AMERISERV FINANCIAL INC /PA/
Form 10-Q
August 05, 2016

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

FORM 10-Q

x **Quarterly Report Pursuant to Section 13 or 15(d)**
of the Securities Exchange Act of 1934
For the period ended **June 30, 2016**

Transition Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934
For the transition period from to

Commission File Number **0-11204**

AmeriServ Financial, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania (State or other jurisdiction of incorporation or organization)	25-1424278 (I.R.S. Employer Identification No.)
	15907-0430

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.Yes x No o

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

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

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

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

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

Class	Outstanding at August 1, 2016
Common Stock, par value $0.01	18,896,876

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Item 1. Financial Statements

AmeriServ Financial, Inc.

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

	June 30, 2016	December 31, 2015
ASSETS		
Cash and due from depository institutions	$20,182	$23,443
Interest bearing deposits	2,788	6,960
Short-term investments in money market funds	4,048	18,107
Total cash and cash equivalents	27,018	48,510
Investment securities:		
Available for sale	120,325	119,467
Held to maturity (fair value $26,228 on June 30, 2016 and $21,533 on December 31, 2015)	25,428	21,419
Loans held for sale	3,140	3,003
Loans	892,875	881,541
Less: Unearned income	502	557
Allowance for loan losses	9,746	9,921
Net loans	882,627	871,063
Premises and equipment, net	11,888	12,108
Accrued interest income receivable	3,286	3,057
Goodwill	11,944	11,944
Bank owned life insurance	37,564	37,228
Net deferred tax asset	8,767	8,993
Federal Home Loan Bank stock	3,737	4,628
Federal Reserve Bank stock	2,125	2,125
Other assets	4,643	4,952
TOTAL ASSETS	$1,142,492	$1,148,497
LIABILITIES		
Non-interest bearing deposits	$173,643	$188,947
Interest bearing deposits	767,288	714,347
Total deposits	940,931	903,294
Short-term borrowings	22,575	48,748
Advances from Federal Home Loan Bank	50,042	48,000
Guaranteed junior subordinated deferrable interest debentures, net	12,900	12,892
Subordinated debt, net	7,430	7,418
Total borrowed funds	92,947	117,058
Other liabilities	9,382	9,172
TOTAL LIABILITIES	1,043,260	1,029,524
SHAREHOLDERS EQUITY		

Preferred stock, no par value; $1,000 per share liquidation preference; 2,000,000 shares authorized; 21,000 shares issued and outstanding on December 31, 2015		21,000
Common stock, par value $0.01 per share; 30,000,000 shares authorized; 26,514,695 shares issued and 18,896,876 outstanding on June 30, 2016; 26,488,630 shares issued and 18,870,811 outstanding on December 31, 2015	265	265
Treasury stock at cost, 7,617,819 shares on June 30, 2016 and December 31, 2015	(74,829)	(74,829)
Capital surplus	145,506	145,441
Retained earnings	34,355	34,651
Accumulated other comprehensive loss, net	(6,065)	(7,555)
TOTAL SHAREHOLDERS EQUITY	99,232	118,973
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$1,142,492	$1,148,497

See accompanying notes to unaudited consolidated financial statements.

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AmeriServ Financial, Inc.

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

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
INTEREST INCOME				
Interest and fees on loans	$9,409	$9,480	$18,874	$18,936
Interest bearing deposits	2	5	9	7
Short-term investments in money market funds	13	1	23	3
Investment securities:				
Available for sale	778	777	1,545	1,690
Held to maturity	187	146	360	296
Total Interest Income	10,389	10,409	20,811	20,932
INTEREST EXPENSE				
Deposits	1,330	1,171	2,584	2,345
Short-term borrowings	5	23	47	33
Advances from Federal Home Loan Bank	159	135	318	260
Guaranteed junior subordinated deferrable interest debentures	280	280	560	560
Subordinated debt	129		258	
Total Interest Expense	1,903	1,609	3,767	3,198
NET INTEREST INCOME	8,486	8,800	17,044	17,734
Provision for loan losses	250	200	3,350	450
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	8,236	8,600	13,694	17,284
NON-INTEREST INCOME				
Trust and investment advisory fees	2,124	2,135	4,199	4,191
Service charges on deposit accounts	404	429	819	848
Net gains on sale of loans	185	225	292	416
Mortgage related fees	98	109	161	224
Net realized gains on investment securities	60	28	117	28
Bank owned life insurance	169	171	336	534
Other income	702	595	1,255	1,163
Total Non-Interest Income	3,742	3,692	7,179	7,404
NON-INTEREST EXPENSE				
Salaries and employee benefits	5,868	5,944	12,034	12,017
Net occupancy expense	690	718	1,427	1,559
Equipment expense	409	480	845	946
Professional fees	1,192	1,275	2,657	2,486
Supplies, postage and freight	154	175	349	353
Miscellaneous taxes and insurance	288	287	579	584
Federal deposit insurance expense	188	164	367	331
Other expense	1,250	1,196	2,492	2,373

Total Non-Interest Expense	10,039	10,239	20,750	20,649
PRETAX INCOME	1,939	2,053	123	4,039
Provision for income tax expense	577	632	28	1,249
NET INCOME	1,362	1,421	95	2,790
Preferred stock dividends		52	15	105
NET INCOME AVAILABLE TO COMMON SHAREHOLDERS	$1,362	$1,369	$80	$2,685
PER COMMON SHARE DATA:				
Basic:				
Net income	$0.07	$0.07	$0.00	$0.14
Average number of shares outstanding	18,897	18,859	18,890	18,855
Diluted:				
Net income	$0.07	$0.07	$0.00	$0.14
Average number of shares outstanding	18,948	18,941	18,943	18,923
Cash dividends declared	$0.01	$0.01	$0.02	$0.02

See accompanying notes to unaudited consolidated financial statements.

AmeriServ Financial, Inc.

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
COMPREHENSIVE INCOME				
Net income	$1,362	$1,421	$95	$2,790
Other comprehensive income, before tax:				
Pension obligation change for defined benefit plan	263	631	767	1,286
Income tax effect	(89)	(215)	(260)	(438)
Unrealized holding gains (losses) on available for sale securities arising during period	493	(946)	1,608	(600)
Income tax effect	(168)	321	(548)	204
Reclassification adjustment for gains on available for sale securities included in net income	(60)	(28)	(117)	(28)
Income tax effect	20	10	40	10
Other comprehensive income (loss)	459	(227)	1,490	434
Comprehensive income	$1,821	$1,194	$1,585	$3,224

See accompanying notes to unaudited consolidated financial statements.

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AmeriServ Financial, Inc.

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

	Six months ended June 30,	
	2016	2015
OPERATING ACTIVITIES		
Net income	$95	$2,790
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	3,350	450
Depreciation expense	892	925
Net amortization of investment securities	203	181
Net realized gains on investment securities available for sale	(117)	(28)
Net gains on loans held for sale	(292)	(416)
Amortization of deferred loan fees	(130)	(133)
Origination of mortgage loans held for sale	(20,215)	(27,878)
Sales of mortgage loans held for sale	20,370	28,952
Increase in accrued interest income receivable	(229)	(183)
Decrease in accrued interest payable	(180)	(255)
Earnings on bank owned life insurance	(336)	(341)
Deferred income taxes	(420)	371
Amortization of deferred issuance costs	20	
Stock based compensation expense	65	156
Other, net	1,326	443
Net cash provided by operating activities	4,402	5,034
INVESTING ACTIVITIES		
Purchases of investment securities available for sale	(18,894)	(7,410)
Purchases of investment securities held to maturity	(4,708)	(1,545)
Proceeds from sales of investment securities available for sale	7,422	519
Proceeds from maturities of investment securities available for sale	12,057	10,380
Proceeds from maturities of investment securities held to maturity	661	1,778
Purchases of regulatory stock	(7,608)	(9,464)
Proceeds from redemption of regulatory stock	8,499	8,332
Long-term loans originated	(108,221)	(118,956)
Principal collected on long-term loans	79,447	76,896
Loans purchased or participated	(4,948)	(5,120)
Loans sold or participated	18,900	12,055
Proceeds from sale of other real estate owned	47	478
Proceeds from life insurance policy		200
Purchases of premises and equipment	(663)	(473)
Net cash used in investing activities	(18,009)	(32,330)
FINANCING ACTIVITIES		
Net increase (decrease) in deposit balances	37,637	(7,053)

Net (decrease) increase in other short-term borrowings	(26,173)	24,550
Principal borrowings on advances from Federal Home Loan Bank	3,042	4,000
Principal repayments on advances from Federal Home Loan Bank	(1,000)	
Preferred stock redemption	(21,000)	
Common stock dividends	(376)	(377)
Preferred stock dividends	(15)	(105)
Net cash (used in) provided by financing activities	(7,885)	21,015
NET DECREASE IN CASH AND CASH EQUIVALENTS	(21,492)	(6,281)
CASH AND CASH EQUIVALENTS AT JANUARY 1	48,510	32,872
CASH AND CASH EQUIVALENTS AT JUNE 30	$27,018	$26,591

See accompanying notes to unaudited consolidated financial statements.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. Principles of Consolidation

The accompanying consolidated financial statements include the accounts of AmeriServ Financial, Inc. (the Company) and its wholly-owned subsidiaries, AmeriServ Financial Bank (the Bank), AmeriServ Trust and Financial Services Company (the Trust Company), and AmeriServ Life Insurance Company (AmeriServ Life). The Bank is a Pennsylvania state-chartered full service bank with 16 locations in Pennsylvania. The Trust Company offers a complete range of trust and financial services and administers assets valued at $2.0 billion that are not reported on the Company s balance sheet at June 30, 2016. AmeriServ Life is a captive insurance company that engages in underwriting as a reinsurer of credit life and disability insurance.

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

2. Basis of Preparation

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

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

3. Recent Accounting Pronouncements

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

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments-Credit Losses: Measurement of Credit Losses on Financial Instruments* (ASU 2016-13), which changes the impairment model for most financial assets. This ASU is intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The underlying premise of the ASU is that financial assets measured at amortized cost should be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. The allowance for credit losses should

reflect management s current estimate of credit losses that are expected to occur over the remaining life of a financial asset. The income statement will be effected for the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. ASU 2016-13 is effective for annual and interim periods beginning after December 15, 2019, and early adoption is permitted for annual and interim periods beginning after December 15, 2018. With certain exceptions, transition to the new requirements will be through a cumulative effect adjustment to opening retained earnings as of the beginning of the first reporting period in which the guidance is adopted. In June 2016, the four federal financial institution regulatory agencies issued a joint statement regarding ASU 2016-13 providing their initial supervisory views regarding the standard s implementation, including as it relates to measurement methods, use of vendors, portfolio segmentation, data collection, processes and controls over allowance methodology, and potential impact on capital. The Company is currently evaluating the impact the adoption of the standard will have on the Company s results of operations.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

4. Earnings Per Common Share

Basic earnings per share include only the weighted average common shares outstanding. Diluted earnings per share include the weighted average common shares outstanding and any potentially dilutive common stock equivalent shares in the calculation. Treasury shares are excluded for earnings per share purposes. Options to purchase 140,527 common shares, at exercise prices ranging from $3.18 to $4.60, were outstanding as of June 30, 2016, but were not included in the computation of diluted earnings per common share because to do so would be antidilutive. Options to purchase 179,304 common shares, at exercise prices ranging from $3.18 to $4.70, were outstanding as of June 30, 2015, but were not included in the computation of diluted earnings per common share because to do so would be antidilutive. Dividends on preferred shares are deducted from net income in the calculation of earnings per common share.

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
	(In thousands, except per share data)			
Numerator:				
Net income	$ 1,362	$ 1,421	$ 95	$ 2,790
Preferred stock dividends		(52)	(15)	(105)
Net income available to common shareholders	$ 1,362	$ 1,369	$ 80	$ 2,685
Denominator:				
Weighted average common shares outstanding (basic)	18,897	18,859	18,890	18,855
Effect of stock options	51	82	53	68
Weighted average common shares outstanding (diluted)	18,948	18,941	18,943	18,923
Earnings per common share:				
Basic	$ 0.07	$ 0.07	$ 0.00	$ 0.14
Diluted	0.07	0.07	0.00	0.14

5. Consolidated Statement of Cash Flows

On a consolidated basis, cash and cash equivalents include cash and due from depository institutions, interest-bearing deposits and short-term investments in money market funds**.** The Company made $445,000 in income tax payments in the first six months of 2016 and $878,000 in the same 2015 period. The Company made total interest payments of $3,947,000 in the first six months of 2016 compared to $3,453,000 in the same 2015 period. The Company had $40,000 non-cash transfers to other real estate owned (OREO) in the first six months of 2016 compared to $132,000 non-cash transfers in the same 2015 period.

6. Investment Securities

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

Investment securities available for sale (AFS):

	June 30, 2016			
	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
US Agency	$ 1,900	$ 2	$	$ 1,902
US Agency mortgage-backed securities	89,109	2,639	(25)	91,723
Corporate bonds	26,600	343	(243)	26,700
Total	$ 117,609	$ 2,984	$ (268)	$ 120,325

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

6. Investment Securities (continued)

Investment securities held to maturity (HTM):

	June 30, 2016			
	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
US Agency mortgage-backed securities	$ 12,248	$ 520	$	$ 12,768
Taxable municipal	7,131	268		7,399
Corporate bonds and other securities	6,049	48	(36)	6,061
Total	$ 25,428	$ 836	$ (36)	$ 26,228

Investment securities available for sale (AFS):

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

Investment securities held to maturity (HTM):

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

Maintaining investment quality is a primary objective of the Company's investment policy which, subject to certain limited exceptions, prohibits the purchase of any investment security below a Moody's Investor's Service or Standard & Poor's rating of A. At June 30, 2016, 79.3% of the portfolio was rated AAA as compared to 79.1% at December 31, 2015. Approximately 8.1% of the portfolio was either rated below A or unrated at June 30, 2016 as compared to 5.7% at December 31, 2015.

The Company sold $3.2 million AFS securities in the second quarter of 2016 resulting in $60,000 of gross investment security gains and sold $7.4 million AFS securities in the first half of 2016 resulting in $123,000 of gross investment security gains and $6,000 of gross investment security losses. The Company sold a $519,000 AFS security for both the second quarter and first six months of 2015 resulting in a $28,000 gross investment security gain.

The book value of securities, both available for sale and held to maturity, pledged to secure public and trust deposits, and certain Federal Home Loan Bank borrowings was $100,488,000 at June 30, 2016 and $87,096,000 at December 31, 2015.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

6. Investment Securities (continued)

The following tables present information concerning investments with unrealized losses as of June 30, 2016 and December 31, 2015 (in thousands):

Total investment securities:

	June 30, 2016					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
US Agency mortgage-backed securities	$1,612	$ (4)	$1,131	$ (21)	$2,743	$ (25)
Corporate bonds and other securities	6,445	(55)	7,775	(224)	14,220	(279)
Total	$8,057	$ (59)	$8,906	$ (245)	$16,963	$ (304)

Total investment securities:

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

The unrealized losses are primarily a result of increases in market yields from the time of purchase. In general, as market yields rise, the value of securities will decrease; as market yields fall, the fair value of securities will increase. There are 18 positions that are considered temporarily impaired at June 30, 2016. Management generally views changes in fair value caused by changes in interest rates as temporary; therefore, these securities have not been classified as other-than-temporarily impaired. Management has also concluded that based on current information we expect to continue to receive scheduled interest payments as well as the entire principal balance. Furthermore, management does not intend to sell these securities and does not believe it will be required to sell these securities before they recover in value.

Contractual maturities of securities at June 30, 2016 are shown below (in thousands). Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without prepayment penalties. The duration of the total investment securities portfolio at June 30, 2016 is 27.0 months and is lower than the duration at December 31, 2015 which was 34.2 months. The duration remains within our internal

established guideline range of 24 to 42 months which we believe is appropriate to maintain proper levels of liquidity, interest rate risk, market valuation sensitivity and profitability.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

6. Investment Securities (continued)

Total investment securities:

	June 30, 2016			
	Available for sale		Held to maturity	
	Cost Basis	Fair Value	Cost Basis	Fair Value
Within 1 year	$ 2,999	$ 3,012	$ 1,000	$ 999
After 1 year but within 5 years	9,800	9,847	2,400	2,392
After 5 years but within 10 years	34,007	34,998	8,234	8,490
After 10 years but within 15 years	36,719	37,704	4,356	4,475
Over 15 years	34,084	34,764	9,438	9,872
Total	$ 117,609	$ 120,325	$ 25,428	$ 26,228

7. Loans

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

	June 30, 2016	December 31, 2015
Commercial	$ 185,540	$ 181,066
Commercial loans secured by real estate	438,827	421,637
Real estate mortgage	248,709	257,937
Consumer	19,297	20,344
Loans, net of unearned income	$ 892,373	$ 880,984

Loan balances at June 30, 2016 and December 31, 2015 are net of unearned income of $502,000 and $557,000, respectively. Real estate-construction loans comprised 2.9% and 3.0% of total loans, net of unearned income at June 30, 2016 and December 31, 2015, respectively.

8. Allowance for Loan Losses

The following tables summarize the rollforward of the allowance for loan losses by portfolio segment for the three and six month periods ending June 30, 2016 and 2015 (in thousands).

	Three months ended June 30, 2016,				
	Balance at	Charge-Offs	Recoveries	Provision (Credit)	Balance at June 30,

	March 31, 2016				2016
Commercial	$ 3,567	$ (14)	$ 4	$ 765	$ 4,322
Commercial loans secured by real estate	3,706		8	(440)	3,274
Real estate mortgage	1,157	(8)	20	(94)	1,075
Consumer	145	(40)	6	24	135
Allocation for general risk	945			(5)	940
Total	$ 9,520	$ (62)	$ 38	$ 250	$ 9,746

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

	Three months ended June 30, 2015,				
	Balance at March 31, 2015	Charge-Offs	Recoveries	Provision (Credit)	Balance at June 30, 2015
Commercial	$ 3,157	$	$ 8	$ 6	$ 3,171
Commercial loans secured by real estate	4,087	(15)	9	59	4,140
Real estate mortgage	1,304	(188)	25	180	1,321
Consumer	191	(16)	5	21	201
Allocation for general risk	950			(66)	884
Total	$ 9,689	$ (219)	$ 47	$ 200	$ 9,717

	Six months ended June 30, 2016,				
	Balance at December 31, 2015	Charge-Offs	Recoveries	Provision (Credit)	Balance at June 30, 2016
Commercial	$ 4,244	$ (3,353)	$ 11	$ 3,420	$ 4,322
Commercial loans secured by real estate	3,449		36	(211)	3,274
Real estate mortgage	1,173	(46)	62	(114)	1,075
Consumer	151	(245)	10	219	135
Allocation for general risk	904			36	940
Total	$ 9,921	$ (3,644)	$ 119	$ 3,350	$ 9,746

	Six months ended June 30, 2015,				
	Balance at December 31, 2014	Charge-Offs	Recoveries	Provision (Credit)	Balance at June 30, 2015
Commercial	$ 3,262	$ (121)	$ 14	$ 16	$ 3,171
Commercial loans secured by real estate	3,902	(15)	51	202	4,140
Real estate mortgage	1,310	(291)	55	247	1,321
Consumer	190	(63)	14	60	201
Allocation for general risk	959			(75)	884
Total	$ 9,623	$ (490)	$ 134	$ 450	$ 9,717

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

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

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

	At June 30, 2016					
	Commercial	Commercial Loans Secured by Real Estate	Real Estate-Mortgage	Consumer	Allocation for General Risk	Total
Loans:						
Individually evaluated for impairment	$986	$ 341	$	$		$1,327
Collectively evaluated for impairment	184,554	438,486	248,709	19,297		891,046
Total loans	$185,540	$ 438,827	$248,709	$19,297		$892,373
Allowance for loan losses:						
Specific reserve allocation	$705	$ 32	$	$	$	$737
General reserve allocation	3,617	3,242	1,075	135	940	9,009
Total allowance for loan losses	$4,322	$ 3,274	$1,075	$135	$ 940	$9,746

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

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

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

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

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

interest owed. The Company does not separately evaluate individual consumer and residential mortgage loans for impairment, unless such loans are part of a larger relationship that is impaired, or are classified as a TDR.

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

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

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

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

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

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

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

	June 30, 2016				
	Impaired Loans with Specific Allowance		Impaired Loans with no Specific Allowance	Total Impaired Loans	
	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	Unpaid Principal Balance
Commercial	$ 739	$ 705	$ 247	$ 986	$ 991
Commercial loans secured by real estate	171	32	170	341	761
Total impaired loans	$ 910	$ 737	$ 417	$ 1,327	$ 1,752

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

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

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Average loan balance:				
Commercial	$ 1,020	$ 200	$ 1,103	$ 110
Commercial loans secured by real estate	352	1,509	523	1,891
Average investment in impaired loans	$ 1,372	$ 1,729	$ 1,626	$ 2,001
Interest income recognized:				
Commercial	$ 4	$ 10	$ 8	$ 11

Commercial loans secured by real estate	3	5	8	11
Interest income recognized on a cash basis on impaired loans	$ 7	$ 15	$ 16	$ 22

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

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

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

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

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

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

	June 30, 2016				
	Pass	Special Mention	Substandard	Doubtful	Total
Commercial	$ 182,450	$ 190	$ 2,196	$ 704	$ 185,540
Commercial loans secured by real estate	430,135	7,375	1,300	17	438,827
Total	$ 612,585	$ 7,565	$ 3,496	$ 721	$ 624,367

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

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

performing and non-performing outstanding balances of the residential and consumer portfolios (in thousands).

	June 30, 2016	
	Performing	Non-Performing
Real estate mortgage	$ 247,832	$ 877
Consumer	19,297	
Total	$ 267,129	$ 877

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

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

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

	June 30, 2016						
	Current	30 59 Days Past Due	60 89 Days Past Due	90 Days Past Due	Total Past Due	Total Loans	90 Days Past Due and Still Accruing
Commercial	$ 184,700	$ 70	$ 282	$ 488	$ 840	$ 185,540	$
Commercial loans secured by real estate	438,655	172			172	438,827	
Real estate mortgage	245,350	1,990	854	515	3,359	248,709	
Consumer	19,228	54	15		69	19,297	
Total	$ 887,933	$ 2,286	$ 1,151	$ 1,003	$ 4,440	$ 892,373	$

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

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

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

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

The Company uses a comprehensive methodology and procedural discipline to maintain an ALL to absorb inherent losses in the loan portfolio. The Company believes this is a critical accounting policy since it involves significant estimates and judgments. The allowance consists of three elements: 1) an allowance established on specifically identified problem loans, 2) formula driven general reserves established for loan categories based upon historical loss experience and other qualitative factors which include delinquency, non-performing and TDR loans, loan trends, economic trends, concentrations of credit, trends in loan volume,

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

8. Allowance for Loan Losses (continued)

experience and depth of management, examination and audit results, effects of any changes in lending policies, and trends in policy, financial information, and documentation exceptions, and 3) a general risk reserve which provides support for variance from our assessment of the previously listed qualitative factors, provides protection against credit risks resulting from other inherent risk factors contained in the Company s loan portfolio, and recognizes the model and estimation risk associated with the specific and formula driven allowances. The qualitative factors used in the formula driven general reserves are evaluated quarterly (and revised if necessary) by the Company s management to establish allocations which accommodate each of the listed risk factors.

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

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

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

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

	June 30, 2016	December 31, 2015
Non-accrual loans		
Commercial	$986	$4,260
Commercial loans secured by real estate	299	18
Real estate mortgage	877	1,788
Total	2,162	6,066
Other real estate owned		
Real estate-mortgage	68	75
Total	68	75
TDR s not in non-accrual		156
Total non-performing assets including TDR	$2,230	$6,297
Total non-performing assets as a percent of loans, net of unearned income, and other real estate owned	0.25 %	0.71 %

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

The following table sets forth, for the periods indicated, (1) the gross interest income that would have been recorded if

non-accrual loans had been current in accordance with their original terms and had been outstanding throughout the period or since origination if held for part of the period, (2) the amount of interest income actually recorded on such loans, and (3) the net reduction in interest income attributable to such loans (in thousands).

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Interest income due in accordance with original terms	$ 20	$ 24	$ 79	$ 48
Interest income recorded				
Net reduction in interest income	$ 20	$ 24	$ 79	$ 48

Consistent with accounting and regulatory guidance, the Bank recognizes a TDR when the Bank, for economic or legal reasons related to a borrower s financial difficulties, grants a concession to the borrower

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

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

that would not normally be considered. Regardless of the form of concession granted, the Bank s objective in offering a TDR is to increase the probability of repayment of the borrower s loan.

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

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

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

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

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

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

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

The following table details the loans modified as TDRs during the three month period ended June 30, 2016 (dollars in thousands).

Loans in non-accrual status	# of Loans	Current Balance	Concession Granted
Commercial loan	2	$ 523	Extension of maturity date

The following table details the loans modified as TDRs during the three month period ended June 30, 2015 (dollars in thousands).

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

In all instances where loans have been modified in troubled debt restructurings the pre- and post-modified balances are the same. The specific ALL reserve for loans modified as TDR s was $523,000 and $542,000 as of June 30, 2016 and 2015, respectively. All TDR s are individually evaluated for impairment and a related allowance is recorded, as needed.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

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

Once a loan is classified as a TDR, this classification will remain until documented improvement in the financial position of the borrower supports confidence that all principal and interest will be paid according to terms. Additionally, the customer must have re-established a track record of timely payments according to the restructured contract terms for a minimum of six consecutive months prior to consideration for removing the loan from non-accrual TDR status. However, a loan will continue to be on non-accrual status until, consistent with our policy, the borrower has made a minimum of an additional six consecutive monthly payments in accordance with the terms of the loan.

The Company had no loans that were classified as TDR s or were subsequently modified during each 12-month period prior to the current reporting periods, which begin January 1, 2016 and 2015 (six month periods) and April 1, 2016 and 2015 (three month periods), respectively, and that subsequently defaulted during these reporting periods.

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

Foreclosed assets acquired in settlement of loans carried at fair value less estimated costs to sell are included in the other assets on the Consolidated Balance Sheet. As of June 30, 2016 and December 31, 2015, a total of $68,000 and $75,000, respectively of residential real estate foreclosed assets were included in other assets. As of June 30, 2016, the Company had initiated formal foreclosure procedures on $244,000 of consumer residential mortgages.

10. Federal Home Loan Bank Borrowings

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

	At June 30, 2016		
Type	Maturing	Amount	Weighted Average Rate
Open Repo Plus	Overnight	$ 22,575	0.56 %
Advances	2016	11,000	0.83
	2017	12,000	1.06
	2018	12,000	1.48
	2019	8,000	1.67
	2020 and over	7,042	1.62
Total advances		50,042	1.29
Total FHLB borrowings		$ 72,617	1.06 %

Type	At December 31, 2015 Maturing	Amount	Weighted Average Rate	
Open Repo Plus	Overnight	$ 48,748	0.43	%
Advances	2016	12,000	0.81	
	2017	12,000	1.06	
	2018	12,000	1.48	
	2019	7,000	1.73	
	2020 and over	5,000	1.69	
Total advances		48,000	1.27	
Total FHLB borrowings		$ 96,748	0.85	%

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

10. Federal Home Loan Bank Borrowings (continued)

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

11. Preferred Stock

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

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

12. Accumulated Other Comprehensive Loss

The following table presents the changes in each component of accumulated other comprehensive loss, net of tax, for the three and six months ended June 30, 2016 and 2015 (in thousands):

	Three months ended June 30, 2016			Three months ended June 30, 2015		
	Net Unrealized Gains and (Losses) on Investment Securities AFS[(1)]	Defined Benefit Pension Items[(1)]	Total[(1)]	Net Unrealized Gains and (Losses) on Investment Securities AFS[(1)]	Defined Benefit Pension Items[(1)]	Total[(1)]
Beginning balance	$1,506	$(8,030)	$(6,524)	$2,072	$(8,313)	$(6,241)
Other comprehensive income (loss) before reclassifications	325	174	499	(625)	416	(209)
Amounts reclassified from accumulated	(40)		(40)	(18)		(18)

other comprehensive loss						
Net current period other comprehensive income (loss)	285	174	459	(643)	416	(227)
Ending balance	$1,791	$(7,856)	$(6,065)	$1,429	$(7,897)	$(6,468)

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

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12. Accumulated Other Comprehensive Loss (continued)

	Six months ended June 30, 2016			Six months ended June 30, 2015		
	Net Unrealized Gains and (Losses) on Investment Securities AFS[1]	Defined Benefit Pension Items[1]	Total[1]	Net Unrealized Gains and (Losses) on Investment Securities AFS[1]	Defined Benefit Pension Items[1]	Total[1]
Beginning balance	$808	$(8,363)	$(7,555)	$1,843	$(8,745)	$(6,902)
Other comprehensive income before reclassifications	1,060	507	1,567	(396)	848	452
Amounts reclassified from accumulated other comprehensive loss	(77)		(77)	(18)		(18)
Net current period other comprehensive income	983	507	1,490	(414)	848	434
Ending balance	$1,791	$(7,856)	$(6,065)	$1,429	$(7,897)	$(6,468)

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

The following table presents the amounts reclassified out of each component of accumulated other comprehensive loss for the three and six months ended June 30, 2016 and 2015 (in thousands):

Details about accumulated other comprehensive loss components	Amount reclassified from accumulated other comprehensive loss[1]		Affected line item in the consolidated statement of operations
	For the three months ended June 30, 2016	For the three months ended June 30, 2015	
Unrealized gains and losses on sale of securities			
	$(60)	$(28)	Net realized gains on investment securities
	20	10	Provision for income tax expense

	$ (40)	$ (18)	Net of tax
Total reclassifications for the period	$ (40)	$ (18)	Net income

(1) Amounts in parentheses indicate credits.

Details about accumulated other comprehensive loss components	Amount reclassified from accumulated other comprehensive loss[1] For the six months ended June 30, 2016	For the six months ended June 30, 2015	Affected line item in the consolidated statement of operations
Unrealized gains and losses on sale of securities			
	$ (117)	$ (28)	Net realized gains on investment securities
	40	10	Provision for income tax expense
	$ (77)	$ (18)	Net of tax
Total reclassifications for the period	$ (77)	$ (18)	Net income

(1) Amounts in parentheses indicate credits.

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13. Regulatory Capital

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

Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital to risk-weighted assets, Tier 1 capital to average assets, and common equity Tier I capital (as defined in the regulations) to risk-weighted assets (RWA) (as defined). Additionally under Basel III rules, the decision was made to opt-out of including accumulated other comprehensive income in regulatory capital. As of June 30, 2016, the Bank was categorized as Well Capitalized under the regulatory framework for prompt corrective action promulgated by the Federal Reserve. The Company believes that no conditions or events have occurred that would change this conclusion as of such date. To be categorized as Well Capitalized, the Bank must maintain minimum Total Capital, Common Equity Tier 1 Capital, Tier 1 Capital, and Tier 1 leverage ratios as set forth in the table. Additionally, while not a regulatory capital ratio, the Company s tangible common equity ratio was 7.72% at June 30, 2016 (in thousands, except ratios).

	At June 30, 2016					
	Company		Bank		Minimum Required For Capital Adequacy Purposes	To be Well Capitalized Under Prompt Corrective Action Regulations*
	Amount	Ratio	Amount	Ratio	Ratio	Ratio
	(In Thousands, Except Ratios)					
Total Capital (To Risk Weighted Assets)	$122,086	13.04%	$105,968	11.39%	8.63 %	10.00 %
Tier 1 Common Equity (To Risk Weighted Assets)	92,670	9.90	95,358	10.25	5.13	6.50
Tier 1 Capital (To Risk Weighted Assets)	104,046	11.11	95,358	10.25	6.63	8.00
Tier 1 Capital (To Average Assets)	104,046	9.29	95,358	8.65	4.00	5.00

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13. Regulatory Capital (continued)

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

* Applies to the Bank only.

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

14. Segment Results

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

Retail banking includes the deposit-gathering branch franchise and lending to both individuals and small businesses. Lending activities include residential mortgage loans, direct consumer loans, and small business commercial loans.

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

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14. Segment Results (continued)

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

The contribution of the major business segments to the Consolidated Statements of Operations for the three and six months ended June 30, 2016 and 2015 were as follows (in thousands):

	Three months ended June 30, 2016		Six months ended June 30, 2016		June 30, 2016
	Total revenue	Net income (loss)	Total revenue	Net income (loss)	Total assets
Retail banking	$ 6,593	$ 895	$ 12,890	$ 1,478	$ 369,270
Commercial banking	4,731	1,367	9,366	532	624,507
Trust	2,202	400	4,379	545	5,427
Investment/Parent	(1,298)	(1,300)	(2,412)	(2,460)	143,288
Total	$ 12,228	$ 1,362	$ 24,223	$ 95	$ 1,142,492

	Three months ended June 30, 2015		Six months ended June 30, 2015		December 31, 2015
	Total revenue	Net income (loss)	Total revenue	Net income (loss)	Total assets
Retail banking	$ 6,539	$ 743	$ 13,063	$ 1,402	$ 415,008
Commercial banking	4,635	1,334	9,373	2,625	589,840
Trust	2,230	396	4,397	776	5,263
Investment/Parent	(912)	(1,052)	(1,695)	(2,013)	138,386
Total	$ 12,492	$ 1,421	$ 25,138	$ 2,790	$ 1,148,497

15. Commitments and Contingent Liabilities

The Company had various outstanding commitments to extend credit approximating $166.7 million and $170.5 million along with standby letters of credit of $9.0 million and $7.5 million as of June 30, 2016 and December 31, 2015, respectively. The Company s exposure to credit loss in the event of nonperformance by the other party to these commitments to extend credit and standby letters of credit is represented by their contractual amounts. The Bank uses the same credit and collateral policies in making commitments and conditional obligations as for all other lending.

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

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16. Pension Benefits

The Company has a noncontributory defined benefit pension plan covering certain employees who work at least 1,000 hours per year. The participants shall have a vested interest in their accrued benefit after five full years of service. The benefits of the plan are based upon the employee s years of service and average annual earnings for the highest five consecutive calendar years during the final ten year period of employment. Plan assets are primarily debt securities (including US Treasury and Agency securities, corporate notes and bonds), listed common stocks (including shares of AmeriServ Financial, Inc. common stock which is limited to 10% of the plan s assets), mutual funds, and short-term cash equivalent instruments. The net periodic pension cost for the three and six months ended June 30, 2016 and 2015 were as follows (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Components of net periodic benefit cost				
Service cost	$ 368	$ 400	$ 736	$ 800
Interest cost	344	325	688	650
Expected return on plan assets	(563)	(525)	(1,126)	(1,050)
Recognized net actuarial loss	314	300	628	600
Net periodic pension cost	$ 463	$ 500	$ 926	$ 1,000

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

17. Disclosures about Fair Value Measurements

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

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

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

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

Assets and Liability Measured on a Recurring Basis

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

The following tables present the assets reported on the Consolidated Balance Sheets at their fair value as of June 30, 2016 and December 31, 2015, by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

17. Disclosures about Fair Value Measurements (continued)

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

	Fair Value Measurements at June 30, 2016 Using			
	Total	(Level 1)	(Level 2)	(Level 3)
US Agency securities	$ 1,902	$	$ 1,902	$
US Agency mortgage-backed securities	91,723		91,723	
Corporate bonds	26,700		26,700	

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

Assets Measured on a Non-recurring Basis

Loans considered impaired are loans for which, based on current information and events, it is probable that the creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. As detailed in the allowance for loan loss footnote, impaired loans are reported at fair value of the underlying collateral if the repayment is expected solely from the collateral. Collateral values are estimated using Level 3 inputs based on observable market data which at times are discounted. At June 30, 2016, impaired loans with a carrying value of $1,327,000 were reduced by a specific valuation allowance totaling $737,000 resulting in a net fair value of $590,000. At December 31, 2015, impaired loans with a carrying value of $4.5 million were reduced by a specific valuation allowance totaling $1.4 million resulting in a net fair value of $3.1 million.

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

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

	Fair Value Measurements at June 30, 2016 Using			
	Total	(Level 1)	(Level 2)	(Level 3)
Impaired loans	$ 590	$	$	$ 590
Other real estate owned	68			68

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

	Quantitative Information About Level 3 Fair Value Measurements			
June 30, 2016	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range (Wgtd Ave)
Impaired loans	$590	Appraisal of collateral(1),(3)	Appraisal adjustments(2)	15% to 20% (18%)
Other real estate owned	68	Appraisal of collateral(1),(3)	Appraisal adjustments(2) Liquidation expenses	0% to 26% (8%) 9% to 55% (16%)

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

17. Disclosures about Fair Value Measurements (continued)

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

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

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

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

DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

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

Fair values have been determined by the Company using independent third party valuations that use the best available data (Level 2) and an estimation methodology (Level 3) the Company believes is suitable for each category of financial instruments. Management believes that cash, cash equivalents, and loans and deposits with floating interest rates have estimated fair values which approximate the recorded book balances. The estimation methodologies used, the estimated fair values based on US GAAP measurements, and recorded book balances at June 30, 2016 and December 31, 2015, were as follows (in thousands):

	June 30, 2016				
	Carrying Value	Fair Value	(Level 1)	(Level 2)	(Level 3)
FINANCIAL ASSETS:					
Cash and cash equivalents	$27,018	$27,018	$27,018	$	$
Investment securities AFS	120,325	120,325		120,325	
Investment securities HTM	25,428	26,228		23,254	2,974
Regulatory stock	5,862	5,862	5,862		
Loans held for sale	3,140	3,221	3,221		
	882,627	888,533			888,533

Loans, net of allowance for loan loss and unearned income					
Accrued interest income receivable	3,286	3,286	3,286		
Bank owned life insurance	37,564	37,564	37,564		
FINANCIAL LIABILITIES:					
Deposits with no stated maturities	$651,488	$651,488	$651,488	$	$
Deposits with stated maturities	289,443	291,548			291,548
Short-term borrowings	22,575	22,575	22,575		
All other borrowings	70,372	75,988			75,988
Accrued interest payable	1,471	1,471	1,471		

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

17. Disclosures about Fair Value Measurements (continued)

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