennsylvania.

FORWARD-LOOKING STATEMENTS

The Company may from time to time make written or oral "forward-looking statements," including statements contained in the Company's filings with the Securities and Exchange Commission ("SEC"), in its reports to shareholders, and in other communications by the Company, which are made in good faith by the Company pursuant to the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements include statements with respect to the Company's beliefs, plans, objectives, goals, expectations, anticipations, estimates and intentions, that are subject to significant risks and uncertainties, and are subject to change based on various factors (some of which are beyond the Company's control). The words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan" and similar expressions are intended to ident forward-looking statements. The following factors, among others, could cause the Company's financial performance to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in the Company's markets; the effects of, and changes in trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System; inflation, interest rate, market and monetary fluctuations; the timely development of and acceptance of new products and services; the ability of the Company to compete with other institutions for business; the composition and concentrations of the Company's lending risk and the adequacy of the Company's reserves to manage those risks; the valuation of the Company's investment securities; the ability of the Company to pay dividends or repurchase common shares; the ability of the Company to retain key personnel; the impact of any pending or threatened litigation against the Company; the marketability of shares of the Company and fluctuations in the value of the Company's share price; the impact of the Company's ability to comply with its regulatory agreements and orders; the effectiveness of the Company's system of internal controls; the ability of the Company to attract additional capital investment; the impact of changes in financial services' laws and regulations (including laws concerning capital adequacy, taxes, banking, securities and insurance); the impact of technological changes and security risks upon the Company's information technology systems; changes in consumer spending and saving habits; the nature, extent, and timing of governmental actions and reforms, and the success of the Company at managing the risks involved in the foregoing and other risks and uncertainties, including those detailed in the

Company’s filings with the SEC.

The Company cautions that the foregoing list of important factors is not all inclusive. Readers are also cautioned not to place undue reliance on any forward-looking statements, which reflect management’s analysis only as of the date of this report, even if subsequently made available by the Company on its website or otherwise. The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company to reflect events or circumstances occurring after the date of this report.

CRITICAL ACCOUNTING POLICIES

In preparing the consolidated financial statements, management has made estimates, judgments and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated statements of condition and results of operations for the periods indicated. Actual results could differ significantly from those estimates.

The Company’s accounting policies are fundamental to understanding management’s discussion and analysis of its financial condition and results of operations. Management has identified the policies on the determination of the allowance for loan and lease losses (“ALLL”), securities’ valuation and impairment evaluation, and the valuation of other real estate owned (“OREO”) and income taxes to be critical, as management is required to make subjective and/or complex judgments about matters that are inherently uncertain and could be most subject to revision as new information becomes available.

The judgments used by management in applying the critical accounting policies discussed below may be affected by a further and prolonged deterioration in the economic environment, which may result in changes to future financial results. Specifically, subsequent evaluations of the loan portfolio, in light of the factors then prevailing, may result in significant changes in the ALLL in future periods, and the inability to collect on outstanding loans could result in increased loan losses. In addition, the valuation of certain securities in the Company’s investment portfolio could be negatively impacted by illiquidity or dislocation in marketplaces resulting in significantly depressed market prices thus leading to impairment losses.

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Allowance for Loan and Lease Losses

Management evaluates the credit quality of the Company's loan portfolio on an ongoing basis, and performs a formal review of the adequacy of the ALLL on a quarterly basis. The ALLL is established through a provision for loan losses charged to earnings and is maintained at a level management considers adequate to absorb estimated probable losses inherent in the loan portfolio as of the evaluation date. Loans, or portions of loans, determined by management to be uncollectible are charged off against the ALLL, while recoveries of amounts previously charged off are credited to the ALLL.

Determining the amount of the ALLL is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, qualitative factors, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. Banking regulators, as an integral part of their examination of the Company, also review the ALLL. Such regulators may require, based on their judgments about information available to them at the time of their examination, that certain loan balances be charged off or require that adjustments be made to the ALLL. Additionally, the ALLL is determined, in part, by the composition and size of the loan portfolio.

The ALLL consists of two components, a specific component and a general component. The specific component relates to loans that are classified as impaired. For such loans, an allowance is established when the discounted cash flows, collateral value or observable market price of the impaired loan is lower than the carrying value of that loan. The general component covers all other loans and is based on historical loss experience adjusted by qualitative factors. The general reserve component of the ALLL is based on pools of unimpaired loans segregated by loan segment and risk rating categories of "Pass", "Special Mention" or "Substandard and Accruing." Historical loss factors and various qualitative factors are applied based on the risk profile in each risk rating category to determine the appropriate reserve related to those loans. Substandard loans on nonaccrual status above the $100 thousand loan relationship threshold and all loans considered troubled debt restructurings ("TDRs") are classified as impaired.

See Note 2-"Summary of Significant Accounting Policies" and Note 5-"Loans" of the notes to consolidated financial statements included in Item 8-"Financial Statements and Supplementary Data" to this Annual Report on Form 10-K for additional information about the ALLL.

Securities Valuation and Evaluation for Impairment

Management utilizes various inputs to determine the fair value of its investment portfolio. To the extent they exist, unadjusted quoted market prices in active markets (Level 1) or quoted prices for similar assets or models using inputs that are observable, either directly or indirectly (Level 2) are utilized to determine the fair value of each investment in the portfolio. In the absence of observable inputs or if markets are illiquid, valuation techniques are used to determine fair value of any investments that require inputs that are both unobservable and significant to the fair value measurement (Level 3). For Level 3 inputs, valuation techniques are based on various assumptions, including, but not limited to, cash flows, discount rates, adjustments for nonperformance and liquidity, and liquidation values. A significant degree of judgment is involved in valuing investments using Level 3 inputs. The use of different assumptions could have a positive or negative effect on the consolidated statements of financial condition or results of operations. See Note 6-“Securities” and Note 7-“Fair Value Measurements” of the notes to consolidated financial statements included in Item 8 – “Financial Statements and Supplementary Data” to this Annual Report on Form 10-K for additional information about the Company’s securities valuation techniques.

On a quarterly basis, management evaluates individual investment securities classified as held-to-maturity and available-for-sale having unrealized losses to determine whether or not the security is other-than-temporarily-impaired (“OTTI”). The analysis of OTTI requires the use of various assumptions, including but not limited to, the length of time an investment’s fair value is less than book value, the severity of the investment’s decline, any credit deterioration of the issuer, whether management intends to sell the security, and whether it is more-likely-than-not that the Company will be required to sell the security prior to recovery of its amortized cost basis. Debt investment securities deemed to be OTTI are written down by the impairment related to the estimated credit loss, and the non-credit related impairment loss is recognized in other comprehensive income. The Company did not recognize OTTI charges on investment securities for years ended December 31, 2015, 2014 and 2013 within the consolidated statements of income.

See Note 2-“Summary of Significant Accounting Policies” and Note 4-“Securities” of the notes to consolidated financial statements included in Item 8-“Financial Statements and Supplementary Data” to this Annual Report on Form 10-K for additional information about valuation of securities.

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Other Real Estate Owned

OREO consists of property acquired through foreclosure, abandonment or conveyance of deed in-lieu of foreclosure of a loan, and bank premises that is no longer used for operation or for future expansion. OREO is held for sale and is initially recorded at fair value less costs to sell at the date of acquisition or transfer, which establishes a new cost basis. Upon acquisition of the property through foreclosure or deed-in-lieu of foreclosure, any write-down to fair value less estimated selling costs is charged to the ALLL. The determination is made on an individual asset basis. Bank premises no longer used for operations or future expansion are transferred to OREO at fair value less estimated selling costs with any related write-down included in non-interest expense unless conditions warrant an adjustment to value, as determined by management. Subsequent to acquisition, valuations are periodically performed by management and the assets are carried at the lower of cost basis or fair value less cost to sell. Fair value is determined through external appraisals, current letters of intent, broker price opinions or executed agreements of sale. Costs relating to the development and improvement of the OREO properties may be capitalized, while holding period costs and any subsequent changes to the valuation allowance are charged to expense as incurred.

Income Taxes

The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity’s financial statements or tax returns. Judgment is required in assessing the future tax consequences of events that have been recognized in the Company’s consolidated financial statements or tax returns. Fluctuations in the actual outcome of these future tax consequences could impact the Company’s consolidated financial condition or results of operations.

The Company records an income tax provision or benefit based on the amount of tax, including alternative minimum tax, currently payable or receivable and the change in deferred tax assets and liabilities. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial and tax reporting purposes. Management conducts quarterly assessments of all available positive and negative evidence to determine the amount of deferred tax assets that will more likely than not be realized. A valuation allowance is established for deferred tax assets and records a charge to income if management determines, based on available evidence at the time the determination is made, that it is more likely than not that some portion or all of the deferred tax assets will not be realized. In evaluating the need for a valuation allowance, management considers past operating results, estimates of future taxable income based on approved business plans, future capital requirements and ongoing tax planning strategies. This evaluation process involves significant management judgment about assumptions that are subject to change from period to period depending on the related circumstances. The recognition of deferred tax assets requires management to make significant assumptions and judgments about future earnings, the periods in which items will impact taxable income, future corporate tax rates, and the application of inherently complex tax laws. The use of different estimates can result in changes in the amounts of deferred tax items recognized, which can result in equity and earnings volatility because such changes are reported in current period earnings. On December 31, 2010,

management established a valuation allowance equal to 100 percent of the Company's net deferred tax asset, excluding deferred tax assets and liabilities related to unrealized holding gains and losses on available-for-sale securities, and has maintained such an allowance through December 31, 2014. As part of its evaluation conducted as of December 31, 2015, management reviewed all the positive and negative evidence available at that time and concluded that significant positive evidence outweighed any negative evidence and the valuation allowance previously established for the Company's deferred tax assets should be reversed, except for the amount established for charitable contribution carryovers.

In connection with determining the income tax provision or benefit, the Company considers maintaining liabilities for uncertain tax positions and tax strategies that management believes contain an element of uncertainty. Periodically, the Company evaluates each of its tax positions and strategies to determine whether a liability for uncertain tax benefits is required. As of December 31, 2015 and 2014, the Company determined that it did not have any uncertain tax positions or tax strategies and that no liability was required to be recorded.

See Note 2-"Summary of Significant Accounting Policies" and Note 13-"Income Taxes" of the notes to consolidated financial statements included in Item 8-"Financial Statements and Supplementary Data" to this Annual Report on Form 10-K for additional information about the reversal of the valuation allowance for deferred tax assets and the accounting for income taxes.

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New Authoritative Accounting Guidance

Accounting Standards Update ("ASU") 2014-04, Receivables-Troubled Debt Restructurings by Creditors (Subtopic 310-40): "Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure," clarifies 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 (a) the creditor obtaining legal title to residential real estate property upon completion of a foreclosure or (b) 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 the amount of foreclosed residential real estate property held by the creditor and 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 adoption of this guidance on January 1, 2015 did not have a material effect on the operating results or financial position of the Company.

ASU 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant and Equipment (Topic 360): "Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity," changes the criteria for reporting a discontinued operation. Under the new guidance, a disposal of a component of an entity or group of components of an entity is required to be reported in discontinued operations if the disposal represents a strategic shift that has (or will have) a major effect on the entity's operations and financial results. This new guidance reduces complexity by removing the complex and extensive implementation guidance and illustrations that are necessary to apply the current definition of a discontinued operation. The new guidance also requires expanded disclosures about discontinued operations that will provide users with more information about the assets, liabilities, revenues and expenses of a discontinued operation and will require pre-tax income attributable to a disposal of a significant part of an organization that does not qualify for discontinued operations reporting, which will provide users with information about the ongoing trends in a reporting organization's results from continuing operations. The adoption of this guidance on January 1, 2015 did not have a material effect on the operating results or financial position of the Company.

ASU 2014-11, Transfers and Servicing (Topic 860): "Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures," changes the accounting for repurchase-to-maturity transactions and repurchase financing arrangements by aligning the accounting for these transactions with the accounting for other typical repurchase agreements. Going forward, these transactions would all be accounted for as secured borrowings. The new guidance eliminates sale accounting for repurchase-to-maturity transactions and supersedes the guidance under which a transfer of a financial assets and a contemporaneous repurchase financing could be accounted for on a combined basis as a forward arrangement, which has resulted in outcomes referred to as off-balance sheet accounting. ASU 2014-11 also requires a new disclosure for transactions economically similar to repurchase agreements in which the transferor retains substantially all of the exposure to the economic return on the transferred financial assets throughout the term of the transaction, and requires expanded disclosure about the nature of the collateral pledged in repurchase agreements and similar transactions accounted for as secured borrowings. The adoption of this guidance on January 1, 2015 did not have a material effect on the operating results or financial position of the Company.

ASU 2014-14, Receivables – Troubled Debt Restructurings by Creditors (Subtopic 310-40): "Classification of Certain Government-Guaranteed Mortgage Loans Upon Foreclosure," requires that a mortgage loan be derecognized 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 adoption of this guidance on January 1, 2015 did not have a material effect on the operating results or financial position of the Company

Accounting Guidance to be Adopted in Future Periods

ASU 2014-09, Revenue from Contracts with Customers (Topic 606): Section A, "Summary and Amendments That Create Revenue from Contracts with Customers (Topic 606) and Other Assets and Deferred Costs-Contract with Customers (Subtopic 340-40);" Section B, "Conforming Amendments to Other Topics and Subtopics in the Codification and Status Tables;" and Section C, "Background Information and Basis for Conclusions," provides a robust framework for addressing revenue recognition issues, upon its effective date, and replaces almost all existing revenue recognition guidance, including industry specific guidance, in current GAAP. The core principle of ASU 2014-09 is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. ASU 2014-09 will also result in enhanced interim and annual disclosures, both qualitative and quantitative, about revenue in order to help financial statement users understand the nature, amount, timing and uncertainty of revenue and related cash flows. ASU 2014-09 is effective in annual reporting periods beginning after December 15, 2016 and the interim periods within that year for public business entities, not-for-profit entities that have issued, or are conduit bond obligors for, securities that are traded, listed or quoted on an exchange or over-the-counter market and employee benefit plans that file or furnish financial statements to the SEC. On August 12, 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): "Deferral of the Effective Date," which defers the adoption of ASU 2014-09 for one year for all entities. Accordingly, the Company will adopt this guidance on January 1, 2018 in accordance with ASU 2015-14, and is currently evaluating the effect this guidance may have on its operating results or financial position.

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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," requires a performance target that affects vesting and that can be achieved after the requisite service period to be treated as a performance condition. To account for such awards, an entity should apply existing guidance as it relates to awards with performance conditions that affect vesting. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent compensation cost attributable to the period(s) for which the requisite service already has been rendered. If the performance target becomes probable of being achieved before the end of the requisite service period, the remaining unrecognized compensation cost should be recognized prospectively over the remaining requisite service periods. The total amount of compensation cost should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest. ASU 2014-12 is effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. The adoption of this guidance on January 1, 2016 is not expected to have a material effect on the operating results or financial position of the Company.

ASU 2014-15, Presentation of Financial Statements – Going Concern (Subtopic 205-40): "Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern," defines management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and provide guidance for related footnote disclosures. ASU 2014-15 requires an entity's management to assess the entity's ability to continue as a going concern by incorporating and expanding upon certain principles that are currently in U.S. auditing standards. Specifically ASU 2014-15: (1) provides a definition of the term substantial doubt; (2) requires an evaluation as to whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date the financial statements are issued (or within one year after the date that the financial statements are available to be issued when applicable); (3) provides principles for considering the mitigating effect of management's plans; (4) requires certain disclosures when substantial doubt is alleviated; and (5) require an express statement and other disclosures when substantial doubt is not alleviated. ASU 2014-15 is effective for annual periods ending after December 15, 2016, and for annual periods and interim periods thereafter. Early application is permitted. The adoption of this guidance on December 31, 2016 is not expected to have a material effect on the operating results or financial position of the Company.

ASU 2015-01, Income Statement – Extraordinary and Unusual Items (Subtopic 225-20): "Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items," will alleviate uncertainty for preparers, auditors and regulators because auditors and regulators will no longer be required to evaluate whether a preparer presented an unusual and/or infrequent item appropriately. Although ASU 2015-01 eliminates the concept of extraordinary items, the presentation and disclosure guidance for items that are unusual in nature or infrequent in occurrence has been retained and has been expanded to include items that are both unusual in nature or infrequent in occurrence. The nature and financial effects of each event or transaction is required to be presented as a separate component of income from continuing operations or, alternatively, in the notes to the financial statements. ASU 2015-01 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption of this guidance is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. The adoption of this guidance on January 1, 2016 is not expected to have a material effect on the operating results or financial position of the Company.

ASU 2015-02, Consolidation (Topic 810): “Amendments to the Consolidation Analysis,” improves targeted areas of the consolidation guidance and reduces the number of consolidation models. The new consolidation standard changes the way reporting enterprises evaluate whether (a) they should consolidate limited partnerships and similar entities, (b) fees paid to a decision maker or service provider are variable interests in a variable interest entity (“VIE”), and (c) variable interests in a VIE held by related parties of the reporting enterprise require the reporting enterprise to consolidate the VIE. It also eliminates the VIE consolidation model based on majority exposure to variability that applied to certain investment companies and similar entities. ASU 2015-02 is effective for public entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. The adoption of this guidance on January 1, 2016 is not expected to have a material effect on the operating results or financial position of the Company.

ASU 2015-03, Interest – Imputation of Interest (Subtopic 835-30): “Simplifying the Presentation of Debt Issuance Costs,” more closely aligns the presentation of debt issuance costs under U.S. GAAP with the presentation under comparable IFRS standards. Under ASU 2015-03, debt issuance costs related to a recognized debt liability will no longer be recorded as a separate asset, but will be presented on the balance sheet as a direct deduction from the debt liability, similar to the presentation of debt discounts. The costs will continue to be amortized to interest expense using the effective interest method. ASU 2015-03 is effective for public entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015, and requires retrospective application to all prior periods presented in the financial statements. Early adoption of this guidance is permitted. The adoption of this guidance on January 1, 2016 is not expected to have a material effect on the operating results or financial position of the Company.

ASU 2015-05, Intangibles – Goodwill and Other Internal-Use Software (Subtopic 350-40): “Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement,” provides explicit guidance on a customer’s accounting for fees paid in a cloud computing environment. Specifically, the amendments in this ASU 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. ASU 2015-05 is effective for public entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption of this guidance is permitted. The adoption of this guidance on January 1, 2016 is not expected to have a material effect on the operating results or financial position of the Company.

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ASU 2016-01, Financial Instruments – Overall (Subtopic 825-10): "Recognition and Measurement of Financial Assets and Financial Liabilities" requires all equity investments to be measured at fair value with changes in the fair value recognized through net income (other than those accounted for under equity method of accounting or those that result in consolidation of the investee). The amendments in this Update also require 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. In addition, this ASU eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities and the requirement 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 for public business entities. ASU 2016-01 is effective for fiscal years beginning after December 15, 2017 for public entities. The adoption of this guidance on January 1, 2018 is not expected to have a material effect on the operating results or financial position of the Company.

ASU 2016-02, Leases (Topic 842): "Leases" will require organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases with lease terms of more than 12 months. Consistent with current GAAP, the recognition, measurement and presentation of expenses and cash flows arising from a lease by the lessee will primarily depend on its classification as a finance or operating lease. However, unlike current GAAP, which requires only capital leases to be recognized on the balance sheet, the new ASU will require both types of leases to be recognized on the balance sheet. ASU 2016-02 will also require disclosures to help investors and other financial statement users better understand the amount, timing and uncertainty of cash flows arising from leases. The new disclosures will include both qualitative and quantitative requirements that provide additional information about the amounts recorded in the financial statements. ASU 2016-02 is effective with fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018 for public entities. Accordingly, the Company will adopt this guidance on January 1, 2019, and is currently evaluating the effect this guidance may have on its operating results or financial position.

EXECUTIVE OVERVIEW

The following overview should be read in conjunction with this Management's Discussion and Analysis in its entirety.

Results of Operations

The year ended December 31, 2015 was a successful and pivotal year for the Company from not only a profitability standpoint, but a regulatory, strategic and operational standpoint as well. The Company reported record earnings in 2015 of $35.8 million, or $2.17 per diluted common share, an increase of $22.4 million, or 167.1%, compared to $13.4 million, or $0.81 per diluted common share, in 2014. The strong earnings performance was impacted by the

reversal of the deferred tax asset ("DTA") valuation allowance. The Company's earnings performance in 2015 was also impacted by a $5.1 million, or 15.2%, reduction in non-interest expense, a $0.9 million, or 3.3%, increase in net interest income, a $7.1 million, or 47.7%, decrease in non-interest income and a $4.5 million, or 77.1%, decrease in the credit for loan and lease losses. Return on average assets and return on average shareholders' equity equaled 3.57% and 63.24%, respectively, in 2015, compared to 1.38% and 29.50%, respectively, in 2014. For the three months ended December 31, 2015, return on average assets and return on average shareholders' equity were 10.99% and 192.68%, respectively, compared to (0.01)% and (0.24)%, respectively, for the same three months of 2014. The Company did not pay any dividends during the years ended December 31, 2015 and 2014.

Release of Regulatory Enforcement Actions and Improved Risk Profile

On September 8, 2015, the Company was notified by the Federal Reserve Bank of Philadelphia (the "Reserve Bank") that effective September 2, 2015 it was released from the Written Agreement it had been under with the Reserve Bank since November 24, 2010. Previously, on March 25, 2015, the OCC notified First National Community Bank, the Company's wholly-owned subsidiary (the "Bank"), that it was fully and completely released from the Consent Order it entered into with the OCC in September 2010. These releases signify that the Reserve Bank and OCC have determined that the Company and the Bank have met all of the requirements mandated by the Written Agreement and Consent Order.

The release of regulatory enforcement actions, coupled with an improved risk profile, directly resulted in reductions in certain noninterest expenses, specifically regulatory assessments and insurance expense which had been elevated due to operating under the Consent Order and Written Agreement. Regulatory assessments, which include FDIC insurance and OCC assessments, decreased $0.9 million, or 47.3%, while insurance expense decreased $0.3 million, or 30.7%, comparing 2015 and 2014.

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In addition, while operating under the Consent Order, the Company was prohibited from using brokered deposits as a source of liquidity. After the release from the Consent Order, the Company began utilizing this lower-costing funding alternative in the second quarter of 2015.

Management's Focus in 2015

In 2015, management developed strategies and initiatives focused on maximizing profitability and taxable income generation in order to facilitate the reversal of the DTA valuation allowance, and improving customer service and creating efficiencies through the conversion of the Bank's core operating system. These initiatives, which are discussed in further detail in this MD&A, involved, but are not limited to, the following:

The continued repositioning of the investment portfolio in 2015 by selling almost all of the Company's remaining tax-exempt obligations of states and political subdivisions and replacing them with taxable obligations of U.S. government and government-sponsored agencies including, collateralized mortgage obligations, residential mortgage-backed securities and single-maturity bonds in order to maximize the generation of taxable interest income. In addition, the Company was able to benefit from movements in Treasury yields and record a net gain on the sale of investment securities of $2.3 million.

Accelerating a partial prepayment of and modifying the annual interest on the Company's fixed-rate subordinated debentures due September 1, 2019 ("Notes"). On June 30, 2015, the Company repaid $11.0 million, or 44.0%, of outstanding principal of the Notes, and, effective July 1, 2015, modified the annual interest rate paid on the Notes to 4.50% from 9.00%. The prepayment and rate modification resulted in a $0.8 million, or 36.4%, reduction in interest expense related to the Notes comparing 2015 and 2014. In addition to the modification, the Company reinstituted and paid the quarterly interest payments due September 1, 2015 and December 1, 2015 to the Noteholders which included interest accrued for the period June 1, 2015 through August 31, 2015 and September 1, 2015 through November 30, 2015, respectively. While under the Written Agreement, the Company had been deferring the quarterly interest payment on the Notes beginning December 1, 2010, which continued through May 31, 2015. Deferred interest on the Notes that remained outstanding at December 31, 2015 totaled $10.8 million.

Continuing to effectively manage funding costs through the strategic use of lower-costing borrowings through the FHLB and the reinstitution of brokered certificates of deposits to replace maturing, higher-costing certificates of deposit generated through a national deposit listing service. This transitioning was the primary factor leading to a $0.5 million decrease in interest expense on deposits and an 8 basis point reduction in the Company's cost of funds associated with those deposits.

Converting the Bank's core operating system to a state-of-the-art, highly-flexible, real-time operating platform. On November 17, 2015, the Company completed the conversion of its operating system. The Company outsources its data processing through a third party service provider. The Company did capitalize software implementation costs

associated with the conversion and anticipates a minor increase in data processing costs for 2016. The Company expects to realize efficiencies through process improvements, decrease in paper costs and possible reduction in FTEs through attrition.

Balance Sheet Profile

Total assets increased $0.1 billion, or 12.4%, to $1.1 billion at December 31, 2015 from $1.0 billion at December 31, 2014. Net loans grew $66.2 million, or 10.0%, which reflected strong demand for both commercial and consumer loan products. In addition, available-for-sale securities increased $34.8 million, or 15.9%. The balance sheet increase also reflected the change in the DTA valuation allowance in the amount of $30.0 million. Total deposits increased $26.2 million, or 3.3%, to $821.5 million at December 31, 2015 from $795.3 million at the end of 2014. Specifically, non-interest-bearing demand deposits increased $30.5 million, or 24.6%, while interest-bearing deposits decreased $4.3 million, or 0.6%. The increase in non-interest bearing demand deposits primarily reflected the positive balance fluctuations of several large commercial customer relationships. The decrease in interest-bearing deposits was largely related to lower deposit balances of the Company’s municipal customers due to a state budget impasse, and the planned runoff of higher-costing certificates of deposit generated through a national deposits listing service. These decreases were partially offset by the attainment of a large commercial deposit relationship. Due to their lower cost, the Company increased its utilization of FHLB borrowings as an alternative funding source of liquidity by $74.6 million or 121.9%. This was the primary factor leading to a $63.6 million, or 65.9%, increase in total borrowed funds. Partially offsetting the increase in FHLB advances was the $11.0 million principal prepayment of the Company’s subordinated debentures.

Impacted by the DTA valuation allowance reversal, total shareholders’ equity improved $34.8 million, or 67.7%, to $86.2 million at December 31, 2015 from $51.4 million at the end of 2014. Net income for 2015 of $35.8 million, which included an income tax benefit of $27.8 million related to the reversal of the DTA valuation allowance, was the primary factor leading to the Company’s improved capital position.

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At December 31, 2015, the Company's total risk-based capital ratio and the Tier 1 leverage ratio were 11.75% and 7.27%, respectively. The respective ratios for the Bank at December 31, 2015 were 13.79% and 9.79%. The ratios for both the Company and the Bank exceeded the 10.00% and 5.00% required to be well capitalized under the prompt corrective action provisions of the Basel III capital framework for U.S. Banking organizations, which became effective for the Company and the Bank on January 1, 2015.

Looking Ahead to 2016

For 2016, management plans to utilize the Company's improved capital position to reduce its leverage and enhance shareholder value. On January 29, 2016, the Company announced that the board of directors authorized the payment on March 1, 2016 of all interest that the Company had previously been deferring on the Notes. The aggregate payments totaling $10.8 million represent interest accrued and deferred on the Notes from September 1, 2010 through May 31, 2015.

Also on January 29, 2016, the Company announced that the board of directors had declared a first quarter dividend of $0.02 per share on its common stock, payable March 15, 2016 to shareholders of record March 1, 2016. The dividend represents a 1.53% annualized yield based on the the closing stock price of the Company's common stock on December 31, 2015.

In addition, the Company is focused on developing strategies aimed at building on accomplishments achieved in 2015 to improve long-term financial performance, creating process efficiencies post core conversion, and increasing the level of core deposits through collaboration between the Company's retail and commercial banking units and instituting a governmental banking unit in 2016.

Summary of Performance

Net Interest Income

2015 compared to 2014

Net interest income is the difference between (i) interest income, interest and fees on interest-earning assets, and (ii) interest expense, interest paid on the Company's deposits and borrowed funds. Net interest income represents the largest component of the Company's operating income and, as such, is the primary determinant of profitability. Net interest income is impacted by variations in the volume, rate and composition of earning assets and interest-bearing liabilities, changes in general market rates and the level of non-performing assets. Interest income is shown on a fully tax-equivalent basis and is calculated by adjusting tax-free interest using a marginal tax rate of 34.0% in order to equate the yield to that of taxable interest rates.

Tax-equivalent net interest income in 2015 was $28.1 million, a decrease of $0.1 million from $28.2 million in 2014. Tax-equivalent interest income decreased $1.4 million, which was almost entirely offset by a $1.3 million reduction in interest expense.Tax-equivalent interest income was negatively impacted by a continued decline in loan yields and the sell off of tax-free securities and reinvestment into taxable securities, partially offset by higher loan volumes. The decrease in interest expense largely reflected the 44.0% partial prepayment and the modification of the interest rate of the Company's Notes, which had a positive effect on funding costs. In addition, the Company's cost of funds was also favorably impacted by reinstituting the use of lower-costing brokered deposits, including CDARs, as a source of funding.

The Company's tax-equivalent interest margin compressed 9 basis points to 2.99% in 2015 from 3.08% in 2014. Tax-equivalent net interest margin, a key measurement used in the banking industry to measure income from earning assets relative to the cost to fund those assets, is calculated by dividing tax-equivalent net interest income by average interest-earning assets. Rate spread, the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities shown on a fully tax-equivalent basis, was 2.89% for the year ended December 31, 2015, a decrease of 6 basis points compared to 2.95% for the year ended December 31, 2014.

Tax-equivalent interest income was decreased $1.4 million, or 4.0%, to $32.9 million in 2015 from $34.3 million in 2014. Tax-equivalent interest income was significantly impacted by the repositioning of the investment portfolio from tax-exempt obligations of state and political subdivisions to taxable investments. As a result, the average balance of tax-exempt investments decreased $37.9 million, or 94.0%, to $2.4 million in 2015 from $40.3 million in 2014, which caused a $2.6 million corresponding decrease to tax-equivalent interest income. The average balance of taxable investments increased $45.1 million, or 25.0%, but was only able to mitigate the decrease by $1.1 million. The tax-equivalent yield on the investment portfolio decreased 71 basis points from 3.15% in 2014 to 2.44% in 2015. However, a 12 basis point increase in the yield on taxable investment securities more than offset the effects of a 25 basis point decrease in the yield on tax-exempt investment securities. Overall, changes in the volumes and rates on the investment portfolio resulted in a $1.4 million decrease in tax-equivalent interest income in 2015.

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With regard to the loan portfolio, the Company experienced strong loan demand in 2015, which resulted in a $30.3 million, or 4.5%, increase in average total loans to $696.6 million in 2015 compared to $666.3 million in 2014. The average loan growth resulted in additional tax-equivalent interest income of $1.2 million. However, this additional interest income was entirely offset by a 17 basis point decline in the tax-equivalent yield on the loan portfolio to 3.93% in 2015 compared to 4.10% in 2014, which caused a corresponding decrease in tax-equivalent interest income of $1.2 million. The decrease in loan yields reflected competitive pressures for commercial loans within the Company's market area and current promotions involving short-term residential mortgage products and indirect auto loans.

Almost entirely offsetting the decrease in tax-equivalent interest income was a $1.3 million, or 21.9%, decrease in interest expense to $4.8 million in 2015 from $6.1 million in 2014. The decrease in interest expense was driven primarily by a 19 basis point decrease in the Company's cost of funds to 0.61% in 2015 compared to 0.80% in 2014, which resulted in a $1.4 million corresponding decrease in interest expense due to change in rates. Specifically, the modification of the interest rate on the subordinated debentures from 9.0% to 4.5% had the greatest impact on interest expense, as it was the leading factor driving a 116 basis point decrease in the cost of borrowed funds to 2.01% in 2015 from 3.17% in 2014. The decrease in borrowing costs resulted in a $1.2 million reduction in interest expense. In addition, the Company's cost of deposits decreased 8 basis points to 0.39% in 2015 from 0.47% in 2014, which resulted from decreases in the cost of time deposits greater than $100,000 and other time, paritially offset by an increase in the average rate paid for interest-bearing demand deposits. Changes in the average deposit rates resulted in a $0.2 million decrease in interest expense.

Average interest-bearing liabilities increased $11.0 million, or 1.4%, to $782.5 million in 2015 from $771.5 million in 2014. Specifically, a $14.3 million, or 15.2%, increase in average borrowed funds, resulted in additional interest expense of $0.4 million. The additional interest from borrowed funds was almost entirely offset by a $0.3 million reduction in interest expenses resulting from a $3.2 million decrease in average interest-bearing deposits. One of the Company's ALCO initiatives in 2015 included the replacement of higher-costing certificates of deposit originated through a national deposit listing service and maturing certificates of deposit bearing higher interest rates with lower-costing brokered deposits and FHLB of Pittsburgh advances.

2014 compared to 2013

Comparing the years ended December 31, 2014 and 2013, tax-equivalent net interest income was stable, decreasing only $26 thousand, or 0.09%. The Company's tax-equivalent net interest margin contracted 13 basis points to 3.08% in 2014 from 3.21% in 2013,while the rate spread decreased 13 basis points to 2.95% in 2014 compared to 3.08% in 2013. The Company's net interest margin and rate spread were impacted by several strategic tax planning and ALCO initiatives in 2014, as well as an ongoing challenging rate environment and competitive pressures that continued to impact loan pricing.

In 2014, management continued tax planning strategies designed to generate taxable income and reduce the amount of credit and concentration risk within the investment portfolio. Accordingly, management continued repositioning the investment portfolio by selling the majority of the Company's tax-exempt obligations of state and political subdivisions and replacing them with taxable obligations of U.S. government and government-sponsored agencies including collateralized mortgage obligations ("CMOs"), residential mortgage-backed securities and single-maturity bonds. The effect of this repositioning was the primary factor leading to a $534 thousand, or 7.1%, decrease in tax-equivalent interest income genereated from the investment portfolio.

Despite increased demand for the Company's loan products, competition within its market area for loans escalated, which along with the already challenging rate environment, forced loan yields down. In addition, one of the Company's niche markets is indirect auto lending. Demand for these loans increased in 2014 due to several promotions directed at the Company's automobile dealer customers. However, rates offered on consumer automobile loans are generally lower than those offered on other types of loan products offered to commercial customers.

Tax-equivalent interest income decreased $1.1 million, or 3.0%, to $34.3 million in 2014 from $35.4 million in 2013. The repositioning of the investment portfolio accounted for $534 thousand, or 50.6%, of the overall decrease in tax-equivalent interest income. In addition, the tax-equivalent yield on the loan portfolio decreased 27 basis points from 4.37% in 2013 to 4.10% in 2014, which resulted in a corresponding decrease in tax-equivalent interest income of $1.8 million. Specifically, the yield on taxable loans decreased 27 basis points, while the yield on tax-exempt loans fell 37 basis points, and accounted for corresponding decreases in interest income of $1.6 million and $147 thousand, respectively. Partially offsetting this decrease due to loan yields was a $29.9 million, or 4.7%, increase in average total loans to $666.3 million in 2014 from $636.5 million in 2013. The growth in average loans resulted in an increase in tax-equivalent interest income of $1.3 million.

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However, the effects of the securities portfolio repositioning and declining loan yields was almost entirely mitigated by a $1.0 million, or 14.3%, reduction in interest expense, which resulted primarily from the planned replacement of maturing certificates of deposit with lower-costing advances from the FHLB. Overall, the Company's cost of funds decreased 14 basis points to 0.80% in 2014 from 0.94% in 2013. The decrease in funding costs resulted in a $1.8 million decrease in interest expense. Partially offsetting the reduction in interest expense due to changes in rates was a $5.8 million, or 0.8%, increase in average interest-bearing liabilities to $771.5 million in 2014 from $765.7 million in 2013.

Total average time deposits decreased $49.0 million, or 15.4%. Of the total decrease in average time deposits, $25.1 million, or 51.2%, resulted from a decrease in average time deposits generated through QwickRate®, a national deposit listing service. In addition, the cost of time deposits decreased 12 basis points to 0.99% in 2014 from 1.11% in 2013, as these rate-sensitive deposits continued to runoff at maturing rates that were higher than current rates. The decrease in volume and cost of time deposits resulted in a combined decrease in interest expense of $0.8 million. Average borrowed funds increased $33.5 million, or 55.5%, to $93.7 million in 2014 from $60.2 million in 2013. The increase in borrowed funds was entirely attributable to an increase in advances through the FHLB of Pittsburgh and resulted in additional interest expense of $1.3 million. However, this was more than entirely offset by a 183 basis point reduction in the cost of borrowed funds, which resulted in a corresponding decrease in interest expense of $1.3 million. Changes in the volumes and rates paid for borrowed funds resulted in a combined net decrease in interest expense of $45 thousand.

Interest-bearing demand deposits and savings deposits averaged $18.5 million and $2.8 million higher in 2014 as compared to 2013, respectively, while the cost of interest-bearing demand deposits and savings accounts each decreased 4 basis points. The changes in volumes and rates for interest-bearing demand deposits and savings accounts netted a combined decrease in interest expense of $139 thousand.

Non-accrual loans

The interest income that would have been earned on non-accrual and restructured loans outstanding at December 31, 2015, 2014 and 2013 in accordance with their original terms approximated $406 thousand, $406 thousand and $572 thousand, respectively. Interest income on impaired loans of $258 thousand, $235 thousand, and $366 thousand was recognized based on payments received in 2015, 2014 and 2013.

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The following table reflects the components of net interest income for each of the three years ended December 31, 2015, 2014 and 2013:

Summary of Net Interest Income

(dollars in thousands)	Year ended December 31, 2015			Year ended December 31, 2014			Year ended December 31, 2013		
	Average Balance	Interest	Yield/ Cost	Average Balance	Interest	Yield/ Cost	Average Balance	Interest	Yield/ Cost
ASSETS									
Earning assets (2)(3)									
Loans-taxable (4)	$654,470	$25,360	3.87 %	$625,969	$25,316	4.04 %	$597,776	$25,744	4.31 %
Loans-tax free (4)	42,135	1,988	4.72 %	40,370	1,989	4.93 %	38,694	2,050	5.30 %
Total loans (1)(2)	696,605	27,348	3.93 %	666,339	27,305	4.10 %	636,470	27,794	4.37 %
Securities-taxable	224,955	5,374	2.39 %	179,903	4,090	2.27 %	131,478	2,406	1.83 %
Securities-tax free	2,419	165	6.82 %	40,277	2,853	7.08 %	70,938	5,071	7.15 %
Total securities (1)(5)	227,374	5,539	2.44 %	220,180	6,943	3.15 %	202,416	7,477	3.69 %
Interest-bearing deposits in other banks	18,076	46	0.25 %	28,729	71	0.25 %	40,067	103	0.26 %
Total earning assets	942,055	32,933	3.50 %	915,248	34,319	3.75 %	878,953	35,374	4.02 %
Non-earning assets	73,587			73,713			89,749		
Allowance for loan and lease losses	(10,729)			(13,094)			(18,613)		
Total assets	$1,004,913			$975,867			$950,089		
LIABILITIES AND SHAREHOLDERS' EQUITY									
Interest-bearing liabilities									
Interest-bearing demand deposits	$358,442	$672	0.19 %	$320,780	$453	0.14 %	$302,258	$559	0.18 %
Savings deposits	91,603	60	0.07 %	88,678	57	0.06 %	85,872	90	0.10 %
Time deposits over $100,000	97,687	679	0.70 %	135,871	1,048	0.77 %	160,728	1,301	0.81 %
Other time deposits	126,851	1,220	0.96 %	132,489	1,622	1.22 %	156,639	2,214	1.41 %
Total interest-bearing deposits	674,583	2,631	0.39 %	677,818	3,180	0.47 %	705,497	4,164	0.59 %
Borrowed funds and other interest-bearing liabilities	107,965	2,170	2.01 %	93,694	2,967	3.17 %	60,240	3,012	5.00 %

Total interest-bearing liabilities	782,548	4,801	0.61 %	771,512	6,147	0.80 %	765,737	7,176	0.94 %
Demand deposits	139,945			134,132			130,186		
Other liabilities	25,744			24,724			19,946		
Shareholders' equity	56,676			45,499			34,220		
Total liabilities and shareholders' equity	$1,004,913			$975,867			950,089		
Net interest income/interest rate apread (6)		28,132	2.89 %		28,172	2.95 %		28,198	3.08 %
Tax equivalent adjustment		(732)			(1,646)			(2,421)	
Net interest income as reported		$27,400			$26,526			$25,777	
Net interest margin (7)			2.99 %			3.08 %			3.21 %

(1) Interest income is presented on a tax-equivalent basis using a 34% rate.
(2) Loans are stated net of unearned income.
(3) Non-accrual loans are included in loans within earning assets.
(4) Loan fees included in interest income are not significant.
(5) The yields for securities that are classified as available-for-sale are based on the average historical amortized cost.
(6) Interest rate spread represents the difference between the average yield on interest-earning assets and the cost of average interest-bearing liabilities and is presented on a tax-equivalent basis.
(7) Net interest income as a percentage of total average interest earning assets.

Rate Volume Analysis

The most significant impact on net income between periods is derived from the interaction of changes in the volume and rates earned or paid on interest-earning assets and interest-bearing liabilities. The volume of earning assets, specifically loans and investments, compared to the volume of interest-bearing liabilities represented by deposits and borrowings, combined with the spread, produces the changes in net interest income between periods. Components of interest income and interest expense are presented on a tax-equivalent basis using the statutory federal income tax rate of 34%.

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The following table summarizes the effect that changes in volumes of earning assets and interest-bearing liabilities and the interest rates earned and paid on these assets and liabilities have on net interest income comparing years ended December 31, 2015 and 2014. The net change or mix component attributable to the combined impact of rate and volume changes has been allocated proportionately to the change due to volume and the change due to rate.

Net Interest Income Changes Due to Rate and Volume

	For the Year Ended December 31, 2015 vs. 2014 Increase (Decrease) due to change in			**For the Year Ended December 31, 2014 vs. 2013 Increase (Decrease) due to change in**		
(in thousands)	**Volume**	**Rate**	**Total**	**Volume**	**Rate**	**Total**
Interest income:						
Loans - taxable	$1,128	$(1,084)	$44	$1,182	$(1,610)	$(428)
Loans - tax free	85	(86)	(1)	86	(147)	(61)
Total loans	1,213	(1,170)	43	1,268	(1,757)	(489)
Securities - taxable	1,067	217	1,284	1,016	668	1,684
Securities - tax free	(2,586)	(102)	(2,688)	(2,211)	(7)	(2,218)
Total securities	(1,519)	115	(1,404)	(1,195)	661	(534)
Interest-bearing deposits in other banks	(27)	2	(25)	(30)	(2)	(32)
Total interest income	(333)	(1,053)	(1,386)	43	(1,098)	(1,055)
Interest expense:						
Interest-bearing demand deposits	58	161	219	33	(139)	(106)
Savings deposits	2	1	3	3	(36)	(33)
Time deposits over $100,000	(316)	(53)	(369)	(208)	(45)	(253)
Other time deposits	(67)	(335)	(402)	(366)	(226)	(592)
Total interest-bearing deposits	(323)	(226)	(549)	(538)	(446)	(984)
Borrowed funds and other interest-bearing liabilities	403	(1,200)	(797)	1,303	(1,348)	(45)
Total interest expense	80	(1,426)	(1,346)	765	(1,794)	(1,029)
Net Interest Income	$(413)	$373	$(40)	$(722)	$696	$(26)

Provision for Loan and Lease Losses

Management closely monitors the loan portfolio and the adequacy of the ALLL considering underlying borrower financial performance and collateral values and associated credit risks. Future material adjustments may be necessary to the provision for loan and lease losses and the ALLL if economic conditions or loan performance differ

substantially from the assumptions management used in making its evaluation of the ALLL. The provision for loan and lease losses is an expense charged against net interest income to provide for probable losses attributable to uncollectible loans and is based on management's analysis of the adequacy of the ALLL. A credit to loan and lease losses reflects the reversal of amounts previously charged to the ALLL.

2015 compared to 2014

For the year ended December 31, 2015, the Company recorded a credit for loan and lease losses of $1.3 million compared to a credit for loan and lease losses of $5.9 million for the year ended December 31, 2014. The credit for loan and lease losses in 2015 was due largely to improvement in the Company's historical loss and certain qualitative factors and levels of classified loans. The balance of loans classified as "Substandard" decreased $8.9 million, or 34.7%, to $16.8 million at December 31, 2015 from $25.7 million at the end of 2014.

Management closely monitors the loan portfolio, nonperforming loans and the adequacy of the ALLL considering underlying borrower financial performance and collateral values and increasing credit risks.

2014 compared to 2013

The Company recorded a credit for loan and lease losses of $5.9 million in 2014, compared to a credit of $6.3 million in 2013.

During 2014, the Bank received a substantial legal settlement in the amount of $5.8 million resulting from judgments filed by the Bank pursuant to a large credit relationship. Of the total amount received, $3.6 million represented full recovery of previously charged-off loans, which was the primary factor leading to the credit for loan and lease losses. The remainder of the settlement represented satisfaction of all past due interest and late charges and reimbursement of all legal fees and other related expenses associated with these credits distributed as follow: 1) $1.8 million included in non-interest income for amounts recovered that were incurred in prior years; and 2) $0.4 million included as a credit to non-interest expense for amounts recovered that were incurred and paid in 2014.

In addition to this settlement, the Company's asset quality metrics improved, which also factored into the release of reserves in 2014. Non-performing loans decreased $0.9 million, or 13.4%, to $5.5 million at December 31, 2014 from $6.4 million at December 31, 2013. The Company recorded net recoveries of $3.4 million for the year ended December 31, 2014, compared to $1.7 million for the same period of 2013.

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Non-Interest Income:

The following table lists the components of non-interest income for the years ended December 31, 2015, 2014 and 2013:

Components of Non-Interest Income

	Year Ended December 31,		
(in thousands)	**2015**	**2014**	**2013**
Deposit service charges	$2,960	$2,975	$2,945
Net gain on the sale of securities	2,296	6,640	2,887
Net gain on the sale of loans held for sale	292	292	362
Net loss on the sale of classified loans	-	-	(223)
Net loss on the sale of education loans	-	(13)	-
Net gain on the sale of other real estate owned	162	209	135
Gain on the sale of bank premises and equipment and other assets	-	-	579
Gain on branch divestitures	-	607	-
Loan-related fees	442	440	423
Income from bank-owned life insurance	564	650	706
Legal settlements	184	2,127	288
Other	900	993	1,181
Total non-interest income	$7,800	$14,920	$9,283

2015 compared to 2014

For the year ended December 31, 2015, non-interest income decreased $7.1 million, or 47.7%, to $7.8 million compared to $14.9 million for the same period of 2014. Non-interest income levels in 2015 were impacted by a reduction in net gains on the sale of securities and non-recurring income in 2014. Year-to-date net gains on the sale of securities totaled $2.3 million in 2015, a decrease of $4.3 million from $6.6 million in 2014. In addition, non-recurring income in 2014 included monies received from the settlement of judgements filed pursuant to a large commercial credit relationship and a net gain recorded on the divestiture of the Company's Monroe County branch offices.

The sale of OREO properties generated net gains of $162 thousand in 2015, a decrease of $47 thousand, or 22.5%, from $209 thousand in 2014. Deposit service charges, loan-related fees and net gains on the sale of loans held for sale all were relatively flat comparing 2015 and 2014. Income from bank-owned life insurance policies and other income

decreased $86 thousand and $93 thousand, respectively, in 2015 as compared to 2014.

2014 compared to 2013

Non-interest income totaled $14.9 million in 2014, an increase of $5.6 million, or 60.7%, from $9.3 million in 2013. The increase was due largely to an increase in net gains on the sale of investment securities, monies received from a legal settlement and a $0.6 million net gain recorded on the divestiture of the Company's Monroe County branch offices. Net gains on the sale of investment securities increased $3.7 million, or 130.0%, to $6.6 million in 2014 from $2.9 million in 2013.

The Company's non-interest income was also impacted by increases in net gains on the sale of OREO properties, deposit service charges and loan related fees, along with decreases in net gains on the sale of mortgage loans held for sale, income from bank-owned life insurance and other income, and a $13 thousand net loss on the sale of the Company's student loan portfolio. In addition, in 2013 the Company sold its administrative facility located in Luzerne County. This property had a net book value of $1.2 million at the time of sale and the Company recorded a gain on the sale of $579 thousand in 2013.

Net gains on the sale of OREO properties in 2014 amounted to $209 thousand, which was an increase of $74 thousand, or 54.8%, compared to a net gain of $135 thousand in 2013. Service charges on deposit accounts increased $30 thousand, or 1.0%, comparing the years ended December 31, 2014 and 2013, which resulted from changes to the Company's service charge structure. Loan-related fees increased $17 thousand, or 4.0%, to $440 thousand in 2014 from $423 thousand in 2013, which was due primarily to additional fees from issuing letters of credit.

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During 2014, the Company held 15- and 20-year mortgages in its portfolio rather than selling these loans on the secondary market as part of its asset/liability management strategy. In addition, the volume of mortgages originated was negatively impacted by new and more stringent regulations, which became effective at the beginning of 2014. Moreover, the volume of mortgage loans refinanced slowed considerably as mortgage rates had remained stable for a considerable time. As a result, net gains recorded on the sale of mortgage loans in 2014 decreased $70 thousand, or 19.3%, to $292 thousand in 2014 from $362 thousand in 2013. Comparing the years ended December 31, 2014 and 2013, income from bank-owned life insurance decreased $56 thousand, or $7.9%, while other income decreased $188 thousand, or 15.9%. A 12.2% decline in revenue generated from wealth management services was the primary factor leading to the decrease in other income.

Non-Interest Expense

The following table lists the major components of non-interest expense for the years ended December 31, 2015, 2014 and 2013:

Components of Non-Interest Expense

	Year Ended December 31,		
(in thousands)	**2015**	**2014**	**2013**
Salaries and employee benefits	$13,810	$13,111	$13,218
Occupancy expense	2,284	2,088	2,215
Equipment expense	1,657	1,471	1,468
Advertising expense	483	470	523
Data processing expense	1,976	2,088	2,066
Regulatory assessments	950	1,801	2,515
Bank shares tax	705	522	800
Expense of other real estate	400	2,569	719
Legal expense	437	1,799	2,488
Professional fees	1,014	1,567	1,674
Insurance expense	659	951	1,179
Loan collection expenses	280	90	482
Legal settlements	777	-	2,500
Other losses	281	2,279	123
Other operating expenses	2,751	2,763	2,978
Total non-interest expense	$28,464	$33,569	$34,948

2015 compared to 2014

Non-interest expense levels were favorably impacted by continued improvement in the Company's risk profile in 2015. Non-interest expense totaled $28.5 million in 2015, a decrease of $5.1 million, or 15.2%, from $33.6 million in 2014. The decrease resulted primarily from reductions in expenses of other real estate owned, regulatory assessments, legal expenses, professional fees, insurance expense and other losses. Partially offsetting these decreases were increases in salaries and employee benefits, occupancy and equipment expense and legal settlements.

Expenses of other real estate owned amounted to $400 thousand in 2015, a decrease of $2.2 million from $2.6 million in 2014. Valuation adjustments to the values of OREO properties decreased $2.0 million comparing 2015 and 2014, which was the primary factor leading to the decrease in OREO-related expenses.

During the second quarter of 2015, the Company was notified by the FDIC that its risk category for FDIC assessments had improved to a risk category I, the lowest risk category from risk category II based upon its most recent regulatory examination. The change in risk categories became effective on February 1, 2015, and as a result the Company's initial base assessment rate for deposit insurance decreased from 0.14 basis points to a range of 0.05 – 0.09 basis points. The change in assessment rate contributed to a decrease in regulatory assessments of $851 thousand, or 47.3%, to $1.0 million in 2015 from $1.8 million in 2014.

Legal expense decreased significantly due to the resolution of longstanding regulatory matters and litigation. Legal expense was $437 thousand in 2015, a decrease of $1.4 million, or 75.7%, from $1.8 million in 2014. Similarly, professional fees in 2015 decreased $553 thousand, or 35.3%, to $1.0 million in 2015 from $1.6 million in 2014, as the Company continues to monitor and decrease its reliance on third-party consultants.

Due to its improved risk profile, in mid-2015, the Company was once again able to renew its professional liability, fidelity bond and errors and omissions insurance policies at lower rates. As a result, insurance expense decreased $292 thousand, or 30.7%, to $0.7 million in 2015 from $1.0 million in 2014.

Other losses sustained by the Company were $281 thousand in 2015, a decrease of $2.0 million compared to $2.3 million. For 2015, other losses predominantly included losses related to debit card transactions and minor losses sustained during the core conversion. Other losses in 2014 included penalties assessed by two regulatory agencies totaling $1.7 million.

Salaries and employee benefits expense increased $699 thousand, or 5.3%, to $13.8 million in 2015 from $13.1 million in 2014. Total salary expense increased $540 thousand, or 5.0%, due to increases in stock-based compensation and employee incentive compensation. At December 31, 2015, the number of full-time equivalent employees was 250 as compared to 237 at December 31, 2014. Payroll taxes and employee benefits increased $158 thousand, or 7.1%, which was due primarily due to increases in state unemployment taxes and costs associated with the establishment of a supplemental executive retirement plan.

On October 1, 2015, the Bank executed a Supplemental Executive Retirement Plan (“SERP”) for a select group of management or highly compensated employees within the meaning of Sections 201(2), 301(a)(3) and 401(a)(1) of The Employee Retirement Income Security Act of 1974. The general provisions of the SERP provide for annual year-end contributions, performance contingent contributions and discretionary contributions. The SERP contributions are unfunded for Federal tax purposes and constitute an unsecured promise by the Bank to pay benefits in the future. Participants in the SERP shall have the status of general unsecured creditors of the Bank. Annual accrued unfunded contributions included in salaries and employee benefits expense totaled $130 thousand in 2015.

The Company has a defined contribution profit sharing plan for employess that includes the provisions under section 401(k) of the Internal Revenue Code (“401(k)”). The 401(k) feature of the plan permits employees to make voluntary salary deferrals, either pre-tax or Roth, up to the dollar limit prescribed by law. The Company may make discretionary matching contributions equal to a uniform percentage of employee salary deferrals. Company discretionary matching contributions are determined each year by management. For 2014, the Company matched 50.0% of employee salary deferrals up to 4.0% for each employee. For 2015, employee salary deferrals of up to 4.0% for each employee were matched 50.0% through June 30, 2015. Effective July 1, 2015, the Company matched 100.0% of employee salary deferrals up to 2.0% for each employee. Company matching contributions to the 401(k) Plan totaled $149 thousand

and $134 thousand in 2015 and 2014, respectively.

Pursuant to the 2015 Employee Stock Grant Plan and the 2014 Employee Stock Grant Plan, the Board of Directors granted 50 shares of the Company’s common stock in both 2015 and 2014, respectively, to each active full and part time employee. There were 13,300 shares at a cost per share of $5.15 granted under the 2015 Stock Grant Plan and 12,850 shares at a cost per share of $6.02 granted under the 2014 Stock Grant Plan. The total costs of these grants were $69 thousand and $77 thousand, respectively, for the years ended December 31, 2015 and 2014, which were included in salaries and employee benefits expense.

Increases in rent expense, real estate taxes and building maintenance costs resulted in a $0.2 million, or 9.3%, increase in occupancy costs, while higher equipment maintenance caused a $0.2 million, or 12.6% increase in equipment expense.

The Company successfully completed a conversion of its core operating system in the fourth quarter of 2015. The Company expects only a minor increase in equipment expense, specifically related to depreciation and maintenance costs, as a result of this conversion.

2014 compared to 2013

The Company experienced a $1.4 million, or 3.9%, decrease in non-interest expense to $33.6 million in 2014 from $34.9 million in 2013. Non-interest expense was primarily impacted by reductions in regulatory assessments, legal expense, loan collection expense, insurance expense, bank shares tax and other operating expenses, partially offset by valuation adjustments to properties held in other real estate owned and other losses, which were primarily related to penalties assessed by certain regulatory agencies. Non-interest expense also benefitted from decreases in salaries and employee benefits and occupancy costs.

During the first quarter of 2014, the Company was notified by the Federal Deposit Insurance Corporation (“FDIC”) that its risk category for FDIC assessments had improved from a risk category III to a risk category II based upon the Company’s most recent regulatory examination. Due to the change in risk categories, the Company’s initial base assessment rate for deposit insurance decreased from 0.23 basis points to 0.14 basis points. The new assessment rate became effective on February 18, 2014. The changes in assessment rates resulted in a $714 thousand, or 28.4%, decrease in regulatory assessments expense included in non-interest expense.

As a result of the resolution of certain long-standing litigation, legal expense declined $689 thousand, or 27.7% to $1.8 million in 2014 from $2.5 million in 2013. Despite the decrease, the Company’s legal expense remains elevated. Decreases in non-performing loans, coupled with reimbursement of certain expenses related to the settlement of judgments filed against parties to a large credit relationship, the Company’s loan collection expenses decreased $392 thousand, or 81.3%. During the second quarter of 2014, the Company’s professional liability, fidelity bond and errors and omissions insurance policies were renewed at lower rates for the upcoming insurance period. As a result, the Company experienced a $228 thousand, or 19.3% decrease in insurance expense comparing 2014 and 2013. Effective January 1, 2014, the Commonwealth of Pennsylvania enacted a reduction in the bank shares tax rate, which resulted in a decrease in bank shares tax expense of $278 thousand, or 34.8%. The $367 thousand, or 11.4%, decrease in other operating expenses resulted primarily from a 41.8% decrease in telecommunication cost associated with enhancements made by the Company to its network.

Expenses associated with other real estate owned increased $1.9 million, or 257.3%, to $2.6 million from $0.7 million for the same period of 2013. The Company recorded valuation adjustments to the cost basis of several OREO properties totaling $2.2 million. The valuation adjustments reflected the continued decline in real estate values for properties located in Monroe County, Pennsylvania. In addition, the Company adjusted the cost basis of four OREO properties to liquidation value, as these properties were approaching the five-year regulatory holding period threshold.

Included in other losses were penalties assessed by regulatory agencies regarding two separate settlements. The Company recorded a penalty in the amount of $175 thousand related to a settlement agreement it reached with the SEC. In addition, the Bank recorded a penalty assessment in the amount of $1.5 million related to a joint settlement agreement it reached with the OCC and FinCEN. These two penalties accounted for approximately 73.5% of other losses recorded in 2014. The remaining amount in other losses in 2014 related to charges incurred on the abandonment of software and losses sustained in several branch robberies, fraudulent debit card transactions and wire transfers.

Salaries and employee benefits expense decreased $107 thousand, or 0.8%, to $13.1 million in 2014 from $13.2 million in 2013. Total salary expense decreased $209 thousand, or 1.9%, due to a decline in the number of full-time equivalent employees, partially offset by increases in stock-based compensation and employee incentive compensation. At December 31, 2014, the number of full-time equivalent employees was 237 as compared to 260 at December 31, 2013. Payroll taxes and employee benefits increased $102 thousand, or 4.9%, which was due primarily to an increase in health care costs.

Under the Company's profit sharing and 401(k) Plan, for 2014 and 2013, the Company matched 50.0% of employee salary deferrals up to 4.0% for each employee. Company matching contributions to the 401(k) Plan totaled $134 thousand and $129 thousand in 2014 and 2013, respectively.

Pursuant to the 2014 Employee Stock Grant Plan and the 2013 Employee Stock Grant Plan, the Board of Directors granted 50 shares of the Company's common stock in both 2014 and 2013, respectively to each active full and part time employee. There were 12,850 shares at a cost per share of $6.02 granted under the 2014 Stock Grant Plan and 14,400 shares at a cost per share of $4.26 granted under the 2013 Stock Grant Plan. The total costs of these grants was $77 thousand and $61 thousand, respectively, for the years ended December 31, 2014 and 2013, which were included in salaries and employee benefits expense.

Occupancy costs decreased $127 thousand, or 5.7%, to $2.1 million in 2014 from $2.2 million in 2013. The decrease in occupancy costs reflected decreases in real estate taxes, utility costs and depreciation, which resulted primarily from the divestitures of the Monroe County branches.

Provision for Income Taxes

The Company recorded an income tax benefit of $27.8 million in 2015, which resulted primarily from the reversal of the valuation allowance for the Company's deferred tax assets. The Company recorded income tax expense of $0.3 million in 2014, which was related entirely to alternative minimum tax. The Company did not record a provision or benefit for income taxes for the year ended December 31, 2013.

Management evaluates the carrying amount of its deferred tax assets on a quarterly basis, or more frequently, if necessary, in accordance with guidance set forth in ASC Topic 740 “Income Taxes,” and applies the criteria in the guidance to determine whether it is more likely than not that some portion, or all, of the deferred tax asset will not be realized within its life cycle, based on the weight of available evidence. If management determines based on available evidence, both positive and negative, that it is more likely than not that some portion or all of the deferred tax asset will not be realized in future periods, a valuation allowance is calculated and recorded. These determinations are inherently subjective and depend upon management’s estimates and judgments used in their evaluation of both positive and negative evidence.

In its evaluation of available evidence, management considered, among other factors, historical financial performance, expectation of future earnings, the ability to carry back losses to recoup taxes previously paid, length of statutory carry forward periods, experience with operating loss and tax credit carry forwards not expiring unused, tax planning strategies and timing of reversals of temporary differences. In assessing the need for a valuation allowance, management carefully weighed both positive and negative evidence currently available. The weight given to the potential effect of positive and negative evidence must be commensurate with the extent to which it can be objectively verified. In particular, additional scrutiny must be given to deferred tax assets of an entity that is in a cumulative loss position in recent years because it is significant negative evidence that is objective and verifiable and therefore difficult to overcome. In line with industry practice, the Company interpreted the term “recent years” to mean the current year and the prior two years based on a rolling twelve quarters and used pre-tax income (loss) adjusted for permanent differences and any non-recurring income, including gains on the sale of securities and a favorable legal settlement in 2014. While the Company generated positive pre-tax book income adjusted for permanent differences in 2014 and 2013, it recorded a pre-tax loss in 2012. In addition, the pre-tax book income in 2014 and 2013 included significant non-recurring or non-taxable income, which when adjusted for, resulted in the Company being in a three-year cumulative loss position at December 31, 2014. Accordingly, based on the analysis of all available positive and negative evidence, management determined that the negative evidence that existed at December 31, 2014 outweighed any positive evidence that existed at that time. Accordingly, management established valuation allowance equal to 100.0% of net deferred tax assets, excluding deferred tax assets or liabilities related to unrealized holding gains and losses on available-for-sale securities.

Management evaluated the carrying amount of the Company’s deferred tax assets at March 31, 2015, June 30, 2015 and September 30, 2015 using pre-tax income (loss) adjusted for permanent differences and non-recurring income on a rolling twelve-quarter basis consistent with its previous evaluations and determined that the Company was in a cumulative three-year loss position at each of the respective quarter ends. Based on each quarterly analysis, management concluded that the negative evidence that existed at each quarter-end outweighed any available positive evidence at those times and determined that the established valuation allowance equal to 100.0% of net deferred tax assets, excluding deferred tax assets or liabilities related to unrealized holding gains and losses on available-for-sale securities, should continue to be maintained.

Management performed an evaluation of the Company’s deferred tax assets at December 31, 2015 and determined that based on its consistent methodology, the Company was now in a cumulative three-year income position, which it considered to be positive evidence. The Company had sustained significant losses in the fourth quarter of 2012, which

at December 31, 2015 were no longer part of this calculation. The negative evidence related to cumulative losses in prior period evaluations no longer existed at December 31, 2015.

In addition, when determining the need for a valuation allowance, management assessed the possible sources of taxable income available under tax law to realize a tax benefit for deductible temporary differences and carryforwards as defined in ASC Topic 740. As part of its assessment, management considered normalization of the Company's core earnings, scheduling the reversal of existing temporary differences at December 31, 2015 and projections of future core earnings based on known facts at December 31, 2015. Management also incorporated into its assessment certain tax planning strategies recently implemented designed to promote the generation of taxable income. These strategies included: 1) the sale of tax-exempt obligations of states and political subdivisions with fair values greater than book values and redeployment of the sales proceeds into taxable investment options; 2) the sale of lower-yielding taxable securities with fair values greater than book values, and the redeployment of the sales proceeds into higher-yielding taxable investment options; and 3) reducing the annual rate paid on the Company's Notes from 9.0% to 4.5% and making an $11.0 million, or 44.0%, principal prepayment on the Notes.

During 2015, positive evidence continued to build and become more apparent by the end of the year. Specifically, the resolution of costly litigation and release from the Consent Order by the OCC on March 25, 2015 and the Written Agreement by the Reserve Bank on September 2, 2015 has led to an improvement in the Company's overall risk profile. The Company was notified by the FDIC that, effective February 1, 2015, its risk category for FDIC insurance improved from Risk Category II to Risk Category I, which resulted in a decrease in the Company's initial base assessment rate for deposit insurance from 0.14 basis points to 0.05 basis points. As a result of these developments, the Company has experienced and anticipates further reductions in its non-interest expense levels, specifically legal expense and regulatory assessments. Furthermore, as a result of the improved risk profile, the Company renewed its professional liability, fidelity bond and errors and omissions insurance policies at lower rates effective July 1, 2015 and accordingly experienced a decrease in insurance expense going forward.

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As part of its assessment, management projected future core earnings for years 2016 through 2040. Years 2016, 2017 and 2018 were based on the Company's annual three-year budget taking into consideration the positive developments and tax planning strategies detailed above. The budget was completed and approved by the Board of Directors in January 2016. For years 2019 through 2040, management used 2018 budgeted core earnings and estimated it to remain flat. Based on these projections the Company is expected to generate normalized core earnings greater that the total deferred tax assets existing at December 31, 2015, which management considered to be positive evidence. In addition, consistent with accounting guidance in ASC 740, management scheduled the reversal of existing temporary differences at December 31, 2015. This analysis supported the reversal of the valuation allowance established for deferred tax assets at December 31, 2015 except for the valuation allowance established for charitable contribution carryforwards. Management does not believe at the current moment that enough positive evidence exists to remove the valuation allowance associated with charitable contribution carryovers. Unlike the expiration period for net operating loss carryforwards (generally 20 years) and AMT Credit carryovers (indefinite), the expiration of an excess charitable contribution carryover occurs after the 5th succeeding tax year for which a charitable contribution is made. Because the Company is in a net deferred tax asset position, without regard to net operating loss carryovers, the reversal of existing temporary timing differences over the next 5 years makes it more likely than not that a portion of the charitable contribution carryovers will not be recognized. Accordingly, management believes a valuation allowance continues to be appropriate strictly in the case of the excess charitable contribution carryover deferred tax asset.

Based on its evaluation of all available positive and negative evidence that existed at December 31, 2015, management concluded the significant positive evidence outweighed any negative evidence and the valuation allowance established for its deferred tax assets should be reversed, except for the amount established for charitable contribution carryovers.

The Company calculates its current and deferred tax provision based on estimates and assumptions that could differ from actual results reflected in income tax returns filed during the subsequent year. Any adjustments required based on filed returns are recorded when identified in the subsequent year.

FINANCIAL CONDITION

Total assets for the Company were $1.1 billion at December 31, 2015, an increase of $120.6 million, or 12.4%, from $970.0 million, at December 31, 2014. The balance sheet growth resulted primarily from a $66.2 million, or 10.1%, increase in loans, net of deferred costs and the allowance for loan and lease losses and a $34.8 million, or 15.9%, increase in available-for-sale securities. The growth in loans and securities were funded by a $26.2 million, or 3.3%, increase in total deposits, coupled with a $74.6 million, or 121.9% increase in advances through the FHLB of Pittsburgh. The Company's balance sheet was also impacted by the reversal of the valuation allowance for its deferred tax assets, which led to a $27.8 million net deferred tax asset.

On June 30, 2015, the Company repaid $11.0 million, or 44.0%, of the principal amount outstanding on the Notes and also amended the original terms of the Notes to reduce the interest rate payable on the Notes from 9.00% to 4.50% effective July 1, 2015. Pursuant to the approved amendment, the remaining $14.0 million in principal on the Notes is to be repaid as follows: (a) 16% of the original principal amount, or $4.0 million, payable on September 1, 2017; (b) 20% of the original principal amount, or $5.0 million, payable on September 1, 2018; and (c) the final 20% of the original principal amount, or $5.0 million, payable on September 1, 2019, the maturity date of the Notes.

The Company's capital position strengthened as evidenced by an increase in total shareholders' equity of $34.8 million, or 67.7% . Net income of $35.8 million, partially offset by a $1.4 million decrease in accumulated other comprehensive income due to depreciation in the fair value of the Company's available-for-sale securities portfolio, accounted for the majority of the capital improvement. Since 2010, in order to comply with the regulatory requirements of the Consent Order and Written Agreement, the Company had suspended paying dividends, and accordingly, did not pay any dividends in 2015 or 2014. As previously mentioned, during 2015 the Company has since been completely released from all formal regulatory actions. On January 29, 2016, the Company declared a $0.02 per share dividend for the first quarter of 2016, payable on March 15, 2016 to shareholders of record on March 1, 2016.

Securities

The Company's investment securities portfolio provides a source of liquidity needed to meet expected loan demand and interest income to increase profitability. Additionally, the Company utilizes the investment securities portfolio to meet pledging requirements to secure public deposits and for other purposes. Management classifies investment securities as either held-to-maturity or available for sale at the time of purchase based on its intent. Held-to-maturity securities are carried at amortized cost, while available-for-sale securities are carried at fair value, with unrealized holding gains and losses reported as a component of shareholders' equity in accumulated other comprehensive income (loss), net of tax. Since the Company sold held-to-maturity securities in 2014 for reasons other than those permitted under GAAP, management did not classify any securities as held-to-maturity in 2014 and 2015. Decisions to purchase or sell investment securities are based upon management's current assessment of long- and short-term economic and financial conditions, including the interest rate environment and asset/liability management and tax planning strategies. Securities with limited marketability and/or restrictions, such as FHLB of Pittsburgh and FRB stocks, are carried at cost. FRB stock is included in other assets.

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At December 31, 2015, the Company's investment portfolio was comprised principally of fixed-rate securities issued by U.S. government or U.S. government-sponsored agencies, which include residential mortgage-backed securities, residential and commercial CMOs and single-maturity bonds and fixed-rate taxable obligations of state and political subdivisions. Except for U.S. government and government-sponsored agencies, there were no securities of any individual issuer that exceeded 10.0% of shareholders' equity as of December 31, 2015.

Because of the predominantly fixed-rate nature of the portfolio, the Company's debt securities are inherently subject to interest rate risk, defined as the risk that an investment's value will change due to a change in interest rates, in the spread between two rates and in the shape of the yield curve. A security's value is usually affected inversely by changes in rates. As previously mentioned, the FOMC raised the federal funds target rate 25 basis points in December 2015. As a result, shorter-term U.S. Treasury rates increased. The 2-year treasury rate was 1.06% at December 31, 2015, an increase of 39 basis points compared to 0.67% at December 31, 2014. However, the yield curve flattened as the 10-year treasury rate decreased 13 basis points to 2.18% at the end of 2015 from 2.31% at the close of 2014. The change in interest rates resulted in an aggregate $1.4 million decrease in the fair value of the Company's available-for-sale securities portfolio. The Company reported a net unrealized holding loss of $238 thousand, net of income taxes of $123 thousand, at December 31, 2015, compared to an unrealized holding gain of $1.1 million, net of income taxes of $0.6 million, at December 31, 2014. The FOMC indicated in its report to Congress in February 2016 that it anticipates that economic conditions will warrant gradual increases in the federal funds rate. Any additional increases in interest rates could result in further depreciation in the fair value of the Company's securities portfolio and capital position.

The following table presents the carrying value of available-for-sale securities, which are carried at fair value, and held-to-maturity securities, which are carried at amortized cost, at December 31, 2015, 2014 and 2013:

Composition of the Investment Portfolio

	December 31,		
(in thousands)	**2015**	**2014**	**2013**
Available-for-sale			
Obligations of U.S. government agencies	$44,043	$29,276	$-
Obligations of state and political subdivisions	75,407	24,509	78,054
U.S. government/government-sponsored agencies:			
Collateralized mortgage obligations - residential	22,269	26,231	3,221
Collateralized mortgage obligations - commercial	89,423	61,256	31,578
Residential mortgage-backed securities	18,098	74,098	89,656
Corporate debt securities	423	420	407
Negotiable certificates of deposit	3,162	2,232	-
Equity securities	948	967	951
Total securities available-for-sale	$253,773	$218,989	$203,867

Held-to-maturity			
Obligations of state and political subdivisions	$-	$-	$2,308

Management actions during 2015 reflected the Company's ongoing investment strategy designed to replace tax-free holdings with taxable securities as required under tax planning initiatives, take advantage of changing market conditions and address the Company's liquidity needs. With regard to tax planning initiatives, the Company currently has $55.6 million in net operating loss ("NOL") carryovers, which it uses to offset any taxable income. In addition, at December 31, 2014 the Company had established a full valuation allowance for its deferred tax assets. Because of this tax position, the Company does not benefit from holding tax-exempt obligations of state and political subdivisions. Accordingly, current tax planning initiatives for 2015 focused on generating sustained taxable income to be able to reduce NOL carryovers and support the reversal of the deferred tax asset valuation allowance.

As part of this strategy in 2015, the Company sold 34 of its available-for-sale securities including 18 tax-exempt and 3 taxable obligations of state and political subdivisions, 9 residential mortgage-backed securities, 3 commercial CMOs and 1 U.S. government agency bond. The securities sold had an aggregate amortized cost of $86.4 million. Gross proceeds received totaled $88.7 million, with net gains of $2.3 million realized upon the sales and included in non-interest income.

During the year ended ended December 31, 2014, the Company sold its entire holdings of held-to-maturity securities comprised of four zero-coupon obligations of state and political subdivisions with an aggregate amortized cost of $2.3 million. Gross proceeds received from the sale of held-to-maturity securities were $2.7 million, with net gains of $0.4 million realized upon the sale. These securities were sold as part of the previoiusly mentioned tax planning initiatives and management's strategy to reduce the amount of potential credit and concentration risk in the investment portfolio. Since the securities were sold for reasons other than those permitted under GAAP, management did not classify securities as held-to-maturity in 2015 and 2014.

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Securities purchased during the year ended December 31, 2015 totaled $133.3 million, including $73.2 million in taxable obligations of state and political subdivisions, $40.7 million in commercial CMOs of U.S. government-sponsored agencies, $17.3 million of single-maturity bonds of U.S. government-sponsored agencies, $1.2 million in residential CMOs of U.S. government-sponsored agencies, and $0.9 million in negotiable certificates of deposit.

The following table presents the maturities of available-for-sale securities, based on carrying value at December 31, 2015, and the weighted average yields of such securities calculated on the basis of the cost and effective yields weighted for the scheduled maturity of each security. The yields on obligations of states and political subdivisions are presented on a tax-equivalent basis using an effective tax rate of 34.0%. Because residential and commercial collateralized mortgage obligations and residential mortgage-backed securities are not due at a single maturity date, they are not included in the maturity categories in the following summary.

Maturity Distribution of the Investment Portfolio

	December 31, 2015						
(dollars in thousands)	Within One Year	> 1 – 5 Years	6-10 Years	Over 10 Years	Collateralized Mortgage Obligations and Mortgage-Backed Securities	No Fixed Maturity	Total
Available-for-sale							
Obligations of U.S. government agencies	$-	$26,574	$17,469	$-	$ -	$ -	$44,043
Yield		1.95 %	2.31 %				2.09 %
Obligations of state and political subdivisions	-	1,513	72,143	1,751	-	-	75,407
Yield		2.30 %	2.80 %	5.95 %			2.86 %
U.S. government/government-sponsored agencies:							
Collateralized mortgage obligations - residential	-	-	-	-	22,269	-	22,269
Yield					2.39 %		2.39 %
Collateralized mortgage obligations - commercial	-	-	-	-	89,423	-	89,423
Yield					2.29 %		2.29 %
	-	-	-	-	18,098	-	18,098

Residential mortgage-backed securities							
Yield					2.81 %		2.81 %
Corporate debt securities	-	-	-	423	-	-	423
Yield				0.95 %			0.95 %
Negotiable certificates of deposit	-	3,162	-	-	-	-	3,162
Yield		2.04 %					2.04 %
Equity securities	-	-	-	-	-	948	948
Yield						3.51 %	3.51 %
Total securities available-for-sale	$-	$31,249	$89,612	$2,174	$ 129,790	$948	$253,773
Weighted yield	0.00 %	1.98 %	2.70 %	4.98 %	2.38 %	3.51 %	2.47 %

OTTI Evaluation

There was no OTTI recognized during the years ended December 31, 2015, 2014 and 2013. For additional information regarding the management's evaluation of securities for OTTI, see Note 4- "Securities" of the notes to consolidated financial statements included in Item 8 – "Financial Statement and Supplementary Data" to this Annual Report on Form 10-K.

Investments in FHLB and Federal Reserve Bank ("FRB") stock, which have limited marketability, are carried at cost and totaled $7.7 million and $4.2 million at December 31, 2015 and 2014, respectively. FRB stock of $1.3 million is included in Other Assets at December 31, 2015 and 2014. Management noted no indicators of impairment for the FHLB of Pittsburgh and FRB of Philadelphia at December 31, 2015.

Loans

Despite unanticipated paydowns on several large commercial lending relationships received in the first quarter of 2015, the Company experienced strong demand for its lending throughout 2015. New loan originations exceeded maturities and payoffs in 2015 and resulted in a $61.7 million, or 9.2%, increase in total loans to $731.2 million at December 31, 2015 from $669.5 million at December 31, 2014. Solid increases were exhibited in both the Company's commercial and retail lending activities.

Historically, commercial lending activities have represented a significant portion of the Company's loan portfolio. Commercial lending includes commercial and industrial loans, commercial real estate loans and construction, land acquisition and development loans, and represented 58.2% and 57.4% of total loans at December 31, 2015 and December 31, 2014, respectively.

From a collateral standpoint, a majority of the Company's loan portfolio consists of loans secured by real estate. Real estate secured loans, which include commercial real estate, construction, land acquisition and development, residential real estate loans and home equity lines of credit ("HELOCs"), increased $28.7 million, or 7.1%, to $433.7 million at December 31, 2015 from $405.0 million at December 31, 2014. Real estate secured loans represented 59.3% of total gross loans at December 31, 2015 and 60.5% at December 31, 2014.

Commercial and industrial loans increased $17.7 million, or 13.5%, during the year to $149.8 million at December 31, 2015 from $132.1 million at December 31, 2014. Commercial and industrial loans consist primarily of equipment loans, working capital financing, automobile floor plans, revolving lines of credit and loans secured by cash and marketable securities. Loans secured by commercial real estate increased $11.7 million, or 5.0%, to $245.2 million at December 31, 2015 from $233.5 million at December 31, 2014. Commercial real estate loans include long-term commercial mortgage financing and are primarily secured by first or second lien mortgages. Construction, land acquisition and development loans increased $12.0 million, or 63.8%, during the year to $30.8 million at December 31, 2015, from $18.8 million at December 31, 2014. The Company continues to monitor its exposure to this higher-risk portfolio segment.

Residential real estate loans totaled $130.7 million at December 31, 2015, an increase of $7.9 million, or 6.4%, from $122.8 million at December 31, 2014. The components of residential real estate loans include fixed-rate and variable-rate mortgage loans. HELOCs are not included in this category but are included in consumer loans. The Company primarily underwrites fixed-rate purchase and refinance of residential mortgage loans for sale in the secondary market to reduce interest rate risk and provide funding for additional loans. In addition, in January 2015, management began a campaign to promote the Company's "WOW" residential mortgage product. This product is a non-saleable mortgage with maturity terms of 7.5, 10 and 14.5 years that offers customers an attractive fixed interest rate, low closing cost and quicker close. As a result of this campaign, the balance outstanding of "WOW" mortgages increased $7.8 million, or 28.8%, to $35.0 million at December 31, 2015 from $27.2 million at December 31, 2014, which accounted for the majority of the growth in residential real estate loans.

Consumer loans totaled $128.5 million at December 31, 2015, an increase of $6.4 million, or 5.3%, from $122.1 million at December 31, 2014, reflecting the growth in the Company's portfolio of indirect automobile loans, which increased $9.4 million, or 10.1%, in 2015.

During 2015, the Company instituted a "Government Banking" sector within its Commercial Banking Unit, which will focus efforts on meeting the banking needs of the municipalities within the Company's market area. Loans to state and municipal governments increased $5.9 million, or 14.6%, to $46.1 million at December 31, 2015 from $40.2 million at December 31, 2014.

The following table summarizes loans receivable, net by category at December 31, 2015, for each of the last five years:

Loan Portfolio Detail

	December 31,				
(in thousands)	**2015**	**2014**	**2013**	**2012**	**2011**
Residential real estate	$130,696	$122,832	$114,925	$90,228	$80,056
Commercial real estate	245,198	233,473	218,524	221,591	256,508
Construction, land acquisition and development	30,843	18,835	24,382	32,502	33,450
Commercial and industrial	149,826	132,057	127,021	109,693	174,233
Consumer	128,533	122,092	118,645	109,783	111,778
State and political subdivisions	46,056	40,205	39,875	33,978	23,496
Total loans, gross	731,152	669,494	643,372	597,775	679,521
Unearned income	(98)	(98)	(143)	(103)	(159)
Net deferred loan costs	2,662	871	668	260	516
Allowance for loan and lease losses	(8,790)	(11,520)	(14,017)	(18,536)	(20,834)
Loans, net	$724,926	$658,747	$629,880	$579,396	$659,044

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The following schedule shows the maturity distribution and interest rate information of the loan portfolio by major classification as of December 31, 2015:

Maturity Distribution of the Loan Portfolio

	December 31, 2015			
(in thousands)	**Within One Year**	**One to Five Years**	**Over Five Years**	**Total**
Residential real estate	$3,033	$6,873	$120,790	$130,696
Commercial real estate	17,094	51,619	176,485	245,198
Construction, land acquisition and development	5,726	6,384	18,733	30,843
Commercial and industrial	84,498	36,393	28,935	149,826
Consumer	8,166	69,290	51,077	128,533
State and political subdivisions	1,200	10,165	34,691	46,056
Total	$119,717	$180,724	$430,711	$731,152
Loans with predetermined interest rates	$20,694	$125,262	$166,061	$312,017
Loans with floating rates	99,023	55,462	264,650	419,135
Total	$119,717	$180,724	$430,711	$731,152

At December 31, 2015, 2014 and 2013, the Bank's loan portfolio was concentrated in loans in the following industries:

Loan Concentrations	**December 31, 2015**		**2014**		**2013**	
(dollars in thousands)	**Amount**	**% of gross loans**	**Amount**	**% of gross loans**	**Amount**	**% of gross loans**
Retail space/shopping centers	$35,292	4.83 %	$33,140	4.95 %	$23,472	3.65 %
Automobile dealers	34,594	4.73 %	24,194	3.61 %	18,467	2.87 %
1-4 family residential investment properties	18,957	2.59 %	12,764	1.91 %	18,839	2.93 %
Colleges and Universities	18,540	2.54 %	16,680	2.49 %	12,671	1.97 %
Office complexes/units	18,487	2.53 %	17,249	2.58 %	17,924	2.79 %
Land subdivision	12,673	1.73 %	15,220	2.27 %	15,974	2.48 %
Physicians	10,677	1.46 %	13,636	2.04 %	13,932	2.17 %

Asset Quality

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at the amount of unpaid principal, net of unearned interest, deferred loan fees and costs, and reduced by the ALLL. The ALLL is established through a provision for loan and lease losses charged to earnings.

The Company has established and consistently applies loan policies and procedures designed to foster sound underwriting and credit monitoring practices. The Company manages credit risk through the efforts of loan officers, the loan review function, and the Loan Quality and the ALLL management committees, as well as oversight from the Board of Directors. The Company continually evaluates its credit risk management practices to ensure it is reacting to problems in the loan portfolio in a timely manner, although, as is the case with any financial institution, a certain degree of credit risk is dependent in part on local and general economic conditions that are beyond the Company’s control.

Under the Company’s risk rating system, loans that are rated pass, special mention, substandard, doubtful, or loss are reviewed regularly as part of the Company’s risk management practices. The Company’s Loan Quality Committee, which consists of key members of senior management, finance and credit administration, meets monthly or more often as necessary to review individual problem credits and workout strategies and provides monthly reports to the Board of Directors.

A loan is considered impaired when it is probable that the Company will be unable to collect all amounts due (including principal and interest) according to the contractual terms of the note and loan agreement. For purposes of the Company's analysis, loans that are modified under a troubled debt restructuring ("TDRs"), loan relationships with an aggregate outstanding balance greater than $100 thousand rated substandard and non-accrual, and loans that are identified as doubtful or loss are considered impaired. Impaired loans are analyzed individually to determine the amount of impairment. The Company utilizes the fair value of collateral method for collateral-dependent loans. A loan is considered to be collateral dependent when repayment of the loan is expected to be provided through the liquidation of the collateral held. For impaired loans that are secured by real estate, external appraisals are obtained annually, or more frequently as warranted, to ascertain a fair value so that the impairment analysis can be updated. Should a current appraisal not be available at the time of impairment analysis, other sources of valuation may be used including, current letters of intent, broker price opinions or executed agreements of sale. For non-collateral-dependent loans, the Company measures impairment based on the present value of expected future cash flows, net of any deferred fees and costs, discounted at the loan's original effective interest rate.

Loans to borrowers that are experiencing financial difficulty that are modified and result in the Company granting concessions to the borrower are classified as TDRs and are considered to be impaired. Such concessions generally involve an extension of a loan's stated maturity date, a reduction of the stated interest rate, payment modifications, capitalization of property taxes with respect to residential mortgage loans or a combination of these modifications. Non-accrual TDRs are returned to accrual status if principal and interest payments, under the modified terms, are brought current, are performing under the modified terms for six consecutive months, and management believes that collection of the remaining interest and principal is probable.

Non-performing loans are monitored on an ongoing basis as part of the Company's loan review process. Additionally, work-out efforts continue and are actively monitored for non-performing loans and OREO through the Loan Quality Committee. A potential loss on a non-performing asset is generally determined by comparing the outstanding loan balance to the fair market value of the pledged collateral, less cost to sell.

Loans are placed on non-accrual when a loan is specifically determined to be impaired or when management believes that the collection of interest or principal is doubtful. This generally occurs when a default of interest or principal has existed for 90 days or more, unless such loan is well secured and in the process of collection, or when management becomes aware of facts or circumstances that the loan would default before 90 days. The Company determines delinquency status based on the number of days since the date of the borrower's last required contractual loan payment. When the interest accrual is discontinued, all unpaid interest income is reversed and charged back against current earnings. Any subsequent cash payments received are applied, first to the outstanding loan amounts, then to the recovery of any charged-off loan amounts, with any excess treated as a recovery of lost interest. A non-accrual loan is returned to accrual status when the loan is current as to principal and interest payments, is performing according to contractual terms for six consecutive months and future payments are reasonably assured.

Management actively manages impaired loans in an effort to reduce loan balances by working with customers to develop strategies to resolve borrower difficulties, through sale or liquidation of collateral, foreclosure, and other appropriate means. Real estate values in the Company’s market area have appeared to stabilize. In addition, employment conditions within the Company’s market area have shown substantial improvement. The unemployment rate for the Scranton/Wilkes-Barre/Hazleton Pennsylvania metropolitan area improved to 5.1% for December 2015 from 6.0% for December 2014. However, continued improvement of these metrics cannot be assured. Any weakening of economic and employment conditions could result in real estate devaluations which could negatively impact asset quality and, accordingly, cause an increase in the provision for loan and lease losses.

Under the fair value of collateral method, the impaired amount of the loan is deemed to be the difference between the loan amount and the fair value of the collateral, less the estimated costs to sell. For the Company’s calculations for real estate secured loans, a factor of 10% is generally utilized to estimate costs to sell, which is based on typical cost factors, such as a 6% broker commission, 1% transfer taxes, and 3% various other miscellaneous costs associated with the sales process. If the valuation indicates that the fair value has deteriorated below the carrying value of the loan, the difference between the fair value and the principal balance is charged off. For impaired loans for which the value of the collateral less costs to sell exceeds the loan value, the impairment is considered to be zero.

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The following schedule reflects non-performing loans including non-performing TDRs, OREO and accruing TDRs as of December 31 for each of the last five years:

Non-performing Loans, OREO and Accruing TDRs

	December 31,				
(dollars in thousands)	**2015**	**2014**	**2013**	**2012**	**2011**
Non-accrual loans, including non-accrual TDRs	$3,788	$5,522	$6,356	$9,652	$19,913
Loans past due 90 days or more and still accruing	-	-	19	57	5
Total non-performing loans	3,788	5,522	6,375	9,709	19,918
Other real estate owned	3,154	2,255	4,246	3,983	6,958
Total non-performing loans and OREO	$6,942	$7,777	$10,621	$13,692	$26,876
Accruing TDRs	$4,982	$5,282	$3,995	$7,517	$5,680
Non-performing loans as a percentage of gross loans	0.52 %	0.82 %	0.99 %	1.62 %	2.93 %

Work-out efforts focused on the effective management and resolution of problem credits and the prompt and aggressive disposition of foreclosed properties lead to continued improvement in the Company’s asset quality in 2015. Total non-performing loans and OREO decreased $0.8 million, or 10.7%, to $6.9 million at December 31, 2015 from $7.8 million at December 31, 2014. The Company’s ratio of non-performing loans to total gross loans improved to 0.52% at December 31, 2015 from 0.82% at December 31, 2014, as management continued to reduce the balance of non-accrual loans. Moreover, the Company’s ratio of non-performing loans and OREO as a percentage of shareholders’ equity decreased to 8.1% at December 31, 2015 from 15.1% at December 31, 2014. Management continues to monitor non-accrual loans, delinquency trends and economic conditions within the Company’s market area on an on-going basis in order to proactively address any potential collection-related issues.

TDRs at December 31, 2015 and 2014 were $5.8 million and $9.0 million, respectively. Accruing and non-accruing TDRs were $5.0 million and $0.8 million, respectively at December 31, 2015 and $5.3 million and $3.7 million, respectively at December 31, 2014. There were 8 loans modified as TDRs during the year ended ended December 31, 2015, with an aggregate post-modification outstanding balance of $1.7 million. New modifications during the year ended December 31, 2015 included 5 residential real estate loans, 1 commercial real estate loan, 1 construction, land acquisition and development loan and 1 commercial and industrial loan. The terms of such modifications included one or a combination of the following: extension of term, capitalization of real estate taxes or principal forbearance.

The average balance of impaired loans was $11.1 million and $9.5 million for the years ended December 31, 2015 and 2014, respectively. The Company recognized $258 thousand and $235 thousand of interest income on impaired loans

for the years ended December 31, 2015 and 2014, respectively.

The following table presents the changes in non-performing loans for the years ended December 31, 2015 and 2014. Loan foreclosures represent recorded investment at time of foreclosure not including the effect of any guarantees:

Changes in Non-performing Loans

(in thousands)	**Year ended December 31, 2015**	**2014**
Balance, January 1	$5,522	$6,375
Loans newly placed on non-accrual	5,636	2,348
Change in loans past due 90 days or more and still accruing	-	(19)
Loan foreclosures	(3,697)	(13)
Loans returned to performing status	(135)	(222)
Loans charged-off	(2,576)	(1,289)
Loan payments received	(962)	(1,658)
Balance, December 31	$3,788	$5,522

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The additional interest income that would have been earned on non-accrual and restructured loans had the loans been performing in accordance with their original terms for both of the years ended December 31, 2015 and 2014 approximated $0.4 million.

The Company had one large commercial real estate loan in the amount of $3.5 million that was a nonperforming TDR at December 31, 2014. The loan is also supported by a guarantee by a U.S. governmental agency. The Company foreclosed upon this property and it was transferred to OREO in 2015 at its fair value less cost to sell of $1.5 million, which is based on a signed sales agreement with an unrelated third party that is scheduled to close prior to the close of the first quarter of 2016. The remaining loan balance of $2.1 million is included in other assets as a receivable due from the U.S. governmental agency.

The majority of the loans placed on non-accrual status were comprised of three commercial relationships totaling $3.1 million. Specifically, one relationship involving a construction, land acquisition and development loan with a recorded investment of $0.7 million was placed on non-accrual in the third quarter of 2015, and based on a current appraisal, written down $0.3 million to $0.4 million. Another commercial relationship involving a commercial real estate loan and a commercial and industrial loan with an aggregate recorded investment of $0.8 million was also placed on non-accrual in the third quarter of 2015. In the second quarter of 2015 one large commercial real estate loan with a recorded investment of $1.7 million was modified as a TDR and placed on non-accrual. As part of its impairment analysis, the Company determined this loan to be collateral-dependent, with the analysis resulting in the loan being partially charged-down in the amount of $0.9 million.

In addition to the non-performing loans identified in the table above, the Bank regularly monitors potential problem loans which consist of substandard and accruing loans. The Company experienced substantial improvement in the volume of these loans which decreased $6.9 million, or 32.4% to $14.4 million at December 31, 2015 from $21.3 million at December 31, 2014.

The following table outlines accruing loan delinquencies and non-accrual loans as a percentage of gross loans at December 31, 2015, 2014 and 2013:

Loan Delinquencies and Non-accrual Loans

			December 31,					
			2015		**2014**		**2013**	
Accruing (in days):								
30	-	59	0.18	%	0.30	%	0.46	%

60 - 89	0.14	%	0.09	%	0.09	%
90+	0.00	%	0.00	%	0.00	%
Non-accrual	0.52	%	0.82	%	0.99	%
Total delinquencies	0.84	%	1.21	%	1.54	%

Total delinquencies, as a percent of gross loans, continued to improve in 2015, as delinquencies for accruing loans decreased $0.2 million to $2.4 million at December 31, 2015 from $2.6 million at December 31, 2014, primarily due to decreases in past due residential real estate and consumer loans. In its evaluation of the ALLL, management considers a variety of qualitative factors including changes in the volume and severity of delinquencies.

While economic conditions improved significantly in the Company’s market area, management continues to recognize some weakness within the local real estate and job markets.. As previously mentioned, the unemployment rate for the Scranton-Wilkes-Barre-Hazleton metropolitan area, the Company’s predominant market area, improved to a seasonally adjusted rate of 5.1% for December 2015 from 6.0% for December 2014. However, unemployment in the Company’s market continues to rank among the highest as compared to Pennsylvania’s 14 metropolitan areas and lags behind the unemployment rate of 4.8% for the entire Commonwealth. The Company tries to mitigate these factors by emphasizing strict underwriting standards.

Allowance for Loan and Lease Losses

The ALLL represents management’s estimate of probable loan losses inherent in the loan portfolio. The ALLL is analyzed in accordance with GAAP and is maintained at a level that is based on management’s evaluation of the adequacy of the ALLL in relation to the risks inherent in the loan portfolio.

As part of its evaluation, management considers qualitative and environmental factors, including, but not limited to:

- Changes in national, local, and business economic conditions and developments, including the condition of various market segments;
- Changes in the nature and volume of the Company’s loan portfolio;

- Changes in the Company's lending policies and procedures, including underwriting standards, collection, charge-off and recovery practices and results;
- Changes in the experience, ability and depth of the Company's management and staff;
- Changes in the quality of the Company's loan review system and the degree of oversight by the Company's Board of Directors;
- Changes in the trend of the volume and severity of past due and classified loans, including trends in the volume of non-accrual loans, TDRs and other loan modifications;
- The existence and effect of any concentrations of credit and changes in the level of such concentrations;
- The effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the Company's current loan portfolio; and
- Analysis of customers' credit quality, including knowledge of their operating environment and financial condition.

Evaluations are intrinsically subjective, as the results are estimated based on management knowledge and experience and are subject to interpretation and modification as information becomes available or as future events occur. Management monitors the loan portfolio on an ongoing basis with emphasis on weakness in both the real estate market and the economy in general and its effect on repayment. Adjustments to the ALLL are made based on management's assessment of the factors noted above.

For purposes of its analysis, all loan relationships with an aggregate balance greater than $100 thousand that are rated substandard and non-accrual, identified as doubtful or loss, and all TDRs are considered impaired and are analyzed individually to determine the amount of impairment. Circumstances such as construction delays, declining real estate values, and the inability of the borrowers to make scheduled payments have resulted in these loan relationships being classified as impaired. The Company utilizes the fair value of collateral method for collateral-dependent loans and TDRs for which repayment depends on the sale of collateral. For non-collateral-dependent loans and TDRs, the Company measures impairment based on the present value of expected future cash flows discounted at the loan's original effective interest rate. With regard to collateral-dependent loans, appraisals are received at least annually to ensure that impairment measurements reflect current market conditions. Should a current appraisal not be available at the time of impairment analysis, other valuation sources including current letters of intent, broker price opinions or executed agreements of sale may be used. Only downward adjustments are made based on these supporting values. Included in all impairment calculations is a cost to sell adjustment of approximately 10%, which is based on typical cost factors, including a 6% broker commission, 1% transfer taxes and 3% various other miscellaneous costs associated with the sales process. Sales costs are periodically revised based on actual experience. The ALLL analysis is adjusted for subsequent events that may arise after the end of the reporting period but before the financial reports are filed.

The Company's ALLL consists of both specific and general components. At December 31, 2015, the ALLL that related to impaired loans that are individually evaluated for impairment, the guidance for which is provided by ASC 310 "*Impairment of a Loan*" ("ASC 310"), was $381 thousand, or 4.3%, of the total ALLL. A general allocation of $8.4 million was calculated for loans analyzed collectively under ASC 450 "*Contingencies*" ("ASC 450"), which represented 95.7% of the total ALLL of $8.8 million. The ratio of the ALLL to total loans at December 31, 2015 and December 31, 2014 was 1.20% and 1.72%, respectively, based on total loans of $731.2 million and $669.5 million, respectively. The decrease in the ALLL as a percentage of total loans reflects asset quality improvements, reductions in historical

loss factors and improvements in qualitative factors.

At December 31, 2015, based on its evaluation of the ALLL, management established an unallocated reserve of $74 thousand. As part of its evaluation, management applies loss rates to each loan segment. The loss rates are based on actual historical loss experience for the respective loan segment. The Company has experienced net recoveries related to its commercial and industrial segment of the loan portfolio for the majority of the quarters in the twelve-quarter lookback period, which resulted in an overall negative historical loss factor for this segment. Management decided to reverse the negative provision created by the negative historical loss factor and establish an unallocated reserve. Management will continue to monitor the unallocated balance for propriety as part of its quarterly evaluation of the ALLL.

The ALLL equaled $8.8 million at December 31, 2015, a decrease of $2.7 million from $11.5 million at December 31, 2014. The Company recorded net charge offs of $1.4 million in 2015. However, due to continued improvement in historical loss ratios, levels of criticized loans and qualitative factors, the Company recorded a credit for loan and lease losses of $1.3 million for the year ended December 31, 2015.

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The following table presents an allocation of the ALLL and percent of loans in each category at December 31, for each of the last five years:

Allocation of the ALLL

	December 31, 2015		**2014**		**2013**		**2012**		**2011**	
(dollars in thousands)	**Allowance**	**Percentage of Loans in** Each Category to Total Loans	**Allowance**	**Percentage of Loans in** Each Category to Total Loans	**Allowance**	**Percentage of Loans in** Each Category to Total Loans	**Allowance**	**Percentage of Loans in** Each Category to Total Loans	**Allowance**	**Percentage of Loans in** Each Category to Total Loans
Residential real estate	$1,333	17.87 %	$1,772	18.35 %	$2,287	17.86 %	$1,764	15.09 %	$1,823	11.78 %
Commercial real estate	3,346	33.54 %	4,663	34.87 %	6,017	33.97 %	8,062	37.07 %	11,151	37.75 %
Construction, land acquisition and development	853	4.22 %	665	2.81 %	924	3.79 %	2,162	5.44 %	2,590	4.92 %
Commercial and industrial	1,205	20.49 %	2,104	19.72 %	2,321	19.74 %	4,167	18.35 %	3,292	25.64 %
Consumer	1,494	17.58 %	1,673	18.24 %	1,789	18.44 %	1,708	18.37 %	1,526	16.45 %
State and political subdivisions	485	6.30 %	598	6.01 %	679	6.20 %	673	5.68 %	452	3.46 %
Unallocated	74	0.00 %	45	0.00 %	-	0.00 %	-	0.00 %	-	0.00 %
Total	$8,790	100.00%	$11,520	100.00%	$14,017	100.00%	$18,536	100.00%	$20,834	100.00%

The following table presents an analysis of the ALLL category for each of the last five years:

Reconciliation of the ALLL

	For the Year Ended December 31,				
(in thousands)	**2015**	**2014**	**2013**	**2012**	**2011**
Balance, January 1,	$11,520	$14,017	$18,536	$20,834	$22,575
Charge-offs:					
Residential real estate	139	204	664	683	1,273
Commercial real estate	912	-	65	3,298	2,395
Construction, land acquisition and development	688	45	179	258	1,857
Commercial and industrial	180	217	341	3,389	416
Consumer	716	922	655	673	739
State and political subdivision	-	-	-	-	-
Total charge-offs	2,635	1,388	1,904	8,301	6,680
Recoveries of charged-off loans:					
Residential real estate	58	90	343	35	57
Commercial real estate	307	362	879	1,035	93
Construction, land acquisition and development	-	3,538	130	265	2,188
Commercial and industrial	400	262	1,853	265	1,852
Consumer	485	508	450	338	226
State and political subdivision	-	-	-	-	-
Total recoveries	1,250	4,760	3,655	1,938	4,416
Net charge-offs (recoveries)	1,385	(3,372)	(1,751)	6,363	2,264
(Credit) provision for loan and lease losses	(1,345)	(5,869)	(6,270)	4,065	523
Balance, December 31	$8,790	$11,520	$14,017	$18,536	$20,834
Ratios:					
Net charge-offs (recoveries) as a percentage of average loans	0.20 %	(0.51)%	(0.28)%	0.97 %	0.31 %
Allowance for loan and lease losses as a percent of gross loans outstanding at period end	1.20 %	1.72 %	2.18 %	3.10 %	3.07 %

Other Real Estate Owned

At December 31, 2015, there were 11 properties with an aggregate carrying value of $3.2 million in OREO, compared to 15 properties with an aggregate balance of $2.3 million at December 31, 2014. During the year ended December 31, 2015, there were four properties with an aggregate carrying value of $1.7 million foreclosed upon. Comprising approximately 91.0% of the carrying value of the foreclosures was one commercial real estate property with a fair value less cost to sell of $1.5 million. The property is currently under a sales agreement, which is scheduled to close by the end of the first quarter of 2016. During the year ended December 31, 2014, the Company foreclosed on one property with a carrying value of $13 thousand.

Included in OREO were three properties previously held in bank premises and equipment that were transferred to OREO due to a change in their intended use. The properties include two commercial lots previously held for future expansion and a former branch office located in Stroudsburg, Pennsylvania. The aggregate carrying value of these properties was $1.4 million and represented 43.7% of OREO at December 31, 2015.

During the year ended December 31, 2015, there were seven sales and one partial sale of properties with an aggregate carrying value of $0.6 million. The Company realized net gains on the sale of these properties of $162 thousand, which is included in non-interest income. There were eight sales and two partial sales of properties with an aggregate carrying value of $1.6 million during the twelve months ended December 31, 2014. The Company realized net gains on the sale of these properties of $209 thousand, which is included in non-interest income for the year ended December 31, 2014.

The Company adjusts for subsequent declines in the fair value of OREO properties through valuation adjustments included in non-interest expense. Valuation adjustments totaled $0.2 million in 2015 and $2.2 million in 2014. The large valuation adjustment in 2014 included writedowns to liquidation value of four properties that were approaching the regulatory 5-year holding period and subsequent writedowns on two properties that were transferred from bank premises and equipment located in Monroe County, Pennsylvania due to continued declines in real estate values in this area.

The Company actively markets OREO properties for sale through a variety of channels including internal marketing and the use of outside brokers/realtors. The carrying value of OREO is generally calculated at an amount not greater than 90% of the most recent fair market appraised value unless specific conditions warrant an exception. A 10% factor is generally used to estimate costs to sell, which is based on typical cost factors, such as 6% broker commission, 1% transfer taxes, and 3% various other miscellaneous costs associated with the sales process. This fair value is updated on an annual basis or more frequently if new valuation information is available. Further deterioration in the real estate market could result in additional losses on these properties.

The following table presents the activity in OREO for each of the three years ended December 31, 2015, 2014 and 2013:

Activity in OREO

(in thousands)	**For the Years Ended December 31,**		
	2015	**2014**	**2013**
Balance, Janauary 1	$2,255	$4,246	$3,983
Property foreclosures	1,717	13	255
Bank premises transferred to OREO	-	1,749	1,819
Valuation adjustments	(208)	(2,200)	(223)
Carrying value of OREO sold	(610)	(1,553)	(1,588)
Balance, December 31	$3,154	$2,255	$4,246

The following table presents a distribution of OREO at December 31 for the past five years:

Distribution of OREO

(in thousands)	**December 31,**				
	2015	**2014**	**2013**	**2012**	**2011**
Land / lots	$785	$1,287	$3,549	$2,711	$4,293
Commercial real estate	2,342	941	647	1,245	1,845
Residential real estate	27	27	50	27	820
Total other real estate owned	$3,154	$2,255	$4,246	$3,983	$6,958

The expenses related to maintaining OREO, including the subsequent write-downs of the properties related to declines in value since foreclosure, net of any income received, amounted to $0.4 million, $2.6 million, and $0.7 million for the years ended December 31, 2015, 2014, and 2013, respectively.

Deposits

Total deposits increased $26.2 million, or 3.3%, to $821.5 million at December 31, 2015 from $795.3 million at the end of 2014. Non-interest-bearing demand deposits increased $30.5 million, or 24.6%, while interest-bearing deposits decreased $4.3 million, or 0.6%. The increase in non-interest-bearing demand deposits primarily reflected balance fluctuations of several large commercial relationships. The decrease in interest-bearing deposits was primarily due to a decrease in time deposits $100 thousand and over of $35.8 million, partially offset by increases in interest-bearing demand, savings and other time deposits of $18.6 million, $3.4 million and $9.6 million, respectively. The 32.0% decrease in large denomination time deposits was due largely to the planned runoff of $33.3 million in certificates of deposit that were generated through a national deposit listing service. As part of the Company's asset/liability management strategy, management focused on replacing these higher-costing deposits as they matured with lower-costing core-customer deposits, brokered certificates of deposit and advances through the FHLB of Pittsburgh. The 5.4% increase in interest-bearing demand deposits reflected a $68.9 million, or 70.2%, increase in money market accounts, which was due primarly to the attainment of a large deposit relationship at the end of the second quarter of 2015. Partially offsetting the increase in money market accounts was a $51.2 million, or 22.1%, decrease in NOW accounts, which resulted from decreases in public fund balances, as a state budget impasse caused delays in funding for the Company's municipal customers, as well as the loss of one large public fund deposit relationship in the third quarter of 2015.

Non-interest-bearing demand deposits averaged $5.8 million, or 4.3%, higher in 2015 as compared to 2014. Interest-bearing deposits averaged $674.6 million in 2015, a decrease of $3.2 million, or 0.5%, compared to $677.8 million in 2014. The decline was concentrated in time deposits, as average time deposits over $100,000 decreased $38.2 million, or 28.1%, to $97.7 million in 2015 from $135.9 million in 2014 due to the planned runoff of the certificates generated throught the national listing service. Time deposits with balances less than $100 thousand declined $5.6 million, or 4.3%, to $126.9 million in 2015 from $132.5 million in 2014. Partially offsetting the decreases in time deposits were increases in average interest-bearing demand and savings deposits which grew $37.7 million, or 11.7%, and $2.9 million, or 3.3%, respectively, comparing 2015 and 2014. The Company was successful in continuing to reduce its funding costs as evidenced by an 8 basis point decrease in the rate paid on average interest-bearing deposits to 0.39% in 2015 from 0.47% in 2014. The decrease was driven primarily by pricing decreases from time deposits, which are sensitive to interest rate changes. The Company elected to allow higher-costing time deposits to mature and chose to be more conservative in setting rates on new deposits and renewals. The average rate paid on time deposits with balances less than $100 thousand decreased 26 basis points to 0.96%, while the rate paid on time deposits over $100 thousand decreased 7 basis points to 0.70% during 2015.

Management recognizes the importance of deposit growth as the Company's primary funding source for its loan products and is in the process of developing new products and strategies focused on growing commercial and consumer demand deposit balances and municipal deposit relationships in 2016.

The average amount of, and the rate paid on, the major classifications of deposits for the past three years are summarized in the following table:

Deposit Distribution

	For the Year Ended December 31,					
	2015		2014		2013	
(dollars in thousands)	Amount	Rate	Amount	Rate	Amount	Rate
Interest-bearing deposits:						
Demand	$358,442	0.19%	$320,780	0.14%	$302,258	0.18%
Savings	91,603	0.07%	88,678	0.06%	85,872	0.10%
Time	224,538	0.85%	268,360	0.99%	317,367	1.11%
Total interest-bearing deposits	674,583	0.39%	677,818	0.47%	705,497	0.59%
Non-interest-bearing deposits	139,945		134,132		130,186	
Total deposits	$814,528		$811,950		$835,683	

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The following table presents the maturity distribution of time deposits of $100,000 or more at December 31, 2015 and 2014:

Maturity Distribution of Time Deposits Greater than $100,000

	December 31,	
(in thousands)	**2015**	**2014**
3 months or less	$26,773	$30,040
Over 3 through 6 months	16,186	27,919
Over 6 through 12 months	19,185	32,052
Over 12 months	14,053	22,033
Total	$76,197	$112,044

Borrowings

Short-term borrowings generally represent overnight borrowing transactions through the FHLB providing for short-term funding requirements of the Company and mature within one business day of the transaction. Short-term borrowings may also include Federal funds sold and borrowings through the FRB discount window and are considered to be a contingency source of funding. Other than testing its availability for contingency funding planning purposes, the Company did not purchase any Federal funds or borrow from the Federal Reserve discount window during the years ended December 31, 2015, 2014 and 2013. The Company had $60.5 million in outstanding short-term borrowings with the FHLB of Pittsburgh at December 31, 2015. There were no short-term borrowings outstanding at December 31, 2014 and 2013.

Long-term debt is comprised of FHLB term advances, subordinated debentures and junior subordinated debentures and totaled $99.6 million at December 31, 2015, an increase of $3.1 million, or 3.2%, from $96.5 million at December 31, 2014. The increase was related a $14.1 million increase in advances through the FHLB of Pittsburgh, partially offset by an $11.0 million reduction in the Notes. FHLB advances are collateralized under a blanket pledge agreement. The Company is also required to purchase FHLB stock based upon the amount of advances outstanding. Due to the increase in FHLB advances, the FHLB stock required to be held by the Company was $6.3 million at December 31, 2015, an increase of $3.5 million from $2.8 million at December 31, 2014. At December 31, 2015, the Company had $127.3 million of credit with the FHLB available for borrowing purposes.

On September 1, 2009, the Company offered only to accredited investors up to $25.0 million principal amount of unsecured subordinated debentures due September 1, 2019 (the "Notes"). Prior to July 1, 2015, the Notes had a fixed interest rate of 9% per annum. Payments of interest are payable to registered holders of the Notes (the "Noteholders") quarterly on the first of every third month, subject to the right of the Company to defer such payment. On June 30, 2015, pursuant to approval from all of the Noteholders and the Reserve Bank, the Company amended the original terms of the Notes to reduce the interest rate payable from 9.00% to 4.50% effective July 1, 2015 and to accelerate a partial repayment of principal amount under the Notes. Pursuant to the approved amendment, on June 30, 2015, the Company repaid 44% of the original principal amount, or $11.0 million, of the Notes outstanding to the holders on June 30, 2015, with the remaining $14.0 million in principal to be repaid as follows: (a) 16% of the original principal amount, or $4.0 million, payable on September 1, 2017; (b) 20% of the original principal amounts, or $5.0 million, payable on September 1, 2018; and (c) the final 20% of the original principal amount, or $5.0 million, payable on September 1, 2019, the maturity date of the Notes. The principal balance outstanding for these notes was $14.0 million at December 31, 2015 and $25.0 million at December 31, 2014.

While the Company was under the Written Agreement, principal and interest payments on the Notes required written non-objection from the Reserve Bank. Pursuant to the Written Agreement, the Company had been deferring the quarterly interest payments on the Notes beginning December 1, 2010 and ending on June 1, 2015. Regularly scheduled quarterly interest payments were resumed on September 1, 2015, and it is the Company's intent to continue scheduled interest payments on a go-forward basis. Additionally, on January 27, 2016, that the Board of Directors authorized payment on March 1, 2016 of all interest that the Company had previously been deferring on the Notes. The aggregate payment, totaling $11.0 million, includes all deferred interest and interest that is due and payable on March 1, 2016. The accrued and unpaid interest associated with the Notes amounted to $10.9 million and $9.9 million at December 31, 2015 and 2014, respectively.

The Company also had $10.3 million of junior subordinated debentures at December 31, 2015 and 2014. The interest rate on these debentures, resets quarterly at a spread of 1.67% above the current 3-month Libor rate. The average rate paid for junior subordinated debentures in 2015 was 1.99%, compared to 1.93% in 2014.

Average borrowed funds increased $14.3 million, or 15.2%, to $108.0 million in 2015 from $93.7 million in 2014. The average rate paid for long-term debt decreased 116 basis points to 2.01% in 2015 from 3.17% in 2014. The decrease in rate on the long-term debt was due to a reduction in the interest rate on the Company's subordinated notes, coupled with a decrease in the cost of FHLB funding. The Company participates in the FHLB's "Community Lending Program," which offers match funding for loans originated for qualified community and economic development projects at very competitive rates that are typically 15 to 25 basis points below the FHLB's regular published rates. Of the $75.3 million in FHLB term advances outstanding at December 31, 2015, $46.4 million were advances under this program had a weighted-average cost of 0.33% and maturity terms ranging from three months to two years.

The maximum amount of total borrowings outstanding at any month end during the years ended December 31, 2015 and 2014 were $160.1 million and $122.7 million, respectively. For further discussion of the Company's borrowings, see Note 11-"Borrowed Funds" in the Notes to the consolidated financial statements included in Item 8 hereof to this Annual Report on Form 10-K.

Liquidity

The term liquidity refers to the ability of the Company to generate sufficient amounts of cash to meet its cash flow needs. Liquidity is required to fulfill the borrowing needs of the Company's credit customers and the withdrawal and maturity requirements of its deposit customers, as well as to meet other financial commitments. The Company's liquidity position is impacted by several factors, which include, among others, loan origination volumes, loan and investment maturity structure and cash flows, deposit demand and certificate of deposit maturity structure and retention. The Company has liquidity and contingent funding policies in place that are designed with controls in place to provide advanced detection of potentially significant funding shortfalls, establish methods for assessing and monitoring risk levels, and institute prompt responses that may alleviate a potential liquidity crisis. Management monitors the Company's liquidity position and fluctuations daily so that the Company can adapt accordingly to market influences and balance sheet trends. Management also forecasts liquidity needs, performs stress tests on its liquidity levels and develops strategies to ensure adequate liquidity at all times.

The Company's statements of cash flows present the change in cash and cash equivalents from operating, investing and financing activities. Cash and due from banks and interest-bearing deposits in other banks are the Company's most liquid assets. At December 31, 2015, cash and cash equivalents totaled $21.1 million, a decrease of $14.6 million from $35.7 million at December 31, 2014, as net cash outlays for investing activities exceeded net cash inflows from operating and financing activities. Cash outlays for investing activities used $109.0 million of cash and cash equivalents during the year ended December 31, 2015, which was due largely to a net increase in loans to customers of $68.8 million. In addition, purchases of available-for-sale securities, net of proceeds received from sales, maturities, calls and principal reductions from securities, and FHLB of Pittsburgh stock used $36.0 million and $3.5 million of cash and cash equivalents, respectively. Financing activities provided $89.8 million in net cash, which resulted primarily from $74.6 million in proceeds from FHLB of Pittsburgh advances, net of repayments, and a $26.2 million net increase in deposits. Partially offsetting these inflows was an $11.0 million principal reduction on the Notes.

Additionally, the Company's operating activities provided $4.6 million in net cash in 2015. Net income, adjusted for the effects of non cash transactions including, among others, depereciation and amortization, the credit for loan and lease losses and change in deferred taxes, is the primary source of funds from operations.

Despite the decrease in cash and cash equivalents, management believes that the Company's liquidity position is sufficient to meet its cash flow needs as of December 31, 2015. The Company generally utilizes core deposits as its primary source of liquidity. Core deposits include non-interest-bearing and interest-bearing demand deposits, savings deposits and other time deposits, net of brokered deposits and deposits generated through the Promontory Interfinancial Network, which include time deposits issued under Certificate of Deposit Account Registry Service ("CDARs") and money market and NOW accounts issued through the Insured Cash Sweep ("ICS") program. Participating in the Promontory Interfinancial Network programs allow the Company to service and attract potential high-balance deposits customers who want the security of full-FDIC insurance but want to maintain a local deposit relationship. Core deposits averaged $680.8 million for the year ended December 31, 2015, an increase of $9.3 million, or 1.4%, compared to $671.5 million for the year ended December 31, 2014. The increase in core deposits primarily reflected growth in interest-bearing demand, net of deposits issued through the ICS program, of $15.7 million, non-interest-bearing demand deposits of $5.8 million and savings deposits of $2.9 million. Partially offsetting these increases was a decrease in other time deposits, net of brokered deposits and CDARs certificates, of $15.1 million. In addition to core deposits, the Company currently utilizes brokered certificates of deposit, funding through the Promontory Financial Network and advances through the FHLB of Pittsburgh as alternative sources of liquidity. At December 31, 2015, the Company had available borrowing capacity with the FHLB of Pittsburgh of $160.2 million.

Capital

A strong capital base is essential to the continued growth and profitability of the Company and is therefore a management priority. The Company's principal capital planning goals are to provide an adequate return to shareholders while retaining a sufficient base from which to provide for future growth, while at the same time complying with all regulatory standards. As more fully described in Note 17, "Regulatory Matters" to the notes to the consolidated financial statements included in Item 8 of this Annual Report on Form 10-K, regulatory authorities have prescribed specified minimum capital ratios as guidelines for determining capital adequacy to help assure the safety and soundness of financial institutions.

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The following schedules present information regarding the Company’s risk-based capital at December 31, 2015, 2014, and 2013 and selected other capital ratios:

	December 31,		
(in thousands)	**2015**	**2014**	**2013**
Company:			
Tier I common equity	$74,945	N/A	N/A
Tier I capital	74,945	$59,930	$46,165
Tier II capital:			
Subordinated notes	9,800	25,000	23,085
Allowable portion of allowance for loan losses	9,090	8,591	8,462
Total tier II capital	18,890	33,591	31,547
Total risk-based capital	$93,835	$93,521	$77,712
Total risk-weighted assets	$795,887	$683,956	$670,894
Total average assets (for Tier 1 leverage ratio)	$1,031,426	$990,346	$980,754
Bank:			
Tier I common equity	$100,949	N/A	N/A
Tier I capital	100,949	96,816	81,581
Tier II capital:			
Allowable portion of allowance for loan losses	9,090	8,587	8,456
Total tier II capital	9,090	8,587	8,456
Total risk-based capital	$110,039	$105,403	$90,037
Total risk-weighted assets	$795,490	$683,576	$670,416
Total average assets (for Tier 1 leverage ratio)	$1,030,828	$990,407	$980,747

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	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provision	
(dollars in thousands)	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
December 31, 2015						
Total capital (to risk-weighted assets)						
Company	$93,835	11.79%	$>63,671	8.00 %	N/A	N/A
Bank	$110,039	13.83%	$>63,639	8.00 %	$>79,549	10.00%
Tier I capital (to risk-weighted assets)						
Company	$74,945	9.42 %	$>47,753	6.00 %	N/A	N/A
Bank	$100,949	12.69%	$>47,729	6.00 %	$>63,639	8.00 %
Tier I common equity (to risk-weighted assets)						
Company	$74,945	9.42 %	$>35,815	4.50 %	N/A	N/A
Bank	$100,949	12.69%	$>35,797	4.50 %	$>51,707	6.50 %
Tier I capital (to average assets)						
Company	$74,945	7.27 %	$>41,257	4.00 %	N/A	N/A
Bank	$100,949	9.79 %	$>41,233	4.00 %	$>51,541	5.00 %

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provision	
(dollars in thousands)	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
December 31, 2014						
Total capital (to risk-weighted assets)						
Company	$93,521	13.67%	$>54,717	>8.00%	N/A	N/A
Bank	$105,403	15.42%	$>54,686	>8.00%	$>68,358	>10.00%
Tier I capital (to risk-weighted assets)						
Company	$59,930	8.76 %	$>27,358	>4.00%	N/A	N/A
Bank	$96,816	14.16%	$>27,343	>4.00%	$>41,015	>6.00 %
Tier I capital (to average assets)						
Company	$59,830	6.05 %	$>39,614	>4.00%	N/A	N/A
Bank	$96,816	9.78 %	$>39,616	>4.00%	$>49,520	>5.00 %

Despite net income of $35.8 million in 2015, the Company's total regulatory capital increased only $0.3 million to $93.8 million at December 31, 2015 from $93.5 million at December 31, 2014. For regulatory capital purposes, Tier I capital is adjusted for deferred tax assets that arise of NOLs and tax credit carryforwards. In addition, the Company's Tier II capital was impacted by the $11.0 million prepayment of the Notes. The Company's and the Bank's risk-based capital ratios exceeded the minimum regulatory capital ratios required for adequately capitalized institutions. Based on the most recent notification from the OCC, the Bank was categorized as well capitalized at December 31, 2015 and

2014. There are no conditions or events since this notification the management believes have changed this category.

As of December 31, 2015, there were 33,485,755 common shares available for future sale or share dividends. The number of shareholders of record at December 31, 2015 was 1,778. Quarterly market highs and lows, dividends paid and known market makers are highlighted in Part I, Item 5 of this report. Refer to Note 17, “Regulatory Matters,” to the Notes to consolidated financial statements included in Item 8 of this Annual Report on Form 10-K for further discussion of our capital requirements and dividend limitations.

Additionally, the Company has available 20,000,000 authorized shares of preferred stock. There were no preferred shares issued and outstanding at December 31, 2015 and 2014.

During 1999, the Company implemented a Dividend Reinvestment Plan (“DRP”) which permits participants to automatically reinvest cash dividends on all of their shares and to make voluntary cash contributions under terms of the plan. Under the DRP, participants purchase, at a 10% discount to the 10-day trading average, common shares that are either newly-issued by the Company or acquired by the plan administrator in the open market or privately. While under the Consent Order and Written Agreement, the Company was prohibited from paying dividends without the prior approval of the OCC and the Reserve Bank. Accordingly, the board of directors on February 26, 2010 voted to suspend payment of the Company’s quarterly dividend in an effort to conserve capital and subsequently suspended the operation of the DRP Plan in 2011. There was no new capital issued under the DRP in 2015 and 2014. The Company plans to reinstate the DRP Plan in 2016.

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As previously mentioned, the Company and the Bank was released from all regulatory enforcement actions and is no longer subject to the provisions of the Consent Order or Written Agreement. On January 27, 2016, the Company declared a $0.02 per share dividend payable on March 15, 2016 to shareholders of record March 1, 2016.

Off-Balance Sheet Arrangements

In the normal course of operations, the Company engages in a variety of financial transactions that, in accordance with GAAP, are not recorded in our consolidated financial statements, or are recorded in amounts that differ from the notional amounts. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions may be used for general corporate purposes or for customer needs. Corporate purpose transactions would be used to help manage credit, interest rate and liquidity risk or to optimize capital. Customer transactions are used to manage customers' requests for funding.

For the year ended December 31, 2015, the Company did not engage in any off-balance sheet transactions that would have or would be reasonably likely to have a material effect on its consolidated financial condition. For a further discussion of the Company’s off-balance sheet arrangements, refer to Note 15, “Commitments, Contingencies, and Concentrations” to the notes to the consolidated financial statements included in Item 8 hereof to this Annual Report on Form 10-K.

Financial instruments whose contract amounts represent credit risk at December 31 are as follows:

Off-Balance Sheet Commitments

	December 31,	
(in thousands)	**2015**	**2014**
Commitments to extend credit	$170,465	$181,446
Standby letters of credit	22,092	21,364

The following table details the Company’s commercial commitments summarized by expiration at December 31, 2015:

Expiration of Off-Balance Sheet Commitments

(in thousands)	Total Amounts Commited	Less Than one Year	1-3 Years	3-5 Years	More Than 5 Years
Commitments to extend credit	$ 170,465	$170,447	$ 18	$ -	$ -
Standby letters of credit	22,092	22,092	-	-	-
Total	$ 192,557	$192,539	$ 18	$ -	$ -

In order to provide for probable losses inherent in these instruments, the Company recorded reserves for unfunded commitments of $300 thousand and $416 thousand at December 31, 2015 and 2014, respectively, which were included in other liabilities on the consolidated statements of financial condition.

The Company's Finance unit proactively monitors the level of unused commitments against the Company's available sources of liquidity from its investment portfolio, from deposit gathering activities as well as available unused borrowing capacity from the FHLB and the Federal Reserve. The Finance unit reports the results of its liquidity monitoring regularly to the Company's Asset/Liability Committee, the Rate and Liquidity Committee, the Senior Management Committee and the Board of Directors.

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Contractual Obligations

The following table details the Company's contractual obligations as of December 31, 2015. Payments due by period in the following table are based on final maturity dates without consideration of early redemption.

Maturities of Contractual Obligations

	Contractual Payments Due by Period				
(in thousands)	Total	Less Than one Year	1-3 Years	3-5 Years	More Than 5 Years
Federal Home Loan Bank advances	$135,802	$114,423	$15,000	$6,379	$-
Subordinated debentures	14,000	-	9,000	5,000	-
Junior subordinated debt	10,310	-	-	-	10,310
Operating lease obligations	1,677	585	587	228	277
Total contractual cash obligations	$161,789	$115,008	$24,587	$11,607	$10,587

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Interest Rate Risk

Interest Rate Sensitivity

Market risk is the risk to earnings and/or financial position resulting from adverse changes in market rates or prices, such as interest rates, foreign exchange rates or equity prices. The Company's exposure to market risk is primarily interest rate risk associated with our lending, investing and deposit gathering activities, all of which are other than trading. Changes in interest rates affect earnings by changing net interest income and the level of other interest-sensitive income and operating expenses. In addition, variations in interest rates affect the underlying economic value of our assets, liabilities and off-balance sheet items.

Asset and Liability Management

The Company manages these objectives through its Asset and Liability Management Committee ("ALCO") and its Rate and Liquidity and Investment Committees, which consist of certain members of senior management and certain members of the finance department. Members of the committees meet regularly to develop balance sheet strategies affecting the future level of net interest income, liquidity and capital. The major objectives of ALCO are to:

- Manage exposure to changes in the interest rate environment by limiting the changes in net interest margin to an acceptable level within a reasonable range of interest rates;
- Ensure adequate liquidity and funding;
- Maintain a strong capital base; and
- Maximize net interest income opportunities.

ALCO monitors the Company's exposure to changes in net interest income over both a one-year planning horizon and a longer-term strategic horizon. ALCO uses net interest income simulations and economic value of equity ("EVE") simulations as the primary tools in measuring and managing the Company's position and considers balance sheet forecasts, the Company's liquidity position, the economic environment, anticipated direction of interest rates and the Company's earnings sensitivity to changes in these rates in its modeling. In addition, ALCO has established policy tolerance limits for acceptable negative changes in net interest income. Furthermore, as part of its ongoing monitoring, ALCO has been enhanced to require periodic back testing of modeling results, which involves after-the-fact comparisons of projections with the Company's actual performance to measure the validity of assumptions used in the modeling techniques.

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Earnings at Risk and Economic Value at Risk Simulations

Earnings at Risk

Earnings-at-risk simulation measures the change in net interest income and net income under various interest rate scenarios. Specifically, given the current market rates, ALCO looks at "earnings at risk" to determine anticipated changes in net interest income from a base case scenario with rate shock scenarios of + 200, +400 and -100 basis point changes to interest rates. The simulation takes into consideration that not all assets and liabilities re-price equally and simultaneously with market rates (i.e., savings rate).

Economic Value at Risk

While earnings-at-risk simulation measures the short-term risk in the balance sheet, economic value (or portfolio equity) at risk measures the long-term risk by finding the net present value of the future cash flows from the Company's existing assets and liabilities. ALCO examines this ratio regularly, and given the current rate environment, has utilized rate shocks of +200, +400 and - 100 basis points for simulation purposes. Management recognizes that, in some instances, this ratio may contradict the "earnings at risk" ratio.

While ALCO regularly performs a wide variety of simulations under various strategic balance sheet and treasury yield curve scenarios, the following results reflect the Company's sensitivity over the subsequent twelve months based on the following assumptions:

- Asset and liability levels using December 31, 2015 as a starting point;
- Cash flows are based on contractual maturity and amortization schedules with applicable prepayments derived from internal historical data and external sources; and
- Cash flows are reinvested into similar instruments so as to keep interest-earning asset and interest-bearing liability levels constant.

The following table illustrates the simulated impact of parallel and instantaneous interest rate shocks of +400 basis points, +200 basis points and -100 basis points on net interest income and the change in economic value over a one-year time horizon from the December 31, 2015 levels:

	Rates +200		Rates +400		Rates -100	
	Simulation Results	Policy Limit	Simulation Results	Policy Limit	Simulation Results	Policy Limit
Earnings at risk:						
Percent change in net interest income	(3.2)%	(10.0)%	(6.6)%	(20.0)%	(2.0)%	(5.0)%
Economic value at risk:						
Percent change in economic value of equity	(11.2)%	(20.0)%	(20.7)%	(35.0)%	(4.0)%	(10.0)%

Under the model, the Company’s net interest income and economic value of equity is expected to decrease 3.2% and 11.2%, respectively, under a 200 basis point interest rate shock. In comparison, model results at December 31, 2014 indicated net interest income was expected to increase 0.9% given a +200 basis point rate shocks. The shift in Company’s asset/liability position during 2015 primarily reflected an increase in interest-bearing demand deposits and overnight advances from the FHLB of Pittsburgh, which reprice immediately under rate shock scenarios.

This analysis does not represent a Company forecast and should not be relied upon as being indicative of expected operating results. These simulations are based on numerous assumptions: the nature and timing of interest rate levels, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, reinvestment/replacements of asset and liability cash flows, and other factors. While assumptions reflect current economic and local market conditions, the Company cannot make any assurances as to the predictive nature of these assumptions, including changes in interest rates, customer preferences, competition and liquidity needs, or what actions ALCO might take in responding to these changes.

As previously mentioned, as part of its ongoing monitoring, ALCO requires periodic back testing of modeling results, which involves after-the-fact comparisons of projections with the Company’s actual performance to measure the validity of assumptions used in the modeling techniques. As part of its quarterly review, management compared tax-equivalent net interest income recorded for the three months ended December 31, 2015 with tax-equivelent net interest income that was projected for the same three-month period. The variance between actual and projected tax-equivalent net interest income for the three-month period ended December 31, 2015 was $137 thousand or 1.7%. Although the variance was deemed immaterial, ALCO performs a rate/volume analysis between actual and projected results in order to continue to improve the accuracy of its simulation models.

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Item 8. Financial Statements and Supplementary Data.

Report of Independent Registered Public Accounting Firm

Shareholders and Board of Directors of
First National Community Bancorp, Inc. and Subsidiaries

We have audited the accompanying consolidated statements of financial condition of First National Community Bancorp, Inc. and Subsidiaries (the "Company") as of December 31, 2015 and 2014 and the related consolidated statements of income, comprehensive income (loss), changes in shareholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of First National Community Bancorp, Inc. and Subsidiaries as of December 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2015, based on criteria established in *Internal Control-Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 11, 2016 expressed an unqualified opinion.

/s/Baker Tilly Virchow Krause, LLP

Wilkes-Barre, Pennsylvania
March 11, 2016

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders

First National Community Bancorp, Inc. and Subsidiaries

We have audited the accompanying consolidated statements of operations, comprehensive loss, changes in shareholders' equity and cash flows for the year ended December 31, 2013 of First National Community Bancorp, Inc. and Subsidiaries (the "Company"). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether 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 audit provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the results of operations and cash flows of First National Community Bancorp, Inc. and Subsidiaries for the year ended December 31, 2013, in conformity with U.S. generally accepted accounting principles.

/s/ RSM US LLP

New Haven, Connecticut

March 24, 2014

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(in thousands, except share data)	**December 31, 2015**	**December 31, 2014**
Assets		
Cash and cash equivalents:		
Cash and due from banks	$ 19,544	$ 22,657
Interest-bearing deposits in other banks	1,539	13,010
Total cash and cash equivalents	21,083	35,667
Securities available for sale, at fair value	253,773	218,989
Stock in Federal Home Loan Bank of Pittsburgh, at cost	6,344	2,803
Loans held for sale	683	603
Loans, net of allowance for loan and lease losses of $8,790 and $11,520	724,926	658,747
Bank premises and equipment, net	11,193	11,003
Accrued interest receivable	2,475	2,075
Intangible assets	137	302
Bank-owned life insurance	29,381	28,817
Other real estate owned	3,154	2,255
Net deferred tax assets	27,807	-
Other assets	9,662	8,768
Total assets	$ 1,090,618	$ 970,029
Liabilities		
Deposits:		
Demand (non-interest-bearing)	$ 154,531	$ 124,064
Interest-bearing	667,015	671,272
Total deposits	821,546	795,336
Borrowed funds:		
Federal Home Loan Bank of Pittsburgh advances	135,802	61,194
Subordinated debentures	14,000	25,000
Junior subordinated debentures	10,310	10,310
Total borrowed funds	160,112	96,504
Accrued interest payable	11,165	10,262
Other liabilities	11,617	16,529
Total liabilities	1,004,440	918,631
Shareholders' equity		
Preferred shares ($1.25 par)		
Authorized: 20,000,000 shares at December 31, 2015 and December 31, 2014		
Issued and outstanding: 0 shares at December 31, 2015 and December 31, 2014	-	-
Common shares ($1.25 par)		
Authorized: 50,000,000 shares at December 31, 2015 and December 31, 2014		

Issued and outstanding: 16,514,245 shares at December 31, 2015 and 16,484,419 shares at December 31, 2014	20,643	20,605
Additional paid-in capital	62,059	61,781
Retained earnings (accumulated deficit)	3,714	(32,126)
Accumulated other comprehensive (loss) income	(238)	1,138
Total shareholders' equity	86,178	51,398
Total liabilities and shareholders' equity	$ 1,090,618	$ 970,029

The accompanying notes to consolidated financial statements are an integral part of these statements.

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

	For the Year Ended December 31,		
(dollars in thousands, except share data)	**2015**	**2014**	**2013**
Interest income			
Interest and fees on loans	$26,672	$26,629	$27,097
Interest and dividends on securities:			
U.S. government agencies	4,036	3,494	1,859
State and political subdivisions, tax-free	109	1,883	3,347
State and political subdivisions, taxable	905	324	393
Other securities	433	272	154
Total interest and dividends on securities	5,483	5,973	5,753
Interest on interest-bearing deposits in other banks	46	71	103
Total interest income	32,201	32,673	32,953
Interest expense			
Interest on deposits	2,631	3,180	4,164
Interest on borrowed funds:			
Interest on Federal Home Loan Bank of Pittsburgh advances	514	450	527
Interest on subordinated debentures	1,450	2,281	2,281
Interest on junior subordinated debentures	206	236	204
Total interest on borrowed funds	2,170	2,967	3,012
Total interest expense	4,801	6,147	7,176
Net interest income before credit for loan and lease losses	27,400	26,526	25,777
Credit for loan and lease losses	(1,345)	(5,869)	(6,270)
Net interest income after credit for loan and lease losses	28,745	32,395	32,047
Non-interest income			
Deposit service charges	2,960	2,975	2,945
Net gain on the sale of securities	2,296	6,640	2,887
Net gain on the sale of mortgage loans held for sale	292	292	362
Net loss on the sale of classified loans	-	-	(223)
Net loss on the sale of education loans	-	(13)	-
Net gain on the sale of other real estate owned	162	209	135
Gain on the sale of bank premises and equipment and other assets	-	-	579
Gain on branch divestitures	-	607	-
Loan-related fees	442	440	423
Income from bank-owned life insurance	564	650	706
Legal settlements	184	2,127	288
Other	900	993	1,181
Total non-interest income	7,800	14,920	9,283
Non-interest expense			
Salaries and employee benefits	13,810	13,111	13,218
Occupancy expense	2,284	2,088	2,215
Equipment expense	1,657	1,471	1,468

Advertising expense	483	470	523
Data processing expense	1,976	2,088	2,066
Regulatory assessments	950	1,801	2,515
Bank shares tax	705	522	800
Expense of other real estate owned	400	2,569	719
Legal expense	437	1,799	2,488
Professional fees	1,014	1,567	1,674
Insurance expenses	659	951	1,179
Loan collection expenses	280	90	482
Legal settlements	777	-	2,500
Other losses	281	2,279	123
Other operating expenses	2,751	2,763	2,978
Total non-interest expense	28,464	33,569	34,948
Income before income taxes	8,081	13,746	6,382
Income tax (benefit) expense	(27,759)	326	-
Net income	$35,840	$13,420	$6,382
Earnings per share			
Basic	$2.17	$0.81	$0.39
Diluted	$2.17	$0.81	$0.39
Cash Dividends Declared Per Common Share	$-	$-	$-
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING:			
Basic	16,499,622	16,472,660	16,458,353
Diluted	16,499,622	16,472,871	16,458,353

The accompanying notes to consolidated financial statements are an integral part of these statements.

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	For the Year Ended December 31,		
(in thousands)	**2015**	**2014**	**2013**
Net income	$35,840	$13,420	$6,382
Other comprehensive income (loss):			
Unrealized gains (losses) on securities available for sale	211	12,682	(11,946)
Taxes	(72)	(4,312)	4,061
Net of tax amount	139	8,370	(7,885)
Reclassification adjustment for gains included in net income	(2,296)	(6,272)	(2,887)
Taxes	781	2,132	982
Net of tax amount	(1,515)	(4,140)	(1,905)
Total other comprehensive (loss) income	(1,376)	4,230	(9,790)
Comprehensive income (loss)	$34,464	$17,650	$(3,408)

The accompanying notes to consolidated financial statements are an integral part of these statements.

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

For the Years Ended December 31, 2015, 2014 and 2013

(in thousands, except share data)	Number of Common Shares	Common Stock	Additional Paid-in Capital	Accumulated (Deficit) / Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balances, December 31, 2012	16,457,169	$ 20,571	$ 61,584	$ (51,928)	$ 6,698	$ 36,925
Net income for the year	-	-	-	6,382	-	6,382
Stock-based compensation	14,400	18	43	-	-	61
Other comprehensive loss, net of tax of $5,043	-	-	-	-	(9,790)	(9,790)
Balances, December 31, 2013	16,471,569	$ 20,589	$ 61,627	$ (45,546)	$ (3,092)	$ 33,578
Net income for the year	-	-	-	13,420	-	13,420
Stock-based compensation	12,850	16	61	-	-	77
Restricted stock awards	-	-	93	-	-	93
Other comprehensive income, net of tax of $2,180	-	-	-	-	4,230	4,230
Balances, December 31, 2014	16,484,419	$ 20,605	$ 61,781	$ (32,126)	$ 1,138	$ 51,398
Net income for the year	-	-	-	35,840	-	35,840
Stock-based compensation	13,300	17	52	-	-	69
Common stock issued under long-term incentive compensation plan	16,526	21	(21)	-	-	-
Restricted stock awards	-	-	247	-	-	247
Other comprehensive loss, net of tax of $709	-	-	-	-	(1,376)	(1,376)
Balances, December 31, 2015	16,514,245					