

ACNB CORP  
Form 10-Q  
November 05, 2010

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, DC 20549

**FORM 10-Q**

(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

For the quarterly period ended **September 30, 2010**

Commission file number **0-11783**

**ACNB CORPORATION**

(Exact name of Registrant as specified in its charter)

**Pennsylvania**  
(State or other jurisdiction of  
incorporation or organization)

**23-2233457**  
(I.R.S. Employer  
Identification No.)

**16 Lincoln Square, Gettysburg, Pennsylvania**  
(Address of principal executive offices)

**17325-3129**  
(Zip Code)

Registrant's telephone number, including area code: **(717) 334-3161**

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**Common Stock, Par Value \$2.50 per Share**

(Title of class)

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 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.

Large accelerated filer

Accelerated filer

Non-accelerated filer

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 number of shares of the Registrant's Common Stock outstanding on October 29, 2010, was 5,928,343.

## PART I - FINANCIAL INFORMATION

## ACNB CORPORATION

## ITEM 1 - FINANCIAL STATEMENTS

## CONSOLIDATED STATEMENTS OF CONDITION (UNAUDITED)

Dollars in thousands, except per share data	September 30, 2010	September 30, 2009	December 31, 2009
<b>ASSETS</b>			
Cash and due from banks	\$ 15,317	\$ 14,665	\$ 17,875
Interest bearing deposits with banks	17,547	24,424	6,263
<b>Total Cash and Cash Equivalents</b>	<b>32,864</b>	39,089	24,138
Securities available for sale	205,534	214,222	209,872
Securities held to maturity, fair value \$10,844; \$10,394; \$10,334	10,048	10,060	10,057
Loans held for sale	3,761	285	145
Loans, net of allowance for loan losses \$15,278; \$10,994; \$11,981	654,542	629,764	632,706
Premises and equipment	14,344	14,811	14,760
Restricted investment in bank stocks	9,170	9,170	9,170
Investment in bank-owned life insurance	27,200	26,162	26,408
Investments in low-income housing partnerships	4,189	4,480	4,391
Goodwill	5,972	5,972	5,972
Intangible assets	3,848	4,457	4,362
Foreclosed real estate	7,934	585	6,046
Other assets	13,790	8,977	13,877
<b>Total Assets</b>	<b>\$ 993,196</b>	\$ 968,034	\$ 961,904
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>			
<b>LIABILITIES</b>			
Deposits:			
Non-interest bearing	\$ 106,087	\$ 89,001	\$ 93,829
Interest bearing	658,776	626,324	634,694
<b>Total Deposits</b>	<b>764,863</b>	715,325	728,523
Short-term borrowings	41,785	55,369	55,291
Long-term borrowings	81,611	95,396	80,294
Other liabilities	11,113	12,755	9,493
<b>Total Liabilities</b>	<b>899,372</b>	878,845	873,601
<b>STOCKHOLDERS EQUITY</b>			
Common stock, \$2.50 par value; 20,000,000 shares authorized; 5,990,943 shares issued; 5,928,343 shares outstanding	14,977	14,977	14,977

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Treasury stock, at cost (62,600 shares)	(728)	(728)	(728)
Additional paid-in capital	8,787	8,787	8,787
Retained earnings	69,035	64,977	65,623
Accumulated other comprehensive income (loss)	1,753	1,176	(356)
<b>Total Stockholders Equity</b>	<b>93,824</b>	89,189	88,303
<b>Total Liabilities and Stockholders Equity</b>	<b>\$ 993,196</b>	\$ 968,034	\$ 961,904

*The accompanying notes are an integral part of the consolidated financial statements.*

## ACNB CORPORATION

## CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

Dollars in thousands, except per share data	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
<b>INTEREST INCOME</b>				
Loans, including fees	\$ 8,976	\$ 8,989	\$ 27,247	\$ 26,922
Securities:				
Taxable	1,779	2,113	5,576	6,595
Tax-exempt	314	368	1,004	1,120
Dividends	7	8	22	30
Other	24	7	66	13
<b>Total Interest Income</b>	<b>11,100</b>	<b>11,485</b>	<b>33,915</b>	<b>34,680</b>
<b>INTEREST EXPENSE</b>				
Deposits	1,553	2,265	4,828	7,403
Short-term borrowings	25	83	98	278
Long-term borrowings	810	938	2,499	2,961
<b>Total Interest Expense</b>	<b>2,388</b>	<b>3,286</b>	<b>7,425</b>	<b>10,642</b>
<b>Net Interest Income</b>	<b>8,712</b>	<b>8,199</b>	<b>26,490</b>	<b>24,038</b>
<b>PROVISION FOR LOAN LOSSES</b>	<b>1,400</b>	<b>1,200</b>	<b>4,610</b>	<b>3,550</b>
<b>Net Interest Income after Provision for Loan Losses</b>	<b>7,312</b>	<b>6,999</b>	<b>21,880</b>	<b>20,488</b>
<b>OTHER INCOME</b>				
Service charges on deposit accounts	618	644	1,768	1,775
Income from fiduciary activities	350	265	953	761
Earnings on investment in bank-owned life insurance	252	264	759	765
Gain on life insurance proceeds			78	
Net gains on sales of securities	47	14	72	17
Impairment charges on equity securities		(522)		(522)
Service charges on ATM and debit card transactions	287	260	831	742
Commissions from insurance sales	1,137	1,336	3,740	4,265
Other	225	378	743	1,047
<b>Total Other Income</b>	<b>2,916</b>	<b>2,639</b>	<b>8,944</b>	<b>8,850</b>
<b>OTHER EXPENSES</b>				
Salaries and employee benefits	4,216	4,368	12,711	13,039
Net occupancy	520	542	1,658	1,714
Equipment	603	521	1,834	1,622
Other tax	182	200	588	554
Professional services	247	177	728	608
Supplies and postage	160	174	505	519
Marketing	72	108	281	338
FDIC and regulatory	355	346	1,061	1,622
Intangible assets amortization	161	160	482	479

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Other operating	782	784	2,412	2,348
<b>Total Other Expenses</b>	<b>7,298</b>	7,380	<b>22,260</b>	22,843
<b>Income before Income Taxes</b>	<b>2,930</b>	2,258	<b>8,564</b>	6,495
<b>PROVISION FOR INCOME TAXES</b>	<b>626</b>	361	<b>1,773</b>	1,048
<b>Net Income</b>	<b>\$ 2,304</b>	\$ 1,897	<b>\$ 6,791</b>	\$ 5,447
<b>PER SHARE DATA</b>				
Basic earnings	\$ 0.39	\$ 0.32	\$ 1.15	\$ 0.92
Cash dividends declared	\$ 0.19	\$ 0.19	\$ 0.57	\$ 0.57

*The accompanying notes are an integral part of the consolidated financial statements.*

## ACNB CORPORATION

## CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (UNAUDITED)

Nine Months Ended September 30, 2010 and 2009

Dollars in thousands	Common Stock	Treasury Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
<b>BALANCE JANUARY 1, 2009</b>	\$ 14,977	\$ (442)	\$ 8,787	\$ 62,916	\$ (1,799)	\$ 84,439
Comprehensive income:						
Net income				5,447		5,447
Other comprehensive income, net of taxes and reclassification adjustment					2,975	2,975
<b>Total Comprehensive Income</b>						<b>8,422</b>
Treasury stock purchased (27,600 shares)		(286)				(286)
Cash dividends declared				(3,386)		(3,386)
<b>BALANCE SEPTEMBER 30, 2009</b>	\$ 14,977	\$ (728)	\$ 8,787	\$ 64,977	\$ 1,176	\$ 89,189
<b>BALANCE JANUARY 1, 2010</b>	\$ 14,977	\$ (728)	\$ 8,787	\$ 65,623	\$ (356)	\$ 88,303
Comprehensive income:						
Net income				6,791		6,791
Other comprehensive income, net of taxes and reclassification adjustment					2,109	2,109
<b>Total Comprehensive Income</b>						<b>8,900</b>
Cash dividends declared				(3,379)		(3,379)
<b>BALANCE SEPTEMBER 30, 2010</b>	\$ 14,977	\$ (728)	\$ 8,787	\$ 69,035	\$ 1,753	\$ 93,824

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

## ACNB CORPORATION

## CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

Dollars in thousands	Nine Months Ended September 30,	
	2010	2009
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 6,791	\$ 5,447
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on sales of loans, property and foreclosed real estate	(68)	(508)
Earnings on investment in bank-owned life insurance	(759)	(765)
Gain on life insurance proceeds	(78)	
Gains on sales of securities	(72)	(17)
Impairment charges on equity securities		522
Depreciation and amortization	1,773	1,716
Provision for loan losses	4,610	3,550
Net amortization (accretion) of investment securities premiums (discounts)	73	(154)
(Increase) decrease in interest receivable	(296)	293
Decrease in interest payable	(129)	(163)
Mortgage loans originated for sale	(23,385)	(45,276)
Proceeds from loans sold to others	19,992	46,459
(Increase) decrease in other assets	(496)	270
Increase in other liabilities	140	1,765
<b>Net Cash Provided by Operating Activities</b>	<b>8,096</b>	<b>13,139</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from maturities of investment securities available for sale	43,996	62,387
Proceeds from sales of investment securities available for sale	6,561	2,956
Purchase of investment securities held to maturity		(10,064)
Purchase of investment securities available for sale	(41,381)	(23,341)
Net increase in loans	(29,115)	(3,086)
Purchase of bank-owned life insurance	(250)	(100)
Capital expenditures	(903)	(1,595)
Proceeds from life insurance death benefits	294	
Proceeds from sales of property and foreclosed real estate	656	151
<b>Net Cash (Used in) Provided by Investing Activities</b>	<b>(20,142)</b>	<b>27,308</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net increase in demand deposits	12,258	6,515
Net increase in time certificates of deposits and interest bearing deposits	24,082	18,513
Net decrease in short-term borrowings	(13,506)	(28,084)
Dividends paid	(3,379)	(3,386)
Purchase of treasury stock		(286)
Proceeds from long-term borrowings	22,000	68,000
Repayments on long-term borrowings	(20,683)	(79,555)
<b>Net Cash Provided by (Used in) Financing Activities</b>	<b>20,772</b>	<b>(18,283)</b>
<b>Net Increase in Cash and Cash Equivalents</b>	<b>8,726</b>	<b>22,164</b>
<b>CASH AND CASH EQUIVALENTS BEGINNING</b>	<b>24,138</b>	<b>16,925</b>



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<b>CASH AND CASH EQUIVALENTS</b>	<b>ENDING</b>	<b>\$</b>	<b>32,864</b>	<b>\$</b>	<b>39,089</b>
Interest paid		\$	7,554	\$	10,805
Incomes taxes paid		\$	2,300	\$	1,500
Loans transferred to foreclosed real estate		\$	2,669	\$	102

*The accompanying notes are an integral part of the consolidated financial statements.*

**ACNB CORPORATION**

**ITEM 1 - NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. Basis of Presentation**

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments necessary to present fairly ACNB Corporation's financial position as of September 30, 2010 and 2009, and the results of operations, changes in stockholders' equity, and cash flows for the nine months ended September 30, 2010 and 2009. All such adjustments are of a normal recurring nature.

The accounting policies followed by the Corporation are set forth in Note A to the Corporation's financial statements in the 2009 ACNB Corporation Annual Report on Form 10-K, filed with the SEC on March 12, 2010. It is suggested that these consolidated financial statements be read in conjunction with the financial statements and notes thereto included in the Corporation's Annual Report on Form 10-K. The results of operations for the three and nine month periods ended September 30, 2010, are not necessarily indicative of the results to be expected for the full year. For comparative purposes, the September 30, 2009, balances have been reclassified to conform with the 2010 presentation. Such reclassifications had no impact on net income.

The Corporation has evaluated events and transactions occurring subsequent to the balance sheet date of September 30, 2010, for items that should potentially be recognized or disclosed in the consolidated financial statements. The evaluation was conducted through the date these consolidated financial statements were issued.

By letter dated August 17, 2010, the Pennsylvania Department of Banking approved the conversion of Adams County National Bank, the wholly-owned subsidiary of ACNB Corporation, from a national banking association to a Pennsylvania state-chartered bank and trust company. The conversion of Adams County National Bank to ACNB Bank took effect on October 4, 2010. The conversion is not expected to have any material effect on the consolidated financial statements of ACNB Corporation.

**2. Earnings Per Share**

The Corporation has a simple capital structure. Basic earnings per share of common stock is computed based on 5,928,343 and 5,938,581 weighted average shares of common stock outstanding for the nine months ended September 30, 2010 and 2009, respectively, and 5,928,343 for the three months ended September 30, 2010 and 2009, respectively. The Corporation does not have dilutive securities outstanding.

**3. Retirement Benefits**

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The components of net periodic benefit costs related to the non-contributory pension plan for the three month and nine month periods ended September 30 were as follows:

In thousands	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Service cost	\$ 115	\$ 140	\$ 345	\$ 421
Interest cost	268	247	804	741
Expected return on plan assets	(304)	(241)	(912)	(723)
Recognized net actuarial loss	109	145	327	434
Other, net	13	13	39	39
<b>Net Periodic Benefit Cost</b>	<b>\$ 201</b>	<b>\$ 304</b>	<b>\$ 603</b>	<b>\$ 912</b>

The Corporation previously disclosed in its financial statements for the year ended December 31, 2009, that it expected to contribute \$1,250,000 to its pension plan in 2010. The full contribution was made to the plan during the first quarter of 2010. The Corporation reduced the benefit formula for the defined benefit pension plan effective January 1, 2010, in order to manage total benefit costs. The new formula is the earned benefit as of December 31, 2009, plus 0.75% of a participant's average monthly pay multiplied by years of benefit service earned on and after January 1, 2010, but not more than 25 years. The benefit percentage factor and maximum years of service eligible were both reduced.

#### 4. Guarantees

The Corporation does not issue any guarantees that would require liability recognition or disclosure, other than its standby letters of credit. Standby letters of credit are written conditional commitments issued by the Corporation to guarantee the performance of a customer to a third party. Generally, all letters of credit, when issued, have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as those that are involved in extending loan facilities to customers. The Corporation generally holds collateral and/or personal guarantees supporting these commitments. The Corporation had \$5,969,000 in standby letters of credit as of September 30, 2010. Management believes that the proceeds obtained through a liquidation of collateral and the enforcement of guarantees should be sufficient to cover the potential amount of future payments required under the corresponding guarantees. The current amount of the liability, as of September 30, 2010, for guarantees under standby letters of credit issued was not material.

#### 5. Comprehensive Income

The Corporation's other comprehensive income (loss) items are unrealized gains (losses) on securities available for sale and an unfunded pension liability. The components of other comprehensive income (loss) for the three month and nine month periods ended September 30 were as follows:

In thousands	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Unrealized holding gains (losses) on available for sale securities arising during the period	\$ (98)	\$ 4,320	\$ 2,901	\$ 3,530
Reclassification of (gains) losses realized in net income	(47)	508	(72)	505
Net Unrealized Gains (Losses)	(145)	4,828	2,829	4,035
Tax effect	(50)	1,641	961	1,372
	(95)	3,187	1,868	2,663
Change in pension liability	122	158	366	473
Tax effect	41	55	125	161
	81	103	241	312
<b>Other Comprehensive Income (Loss)</b>	<b>\$ (14)</b>	<b>\$ 3,290</b>	<b>\$ 2,109</b>	<b>\$ 2,975</b>



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The components of the accumulated other comprehensive income (loss), net of taxes, are as follows:

In thousands	Unrealized Gains on Securities	Pension Liability	Accumulated Other Comprehensive Income (Loss)
<b>BALANCE, SEPTEMBER 30, 2010</b>	\$ 6,074	\$ (4,321)	\$ 1,753
BALANCE, DECEMBER 31, 2009	\$ 4,206	\$ (4,562)	\$ (356)
BALANCE, SEPTEMBER 30, 2009	\$ 6,459	\$ (5,283)	\$ 1,176

6. **Segment Reporting**

Russell Insurance Group, Inc. (RIG) is managed separately from the banking segment, which includes the bank and related financial services that the Corporation offers. RIG offers a broad range of property and casualty, life and health insurance to both commercial and individual clients.

Segment information for the nine month periods ended September 30, 2010 and 2009, is as follows:

In thousands	Banking	Insurance	Intercompany Eliminations	Total
<b>2010</b>				
Net interest income and other income from external customers	\$ 31,947	\$ 3,487	\$	\$ 35,434
Income before income taxes	8,092	472		8,564
Total assets	982,840	11,939	(1,583)	993,196
Capital expenditures	887	16		903
<b>2009</b>				
Net interest income and other income from external customers	\$ 28,632	\$ 4,256	\$	\$ 32,888
Income before income taxes	5,689	806		6,495
Total assets	957,436	13,484	(2,886)	968,034
Capital expenditures	1,562	33		1,595

Segment information for the three month periods ended September 30, 2010 and 2009, is as follows:

In thousands	Banking	Insurance	Intercompany Eliminations	Total
<b>2010</b>				
Net interest income and other income from external customers	\$ 10,730	\$ 898	\$	\$ 11,628

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Income before income taxes	2,841	89		2,930
Total assets	982,840	11,939	(1,583)	993,196
Capital expenditures	240			240

**2009**

Net interest income and other income from external customers	\$	9,505	\$	1,333	\$		\$	10,838
Income before income taxes		2,070		188				2,258
Total assets		957,436		13,484		(2,886)		968,034
Capital expenditures		321		23				344

Intangible assets, representing customer lists purchased by RIG, are amortized over 10 years on a straight line basis. Goodwill is not amortized, but rather is analyzed annually for impairment. However, amortization of goodwill and intangible assets is deductible for tax purposes.

## 7. Securities

Debt securities that management has the positive intent and ability to hold to maturity are classified as held to maturity and recorded at amortized cost. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as available for sale and recorded at fair value, with unrealized gains and losses excluded from earnings and reported, net of tax, in other comprehensive income.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held to maturity and available for sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In assessing potential other-than-temporary impairment losses on debt securities, management considers (1) whether management intends to sell the security, or (2) if it is more likely than not that management will be required to sell the security before recovery, or (3) management does not expect to recover the entire amortized cost basis. In assessing potential other-than-temporary impairment for equity securities, consideration is given to management's intent and ability to hold the securities until recovery of unrealized losses. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Amortized cost and fair value at September 30, 2010, and December 31, 2009, were as follows:

In thousands	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<b>SECURITIES AVAILABLE FOR SALE</b>				
<b>SEPTEMBER 30, 2010</b>				
U.S. Government and agencies	\$ 37,273	\$ 515	\$ 17	\$ 37,771
Mortgage-backed securities - residential	111,837	6,509	40	118,306
State and municipal	34,218	1,675		35,893
Corporate bonds	11,352	479	8	11,823
CRA mutual fund	1,024	24		1,048
Stock in other banks	627	66		693
	\$ 196,331	\$ 9,268	\$ 65	\$ 205,534
<b>DECEMBER 31, 2009</b>				
U.S. Government and agencies	\$ 24,117	\$ 316	\$ 105	\$ 24,328
Mortgage-backed securities - residential	128,073	5,489	65	133,497
State and municipal	40,723	631	83	41,271
Corporate bonds	9,959	215		10,174
Stock in other banks	627		25	602
	\$ 203,499	\$ 6,651	\$ 278	\$ 209,872
<b>SECURITIES HELD TO MATURITY</b>				
<b>SEPTEMBER 30, 2010</b>				
U.S. Government and agencies	\$ 10,048	\$ 796	\$	\$ 10,844



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**DECEMBER 31, 2009**

U.S. Government and agencies	\$	10,057	\$	277	\$	\$	10,334
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At September 30, 2010, two U.S. Government and agencies had unrealized losses, and none of the securities had been in a continuous loss position for 12 months or more. These unrealized losses relate principally to changes in interest rates subsequent to the acquisition of the specific securities. None of the securities in this category had an unrealized loss that exceeded 2% of amortized cost.

At September 30, 2010, two mortgage-backed securities had unrealized losses, and none of the securities had been in a continuous loss position for 12 months or more. These unrealized losses relate principally to changes in interest rates subsequent to the acquisition of the specific securities. None of the securities in this category had an unrealized loss that exceeded 2% of amortized cost.

At September 30, 2010, one corporate bond had an unrealized loss, and this security had been in a continuous loss position for less than 12 months. This unrealized loss relates principally to changes in interest rates subsequent to the acquisition of the specific security. The security in this category had an unrealized loss that was less than 1% of amortized cost.

At December 31, 2009, two U.S. Government and agencies had unrealized losses, and none of the securities had been in a continuous loss position for 12 months or more. These unrealized losses relate principally to changes in interest rates subsequent to the acquisition of the specific securities. None of the securities in this category had an unrealized loss that exceeded 2% of amortized cost.

At December 31, 2009, six mortgage-backed securities had unrealized losses, and one of the securities had been in a continuous loss position for 12 months or more. These unrealized losses relate principally to changes in interest rates subsequent to the acquisition of the specific securities. None of the securities in this category had an unrealized loss that exceeded 2% of amortized cost.

At December 31, 2009, 17 state and municipal securities had unrealized losses, and none of the municipal securities had been in a continuous loss position for 12 months or more. In analyzing the issuer's financial condition, management considers industry analysts' reports, financial performance, and projected target prices of investment analysts within a one-year time frame. None of the securities in this category had an unrealized loss that exceeded 5% of amortized cost, and a majority had unrealized losses totaling less than 1% of amortized cost. Stock in other banks are investments in two local banks that had unrealized losses; however, their market value has diminished in line with other similar bank stocks because of the financial issues impacting the banking industry.

The fair values of securities available for sale (carried at fair value) are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or by matrix pricing (Level 2) which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific security but rather by relying on the security's relationship to other benchmark quoted prices. The Corporation uses an independent service provider to provide matrix pricing and uses the valuation of another provider to compare for reasonableness.

Management routinely sells securities from its available for sale portfolio in an effort to manage and allocate the portfolio. At September 30, 2010, management had not identified any securities with an unrealized loss that it intends to sell.

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The following table shows the Corporation's gross unrealized losses and fair value related to investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at September 30, 2010, and December 31, 2009:

In thousands	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>SECURITIES AVAILABLE FOR SALE</b>						
<b>SEPTEMBER 30, 2010</b>						
U.S. Government and agencies	\$ 1,831	\$ 17	\$	\$	\$ 1,831	\$ 17
Mortgage-backed securities - residential	3,095	40			3,095	40
Corporate bonds	992	8			992	8
	\$ 5,918	\$ 65	\$	\$	\$ 5,918	\$ 65
<b>DECEMBER 31, 2009</b>						
U.S. Government and agencies	\$ 7,953	\$ 105	\$	\$	\$ 7,953	\$ 105
Mortgage-backed securities - residential	16,426	62	482	3	16,908	65
State and municipal	7,757	83			7,757	83
Stock in other banks	602	25			602	25
	\$ 32,738	\$ 275	\$ 482	\$ 3	\$ 33,220	\$ 278

Amortized cost and fair value at September 30, 2010, by contractual maturity are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay with or without penalties.

In thousands	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
1 year or less	\$	\$	\$	\$
Over 1 year through 5 years	37,518	38,544	10,048	10,844
Over 5 years through 10 years	32,238	33,399		
Over 10 years	13,087	13,544		
Mortgage-backed securities - residential	111,837	118,306		
CRA mutual fund and stock in other banks	1,651	1,741		
	\$ 196,331	\$ 205,534	\$ 10,048	\$ 10,844

The Corporation realized gross gains of \$54,000 during the third quarter of 2010 and \$14,000 during the third quarter of 2009 and gross losses of \$7,000 during the third quarter of 2010 and \$0 during the third quarter of 2009 on sales of securities available for sale. State and municipal securities were sold during the second quarter of 2010 at a loss in order to adjust the Corporation's interest rate sensitivity, reduce exposure to geographical locations, balance the mix with other investment types, and reduce risks related to insurance coverage. For the nine month period ended September 30, 2010, the Corporation realized gross gains of \$128,000 and gross losses of \$56,000 on sales of securities available for sale. For the nine month period ended September 30, 2009 the Corporation realized \$75,000 gross gains and \$58,000 gross losses on sales of

securities available for sale.

At September 30, 2010, and December 31, 2009, securities with a carrying value of \$102,607,000 and \$96,927,000, respectively, were pledged as collateral as required by law on public and trust deposits, repurchase agreements, and for other purposes.

8. **Fair Value Measurements**

Management uses its best judgment in estimating the fair value of the Corporation's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Corporation could have realized in a sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective period and have not been reevaluated or updated for purposes of these consolidated financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each period end.

Fair value measurement and disclosure guidance defines fair value as the price that would be received to sell the asset or transfer the liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. Additional guidance is provided on determining when the volume and level of activity for the asset or liability has significantly decreased. The standard also includes guidance on identifying circumstances when a transaction may not be considered orderly.

Fair value measurement and disclosure guidance provides a list of factors that a reporting entity should evaluate to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability. When the reporting entity concludes there has been a significant decrease in the volume and level of activity for the asset or liability, further analysis of the information from that market is needed and significant adjustments to the related prices may be necessary to estimate fair value in accordance with fair value measurement and disclosure guidance.

This guidance further clarifies that when there has been a significant decrease in the volume and level of activity for the asset or liability, some transactions may not be orderly. In those situations, the entity must evaluate the weight of the evidence to determine whether the transaction is orderly. The guidance provides a list of circumstances that may indicate that a transaction is not orderly. A transaction price that is not associated with an orderly transaction is given little, if any, weight when estimating fair value.

Fair value measurement and disclosure guidance establishes a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2: Quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability.

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Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported with little or no market activity).

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An asset or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

For assets measured at fair value, the fair value measurements by level within the fair value hierarchy and the basis of measurement used at September 30, 2010, and December 31, 2009, are as follows:

In thousands	Basis	Fair Value Measurements at September 30, 2010			
		Total	Level 1	Level 2	Level 3
Securities available for sale	Recurring	\$ 205,534	\$ 1,741	\$ 203,793	\$
Impaired loans	Nonrecurring	5,358			5,358
Foreclosed real estate	Nonrecurring	7,934			7,934

In thousands	Basis	Fair Value Measurements at December 31, 2009			
		Total	Level 1	Level 2	Level 3
Securities available for sale	Recurring	\$ 209,872	\$ 602	\$ 209,270	\$
Impaired loans	Nonrecurring	4,447			4,447
Foreclosed real estate	Nonrecurring	6,046			6,046

The following table presents a reconciliation of impaired loans and foreclosed real estate measured at fair value, using significant unobservable inputs (Level 3), for the quarter ended September 30, 2010:

In thousands	Impaired Loans	Foreclosed Real Estate
<b>Balance January 1, 2010</b>	\$ 4,447	\$ 6,046
Amount charged off	(666)	(147)
Settled or otherwise removed from impaired status	(325)	(628)
Additions to impaired status	2,442	
Payments made	(151)	
Increase in valuation allowance	1,373	
Loans transferred to foreclosed real estate	(1,762)	2,663
<b>Balance September 30, 2010</b>	\$ 5,358	\$ 7,934

Accounting Standards Codification (ASC) Topic 825, *Financial Instruments*, requires disclosures about the fair value of financial instruments for interim reporting periods of publicly traded companies, as well as in annual financial statements.

The following information should not be interpreted as an estimate of the fair value of the entire Corporation since a fair value calculation is only provided for a limited portion of the Corporation's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Corporation's disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Corporation's financial instruments at September 30, 2010, and December 31, 2009:

**Cash and Cash Equivalents (Carried at Cost)**

The carrying amounts reported in the balance sheet for cash and short-term instruments approximate those assets' fair value.



## **Securities**

The fair values of securities available for sale (carried at fair value) and held to maturity (carried at amortized cost) are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or by matrix pricing (Level 2) which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific security but rather by relying on the security's relationship to other benchmark quoted prices. The Corporation uses an independent service provider to provide matrix pricing and uses the valuation of another provider to compare for reasonableness.

## **Mortgage Loans Held for Sale (Carried at Lower of Cost or Fair Value)**

The fair values of mortgage loans held for sale are determined as the par amounts to be received at settlement by establishing the respective buyer and rate in advance.

## **Loans (Carried at Cost)**

The fair values of loans are estimated using discounted cash flow analysis, as well as using market rates at the balance sheet date that reflect the credit and interest rate risk inherent in the loans. Projected future cash flows are calculated based upon contractual maturity or call dates, projected repayments, and prepayments of principal. Generally, for variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values.

## **Impaired Loans (Generally Carried at Fair Value)**

Loans for which the Corporation has measured impairment are generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements. The fair value consists of the loan balances less the valuation allowance.

## **Foreclosed Real Estate**

Fair value of real estate acquired through foreclosure is based on independent third-party appraisals of the properties. These assets are included as Level 3 fair values, based on appraisals that consider the sales prices of similar properties in the proximate vicinity.

## **Restricted Investment in Bank Stock (Carried at Cost)**

The carrying amount of required and restricted investment in correspondent bank stock approximates fair value, and considers the limited marketability of such securities.

**Accrued Interest Receivable and Payable (Carried at Cost)**

The carrying amount of accrued interest receivable and accrued interest payable approximates its fair value.

**Deposits (Carried at Cost)**

The fair values disclosed for demand deposits (e.g., interest and non-interest checking, savings, and money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (e.g., their carrying amounts). Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates currently being offered in the market on certificates to a schedule of aggregated expected monthly maturities on time deposits.

**Short-Term Borrowings (Carried at Cost)**

The carrying amounts of short-term borrowings approximate their fair values.

**Long-Term Borrowings (Carried at Cost)**

Fair values of Federal Home Loan Bank (FHLB) advances are estimated using discounted cash flow analysis, based on quoted prices for new FHLB advances with similar credit risk characteristics, terms and remaining maturity. These prices obtained from this active market represent a market value that is deemed to represent the transfer price if the liability were assumed by a third party.

**Off-Balance Sheet Credit-Related Instruments**

Fair values for the Corporation's off-balance sheet financial instruments (lending commitments and letters of credit) are based on fees currently charged in the market to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing.

Estimated fair values of financial instruments at September 30, 2010, and December 31, 2009, were as follows:

In thousands	September 30, 2010		December 31, 2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Financial assets:</b>				
Cash and due from banks	\$ 15,317	\$ 15,317	\$ 17,875	\$ 17,875
Interest bearing deposits in banks	17,547	17,547	6,263	6,263
<b>Investment securities:</b>				
Available for sale	205,534	205,534	209,872	209,872
Held to maturity	10,048	10,844	10,057	10,334
Loans held for sale	3,761	3,761	145	145
Loans, less allowance for loan losses	654,542	679,882	632,706	648,508
Accrued interest receivable	3,948	3,948	3,658	3,658
Restricted investment in bank stocks	9,170	9,170	9,170	9,170
<b>Financial liabilities:</b>				
Deposits	764,863	768,903	728,523	732,089
Short-term borrowings	41,785	41,785	55,291	55,291
Long-term borrowings	81,611	87,422	80,294	83,305
Accrued interest payable	1,993	1,993	2,122	2,122
<b>Off-balance sheet financial instruments</b>				

9. **New Accounting Pronouncements**

**ASU 2009-05**

In August 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2009-05, *Fair Value Measurements and Disclosures (Topic 820): Measuring Liabilities at Fair Value*. The amendments within ASU 2009-05 clarify that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value using one or more of the following techniques:

- A valuation technique that uses:

- a. The quoted price of the identical liability when traded as an asset.
  - b. Quoted prices for similar liabilities or similar liabilities when traded as assets.
- Another valuation technique that is consistent with the principles of Topic 820.

Two examples would be an income approach, such as a present value technique, or a market approach, such as a technique that is based on the amount at the measurement date that the reporting entity would pay to transfer the identical liability or would receive to enter into the identical liability.

When estimating the fair value of a liability, a reporting entity is not required to include a separate input or adjustment to other inputs relating to the existence of a restriction that prevents the transfer of the liability.

Both a quoted price in an active market for the identical liability at the measurement date and the quoted price for the identical liability when traded as an asset in an active market when no adjustments to the quoted price of the asset are required are Level 1 fair value measurements.

This guidance became effective January 1, 2010, and did not have a significant impact on the Corporation's financial condition or results of operations.

#### **ASU 2009-16**

In October 2009, the FASB issued ASU 2009-16, *Transfers and Servicing (Topic 860): Accounting for Transfers of Financial Assets*. This ASU amends the Codification for the issuance of FASB Statement No. 166, *Accounting for Transfers of Financial Assets - An Amendment of FASB Statement No. 140*.

The amendments in this ASU improve financial reporting by eliminating the exceptions for qualifying special-purpose entities from the consolidation guidance and the exception that permitted sale accounting for certain mortgage securitizations when a transferor has not surrendered control over the transferred financial assets. In addition, the amendments require enhanced disclosures about the risks that a transferor continues to be exposed to because of its continuing involvement in transferred financial assets. Comparability and consistency in accounting for transferred financial assets are also improved through clarifications of the requirements for isolation and limitations on portions of financial assets that are eligible for sale accounting.

This guidance became effective January 1, 2010, and did not have a significant impact on the Corporation's financial condition or results of operations.

**ASU 2010-06**

The FASB issued ASU 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*. This ASU requires some new disclosures and clarifies some existing disclosure requirements about fair value measurement as set forth in Codification Subtopic 820-10. The FASB's objective is to improve these disclosures and, thus, increase the transparency in financial reporting. Specifically, ASU 2010-06 amends Codification Subtopic 820-10 to now require:

- A reporting entity to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers; and,
- In the reconciliation for fair value measurements using significant unobservable inputs, a reporting entity should present separately information about purchases, sales, issuances and settlements.

In addition, ASU 2010-06 clarifies the requirements of the following existing disclosures:

- For purposes of reporting fair value measurement for each class of assets and liabilities, a reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities; and,
- A reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements.

ASU 2010-06 is effective for interim and annual reporting periods beginning January 1, 2010, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The Corporation adopted the required provisions of ASU 2010-06, with no significant impact on its financial condition or results of operations.

#### **ASU 2010-09**

The FASB issued ASU 2010-09, *Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements*. The amendments in the ASU remove the requirement for an SEC filer to disclose a date through which subsequent events have been evaluated in both issued and revised financial statements. Revised financial statements include financial statements revised as a result of either correction of an error or retrospective application of U.S. GAAP. The FASB also clarified that if the financial statements have been revised, then an entity that is not an SEC filer should disclose both the date that the financial statements were issued or available to be issued and the date the revised financial statements were issued or available to be issued. The FASB believes these amendments remove potential conflicts with the SEC's literature.

In addition, the amendments in the ASU require an entity that is a conduit bond obligor for conduit debt securities that are traded in a public market to evaluate subsequent events through the date of issuance of its financial statements and must disclose such date.

All of the amendments in the ASU were effective upon issuance on February 24, 2010, except for the use of the issued date for conduit debt obligors. That amendment was effective for interim or annual periods ending after June 15, 2010. The Corporation adopted the required provisions of ASU 2010-09, with no significant impact on its financial condition or results of operations.

#### **ASU 2010-18**

ASU 2010-18, *Receivables (Topic 310): Effect of a Loan Modification When the Loan Is Part of a Pool That Is Accounted for as a Single Asset*, codifies the consensus reached in Emerging Issues Task Force (EITF) Issue No. 09-1, *Effect of a Loan Modification When the Loan Is Part of a Pool That Is Accounted for as a Single Asset*. The amendments to the Codification provide that modifications of loans that are accounted for within a pool under Subtopic 310-30 do not result in the removal of those loans from the pool even if the modification of those loans would otherwise be considered a troubled debt restructuring. An entity will continue to be required to consider whether the pool of assets in which the loan is included is impaired if expected cash flows for the pool change. ASU 2010-18 does not affect the accounting for loans under the scope of Subtopic 310-30 that are not accounted for within pools. Loans accounted for individually under Subtopic 310-30 continue to be subject to the troubled debt restructuring accounting provisions within Subtopic 310-40.

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ASU 2010-18 is effective prospectively for modifications of loans accounted for within pools under Subtopic 310-30 occurring in the first interim or annual period ending on or after July 15, 2010. Early application is permitted. Upon initial adoption of ASU 2010-18, an entity may make a one-time election to terminate accounting for loans as a pool under Subtopic 310-30. This election may be applied on a pool-by-pool basis and does not preclude an entity from applying pool accounting to subsequent acquisitions of loans with credit deterioration.



The Corporation adopted the required provisions of ASU 2010-09, with no significant impact on its financial condition or results of operations.

**ASU 2010-20**

ASU 2010-20, *Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, will help investors assess the credit risk of a company's receivables portfolio and the adequacy of its allowance for credit losses held against the portfolio by expanding credit risk disclosures.

This ASU requires more information about the credit quality of financing receivables in the disclosures to financial statements, such as aging information and credit quality indicators. Both new and existing disclosures must be disaggregated by portfolio segment or class. The disaggregation of information is based on how a company develops its allowance for credit losses and how it manages its credit exposure.

The amendments in this ASU apply to all public and nonpublic entities with financing receivables. Financing receivables include loans and trade accounts receivable. However, short-term trade accounts receivable, receivables measured at fair value or lower of cost or fair value, and debt securities are exempt from these disclosure amendments.

The effective date of ASU 2010-20 differs for public and nonpublic companies. For public companies, the amendments that require disclosures as of the end of a reporting period are effective for periods ending on or after December 15, 2010. The amendments that require disclosures about activity that occurs during a reporting period are effective for periods beginning on or after December 15, 2010. For nonpublic companies, the amendments are effective for annual reporting periods ending on or after December 15, 2011.

The Corporation does not expect the adoption of this standard will have a significant impact on the Corporation's financial condition or results of operations.

**ACNB CORPORATION**

**ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**INTRODUCTION AND FORWARD-LOOKING STATEMENTS**

**Introduction**

The following is management's discussion and analysis of the significant changes in the financial condition, results of operations, capital resources, and liquidity presented in its accompanying consolidated financial statements for ACNB Corporation (the Corporation or ACNB), a financial holding company. Please read this discussion in conjunction with the consolidated financial statements and disclosures included herein. Current performance does not guarantee, assure or indicate similar performance in the future.

**Forward-Looking Statements**

In addition to historical information, this Form 10-Q contains forward-looking statements. Examples of forward-looking statements include, but are not limited to, (a) projections or statements regarding future earnings, expenses, net interest income, other income, earnings or loss per share, asset mix and quality, growth prospects, capital structure, and other financial terms, (b) statements of plans and objectives of management or the Board of Directors, and (c) statements of assumptions, such as economic conditions in the Corporation's market areas. Such forward-looking statements can be identified by the use of forward-looking terminology such as believes, expects, may, intends, will, should, anticipates, negative of any of the foregoing or other variations thereon or comparable terminology, or by discussion of strategy. Forward-looking statements are subject to certain risks and uncertainties such as local economic conditions, competitive factors, and regulatory limitations. Actual results may differ materially from those projected in the forward-looking statements. Such risks, uncertainties and other factors that could cause actual results and experience to differ from those projected include, but are not limited to, the following: the effects of the new laws and regulations, specifically the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act; ineffectiveness of the business strategy due to changes in current or future market conditions; the effects and unanticipated expenses related to the charter conversion of our subsidiary bank from a federal to a state charter; the effects of economic deterioration on current customers, specifically the effect of the economy on loan customers' ability to repay loans; the effects of competition, and of changes in laws and regulations on competition, including industry consolidation and development of competing financial products and services; interest rate movements; the inability to achieve merger-related synergies; difficulties in integrating distinct business operations, including information technology difficulties; disruption from the transaction making it more difficult to maintain relationships with customers and employees, and challenges in establishing and maintaining operations in new markets; volatilities in the securities markets; and, deteriorating economic conditions. We caution readers not to place undue reliance on these forward-looking statements. They only reflect management's analysis as of this date. The Corporation does not revise or update these forward-looking statements to reflect events or changed circumstances. Please carefully review the risk factors described in other documents the Corporation files from time to time with the Securities and Exchange Commission, including the Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, and any Current Reports on Form 8-K.

**CRITICAL ACCOUNTING POLICIES**

The accounting policies that the Corporation's management deems to be most important to the portrayal of its financial condition and results of operations, and that require management's most difficult, subjective or complex judgment, often result in the need to make estimates about the

effect of such matters which are inherently uncertain. The following policies are deemed to be critical accounting policies by management:

The allowance for loan losses represents management's estimate of probable losses inherent in the loan portfolio. Management makes numerous assumptions, estimates and adjustments in determining an adequate allowance. The Corporation assesses the level of potential loss associated with its loan portfolio and provides for that exposure through an allowance for loan losses. The allowance is established through a provision for loan losses charged to earnings. The allowance is an estimate of the losses inherent in the loan portfolio as of the end of each reporting period. The Corporation assesses the adequacy of its allowance on a quarterly basis. The specific methodologies applied on a consistent basis are discussed in greater detail under the caption, *Allowance for Loan Losses*, in a subsequent section of this Management's Discussion and Analysis of Financial Condition and Results of Operations. Regulatory agencies may require additions to the allowance as part of the examination process.

The evaluation of securities for other-than-temporary impairment requires a significant amount of judgment. In estimating other-than-temporary impairment losses, management considers various factors including the length of time the fair value has been below cost, the financial condition of the issuer, and the Corporation's intent to sell, or requirement to sell, the security before recovery of its value. Declines in fair value that are determined to be other than temporary are charged against earnings.

ASC Topic 350, *Intangibles - Goodwill and Other*, requires that goodwill is not amortized to expense, but rather that it be tested for impairment at least annually. Impairment write-downs are charged to results of operations in the period in which the impairment is determined. The Corporation did not identify any impairment on its outstanding goodwill from its most recent testing, which was performed as of December 31, 2009. If certain events occur which might indicate goodwill has been impaired, the goodwill is tested when such events occur. Other acquired intangible assets with finite lives, such as customer lists, are required to be amortized over the estimated lives. These intangibles are generally amortized using the straight line method over estimated useful lives of ten years.

## RESULTS OF OPERATIONS

### Quarter ended September 30, 2010, compared to quarter ended September 30, 2009

#### *Executive Summary*

Net income for the three months ended September 30, 2010, was \$2,304,000 compared to \$1,897,000 for the same quarter in 2009, an increase of \$407,000 or 21%. Earnings per share increased from \$0.32 in 2009 to \$0.39 in 2010. Net interest income increased \$513,000 or 6%; provision for loan losses increased \$200,000 or 17%; other income increased \$277,000 or 10%; and, other expenses decreased \$82,000 or 1%.

#### *Net Interest Income*

Net interest income totaled \$8,712,000 for the quarter ended September 30, 2010, compared to \$8,199,000 for the same period in 2009, an increase of \$513,000 or 6%. Net interest income increased due to a decrease in interest expense resulting from reductions in market rates associated with the continued low rates maintained by the Federal Reserve Bank. Alternative funding sources, such as the FHLB, and other market driver rates are factors in rates the Corporation and the local market pay for deposits. At the end of the third quarter of 2010, several of the core deposit rates continued at practical floors after the Federal Open Market Committee decreased the Federal Funds Target Rate by 400 basis points during 2008 and then maintained it at 0% to 0.25% since that time. Interest expense decreased \$898,000 or 27%. The lower funding costs were combined with lower interest income, which decreased \$385,000 or 3%. Interest income was lower as a result of investment securities paydowns that were not reinvested due to low market rates resulting from Federal Reserve buying activities. Interest income also decreased due to declines in the Federal Funds Target Rate and other market driver rates. These driver rates are indexed to a portion of the loan portfolio in a manner that a decrease in the driver rates decreases the yield on the loans at subsequent rate reset dates. For more information about interest rate risk, please refer to Item 7A - Quantitative and Qualitative Disclosures about Market Risk in the Corporation's Annual Report on Form 10-K dated December 31, 2009, and filed with the SEC on March 12, 2010. Over the longer term, the Corporation continues its strategic direction to increase asset yield and interest income by means of loan growth and rebalancing the composition of earning assets.

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The net interest spread for the third quarter of 2010 was 3.68% compared to 3.46% during the same period in 2009. The yield on interest earning assets decreased by 0.24% when comparing the third quarter of 2010 to 2009, and the cost of interest bearing liabilities decreased by 0.46%. The net interest margin was 3.85% for the third quarter of 2010 and 3.68% for the third quarter of 2009. The net interest margin improvement was mainly a result of the cost of funding decreasing at a higher rate than the rate of change in the yield on assets due to timing of repricing, local market competition, and an improvement in the mix of higher yielding loans in earning assets.

Average earning assets were \$902,702,000 during the third quarter of 2010, an increase of \$12,327,000 from the average for the third quarter of 2009. Average interest bearing liabilities were \$776,331,000 in the third quarter of 2010, an increase of \$4,478,000 from the same quarter in 2009.

### *Provision for Loan Losses*

The provision for loan losses was \$1,400,000 in the third quarter of 2010 compared to \$1,200,000 in the third quarter of 2009, an increase of \$200,000 or 17%. The increase was a result of analysis of the adequacy of the allowance for loan losses. Each quarter, the Corporation measures risk in the loan portfolio compared with the balance in the allowance for loan losses and the current evaluation factors. For more information, please refer to *Allowance for Loan Losses* in the subsequent Financial Condition section. ACNB charges confirmed loan losses to the allowance and credits the allowance for recoveries of previous loan charge-offs. For the third quarter of 2010, the Corporation had net charge-offs of \$466,000, as compared to net charge-offs of \$67,000 for the third quarter of 2009.

*Other Income*

Total other income was \$2,916,000 for the three months ended September 30, 2010, up \$277,000, or 10%, from the third quarter of 2009. Fees from deposit accounts and ATM/debit card revenue were \$905,000, an increase of \$1,000, or 0.1%, due to higher electronic transaction volume. About 57% of this revenue is overdraft-related fees. A revised federal Regulation E, which restricts how banks collect overdraft-related fees, went into effect as of August 15, 2010. The change in Overdraft-related fees from this regulation was not material. Income from fiduciary activities, which include both institutional and personal trust management services, totaled \$350,000 for the three months ended September 30, 2010, as compared to \$265,000 during the third quarter of 2009, a 32% increase as a result of higher average assets under management and higher estate settlement fees. Earnings on bank-owned life insurance decreased by \$12,000, or 5%, as a result of lower crediting rates on some policies. The Corporation's wholly-owned subsidiary, Russell Insurance Group, Inc. (RIG), saw lower revenue, decreasing \$199,000 or 15%. Revenue was constrained because of lower commissions in a soft insurance market, as well as the effects of the prolonged economic recession on business clients. The Corporation took an impairment charge of \$522,000 on two equity securities in the third quarter of 2009; no charge was necessary in the third quarter of 2010. Other income in the quarter ended September 30, 2010, was down 30%, being negatively impacted by decreased fees related to less sales of residential mortgages as a result of continued slow activity in this sector.

*Other Expenses*

The largest component of other expenses is salaries and employee benefits, which decreased by \$152,000, or 3%, when comparing the third quarter of 2010 to the same quarter a year ago. Overall, the net decrease in salaries and employee benefits was the result of:

- Decreased defined benefit pension expense due to the reduced benefit formula implemented by the Corporation on January 1, 2010, and
- Lower production-based commissions and incentives, offset by
- Increases from higher employee usage of 401(k) plan benefits (affecting the employer match), unused paid time off accruals, and payroll taxes;
- Normal merit increases to employees;
- An increase in the number of full-time equivalent employees; and,
- Increased benefit plan costs, particularly medical insurance.

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Net occupancy expense decreased \$22,000, or 4%, in part due to lower specific repair costs between the two quarters. Equipment expense increased by \$82,000, or 16%, as a result of higher maintenance and depreciation on new technology purchases necessary to meet marketplace and regulatory demands or to maintain systems reliability.

Professional services expense totaled \$247,000 during the third quarter of 2010, as compared to \$177,000 for the same period in 2009, an increase of \$70,000 or 40%. This increase was due to higher loan collection legal costs and more corporate governance work including activities related to the conversion to a state charter for the banking subsidiary in early October 2010.

Marketing expense decreased by \$36,000, or 33%. Lower marketing expense for the quarter reflects different specific promotions between the two periods.

FDIC expense for the third quarter of 2010 was \$299,000, an increase of \$5,000 from the third quarter of 2009. Both quarters reflected much higher expense required of all FDIC-insured banks to restore the deposit insurance fund due to the cost of protecting depositors' accounts at failed banks during the severe recession. At the end of the third quarter of 2009, the FDIC announced a plan in which most banks prepaid an estimated three years of regular quarterly premiums at year-end 2009, as opposed to the special assessment similar to which was levied on all insured banks in the second quarter of 2009.

The prepaid assessments did not immediately affect our earnings. ACNB recorded its prepaid assessments as a prepaid expense included in other assets as of December 30, 2009, in the amount of \$3,956,000, the date the payment was made. As of December 31, 2009, and each quarter thereafter, each institution records an expense for its regular quarterly assessment and an offsetting credit to the prepaid expense until the asset is exhausted. Once the asset is exhausted, we expect to record an accrued expense payable each quarter for the assessment payment, which would be made to the FDIC at the end of the following quarter. Even though an estimated premium is prepaid under this plan, the actual expense will vary based on several factors including quarter-end deposit levels and risk ratings.

Other operating expenses decreased by \$29,000, or less than 2%, in the third quarter of 2010, as compared to the third quarter of 2009. The decreases were over a variety of expenses including the benefit of a new internet banking vendor.

#### *Provision for Income Taxes*

The Corporation recognized income taxes of \$626,000, or 21% of pretax income, during the third quarter of 2010, as compared to \$361,000, or 16% of pretax income, during the same period in 2009. The variances from the federal statutory rate of 34% in both periods are generally due to tax-exempt income and investments in low-income housing partnerships (which qualify for federal tax credits). The effective tax rate was higher in 2010 than 2009, as taxable income increased while tax exempt income and tax credits decreased. The income tax provision during the third quarters ended September 30, 2010 and 2009, included low-income housing tax credits of \$145,000 and \$170,000, respectively.

#### **Nine months ended September 30, 2010, compared to nine months ended September 30, 2009**

#### *Executive Summary*

Net income for the nine months ended September 30, 2010, was \$6,791,000 compared to \$5,447,000 for the same period in 2009, an increase of \$1,344,000 or 25%. Earnings per share increased from \$0.92 in 2009 to \$1.15 in 2010. Net interest income increased \$2,452,000 or 10%; provision for loan losses increased \$1,060,000 or 30%; other income increased \$94,000 or 1%; and, other expenses decreased \$583,000 or 3%.

#### *Net Interest Income*

Net interest income totaled \$26,490,000 for the nine months ended September 30, 2010, compared to \$24,038,000 for the same period in 2009, an increase of \$2,452,000 or 10%. Net interest income increased due to a decrease in interest expense resulting from reductions in market rates associated with the continued weakness in broader financial markets. Several of the core deposit rates continued at practical floors after the Federal Open Market Committee decreased the Federal Funds Target Rate to a range of 0% to 0.25% in 2008. In addition, after experiencing losses of principal in equity investments, ACNB customers perhaps valued local institutions and FDIC protection over yield on their funds allocated to bank deposits, thereby lowering the cost of funds despite the increase in volume. Interest expense decreased \$3,217,000 or 30%. The decreased funding costs were partially offset by lower interest income, which decreased \$765,000 or 2%. In the nine months ended September 30, 2010, interest income increased by \$605,000, due to the interest recovery on full payoff of a loan that was in nonaccrual status in prior years. Other than this one-time interest recovery, interest income was lower as a result of investment securities maturities that were not reinvested, primarily due to record low interest yields in maturities with acceptable interest rate risk attributes. Interest income also decreased due to declines in the Federal Funds Target Rate and other market driver rates. These driver rates are indexed to a portion of the loan portfolio in



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a manner that a decrease in the driver rates decreases the yield on the loans at various rate reset dates. For more information about interest rate risk, please refer to Item 7A - Quantitative and Qualitative Disclosures about Market Risk in the Corporation's Annual Report on Form 10-K dated December 31, 2009, and filed with the SEC on March 12, 2010.

The net interest spread for the first nine months of 2010 was 3.83% (3.74% without the one-time interest recovery) compared to 3.43% during the same period in 2009. Without the one-time interest recovery, the yield on interest earning assets decreased by 0.16%, primarily due to rates resetting and new loan origination at lower rates, and the cost of interest bearing liabilities decreased by 0.55%. The net interest margin was 3.99% (3.90% without the one-time interest recovery) for the first nine months of 2010 and 3.66% for the first nine months of 2009.

Average earning assets were \$892,202,000 during the first nine months of 2010, an increase of \$7,043,000 from the average for the first nine months of 2009. Average interest bearing liabilities were \$773,749,000 in the first nine months of 2010, an increase of \$1,986,000 from the same nine months in 2009. Access to funding at favorable rates and the local market that preferred dealing with a stable local institution were factors in the increase in earning assets and local funding sources between the two periods.

*Provision for Loan Losses*

The provision for loan losses was \$4,610,000 in the first nine months of 2010, as compared to \$3,550,000 in the first nine months of 2009. The increase was a result of measured risk in the loan portfolio compared with the balance in the allowance for loan losses after the continuation of the severe recession, as well as charge-off experience in the portfolio, specific potential loss allocations attributed to impaired loans remaining in the portfolio, and the general growth in the loan portfolio. ACNB adjusts the provision for loan losses as necessary to maintain the allowance at a level deemed to meet the risk characteristics of the loan portfolio. For more information, please refer to *Allowance for Loan Losses* in the subsequent Financial Condition section. For the first nine months of 2010, the Corporation had net charge-offs of \$1,312,000, as compared to net recoveries of \$51,000 for the first nine months of 2009.

*Other Income*

Total other income was \$8,944,000 for the nine months ended September 30, 2010, up \$94,000, or 1%, from the first nine months of 2009. Fees from deposit accounts and ATM/debit card revenue were \$2,599,000, an increase of \$82,000, or 3%, due to higher electronic transaction volume. Over 50% of this revenue is overdraft-related fees. A revised federal Regulation E, which restricts how banks collect overdraft-related fees, went into effect as of August 15, 2010. The change in Overdraft-related fees from this regulation was not material. Income from fiduciary activities, which include both institutional and personal trust management services, totaled \$953,000 for the nine months ended September 30, 2010, as compared to \$761,000 during the first nine months of 2009, a 25% increase as a result of higher average assets under management and higher estate fees. Earnings and an insurance death claim gain on bank-owned life insurance increased earnings on investment in bank-owned life insurance by \$72,000, as compared to the prior year. The Corporation's insurance subsidiary, Russell Insurance Group, Inc., experienced a revenue decrease of \$525,000 or 12%. The decrease was in part due to lower amounts of contingent commissions received in the first quarter of 2010. Otherwise, revenue during the nine month period was constrained by generally lower commissions in a soft insurance market and the effects of the prolonged economic recession on business clients. The contingent or extra commission payments from insurance carriers are mostly received in the first quarter of each year, and the amount is at the discretion of various insurance carriers in accordance with applicable insurance regulations. Gains on sales of securities increased by \$55,000 as securities were sold to adjust the interest rate risk position of the portfolio. The Corporation took an impairment charge of \$522,000 on two equity securities in the third quarter of 2009; no charge was necessary in the third quarter of 2010. Other non-interest income was negatively impacted by decreased fees related to less sales of residential mortgages, reflecting continued slow activity in this sector.

*Other Expenses*

The largest component of other expenses is salaries and employee benefits, which decreased by \$328,000, or 3%, when comparing the first nine months of 2010 to the same period a year ago. Overall, the net decrease in salaries and employee benefits was the result of:

- Decreased defined benefit pension expense due to the reduced benefit formula implemented by the Corporation on January 1, 2010, and
- Lower production-based incentive compensation, offset by

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- Varying employee usage of 401(k) plan benefits, unused paid time off accruals, and payroll taxes;
- The timing and rate of normal merit increases to employees;
- An increase in the number of full-time equivalent employees; and,
- Increased benefit plan costs, particularly medical insurance.

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Net occupancy expense decreased by \$56,000, or 3%, when comparing the first nine months of 2010 to the same period a year ago due to lower specific repair costs between the two periods. Equipment expense increased by \$212,000, or 13%, as a result of maintenance and depreciation of new technology purchases.

Professional services expense totaled \$728,000 during the first nine months of 2010, as compared to \$608,000 for the same period in 2009, an increase of \$120,000 or 20%. The increase was due to higher loan collection legal costs and more corporate governance work including activities related to the conversion to a state charter for the banking subsidiary in early October 2010.

Other tax expense increased due to a refund of sales and use tax recognized in 2009. Marketing expense decreased by \$57,000, or 17%, due to the execution of general budgeted reductions in such expenditures.

FDIC expense for the first nine months of 2010 was \$897,000, a decrease of \$563,000 from the same period in 2009. The much higher expense in 2009 was a result of the special assessment required of all FDIC-insured banks to restore the deposit insurance fund due to the cost of protecting depositors' accounts at failed banks during the severe recession. At the end of the third quarter of 2009, the FDIC announced a plan in which most banks prepaid an estimated three years of regular quarterly premiums at year-end 2009, as opposed to the special assessment similar to which was levied on all insured banks in the second quarter of 2009. The prepaid assessments did not immediately affect our earnings. ACNB recorded its prepaid assessments as a prepaid expense included in other assets as of December 30, 2009, in the amount of \$3,956,000, the date the payment was made. As of December 31, 2009, and each quarter thereafter, each institution records an expense for its regular quarterly assessment and an offsetting credit to the prepaid expense until the asset is exhausted. Once the asset is exhausted, we expect to record an accrued expense payable each quarter for the assessment payment, which would be made to the FDIC at the end of the following quarter. Even though an estimated premium is prepaid under this plan, the actual expense will vary based on several factors including quarter-end deposit levels and risk ratings.

Other operating expenses increased \$68,000, or 3%, in the first nine months of 2010, as compared to the first nine months of 2009. Increased costs include higher expenses to maintain other real estate owned properties and the expense related to the conversion to a new internet banking vendor earlier in the year. These increases were partially offset by a variety of other discretionary spending cuts.

### *Provision for Income Taxes*

The Corporation recognized income taxes of \$1,773,000, or 21% of pretax income, during the first nine months of 2010, as compared to \$1,048,000, or 16% of pre-tax income, during the same period in 2009. The variances from the federal statutory rate of 34% in both periods are generally due to tax-exempt income and investments in low-income housing partnerships (which qualify for federal tax credits). The effective tax rate was higher in 2010 than 2009, as taxable income increased while tax exempt income and tax credits decreased. The income tax provision during the nine months ended September 30, 2010 and 2009, included historical and low-income housing tax credits of \$434,000 and \$509,000, respectively.

## **FINANCIAL CONDITION**

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Assets totaled \$993,196,000 at September 30, 2010, compared to \$961,904,000 at December 31, 2009, and \$968,034,000 at September 30, 2009. Average earning assets during the nine months ended September 30, 2010, increased to \$892,202,000 from \$885,159,000 during the same period in 2009. Average interest bearing liabilities increased in 2010 to \$773,749,000 from \$771,763,000 in 2009.

### *Investment Securities*

ACNB uses investment securities to generate interest and dividend income, manage interest rate risk, provide collateral for certain funding products, and provide liquidity. The contraction in the securities portfolio during 2010 and 2009 was designed to fund increased lending in the earning asset mix, but was also a result of relatively low yields available on investments within the credit quality and interest rate sensitivity targets of ACNB. The investment portfolio is comprised of U.S. Government agency, municipal, and corporate securities. These securities provide the appropriate characteristics with respect to credit quality, yield and maturity relative to the management of the overall balance sheet.

At September 30, 2010, the securities balance included a net unrealized gain of \$6,074,000, net of taxes, on available for sale securities versus a net unrealized gain of \$4,206,000, net of taxes, at December 31, 2009. The increase in fair value of securities during 2010 was a result of change in the U.S. Treasury yield curve and the spread from this yield curve required by investors on the types of investment securities that ACNB owns. Actions by the Federal Reserve to stimulate the housing market and lessen the impact of the recession are affecting the spread and currently generally increasing the value of the securities held by ACNB. The Corporation does not own investments consisting of pools of Alt A or subprime mortgages, private label mortgage-backed securities, or trust preferred investments. The fair values of securities available for sale (carried at fair value) are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or by matrix pricing (Level 2) which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific security but rather by relying on the security's relationship to other benchmark quoted prices. The Corporation uses an independent service provider to provide matrix pricing and uses the valuation of another provider to compare for reasonableness. Please refer to Note 7 - Securities in the Notes to Consolidated Financial Statements for more information on the securities portfolio and Note 8 - Fair Value Measurements in the Notes to Consolidated Financial Statements for more information about fair value.

*Loans*

Loans outstanding increased by \$29,062,000, or 5%, from September 30, 2009, to September 30, 2010, and by \$25,133,000, or 4%, from December 31, 2009, to September 30, 2010, due to increases in all categories except commercial construction loans. During the third quarter of 2010, loans secured by commercial real estate increased representing lending to support existing and new customers in its marketplace. Compared to September 30, 2009, commercial loans (including commercial real estate and construction) increased by approximately \$11,400,000 or 4%. The commercial loan increase during this period was the result of in-market lending that replaced certain commercial loans that were not renewed in the third quarter of 2009 due to potential credit risk.

Participation loans at September 30, 2010, totaled approximately \$26,800,000, a decrease of \$1,500,000 compared to September 30, 2009. Residential real estate secured lending increased by \$17,800,000, or 5%, to local borrowers for their residences or to secure small commercial purpose loans. Of the \$17,800,000 increase, \$3,500,000 were mortgage loans secured by junior liens. Home equity loans, which are also in many cases junior liens, decreased by \$1,000,000 because of refinancing into other ACNB lending products, competition from other financial institutions, and customers paying off debt in the uncertain job market and slow real estate market. Junior liens inherently have more credit risk by virtue of the fact that another financial institution generally has a superior security position in the case of foreclosure liquidation of collateral to extinguish the debt. Further, foreclosure actions could become even more prevalent in a continuation of the national or a local economic downturn. Compared to December 31, 2009, commercial loans outstanding at September 30, 2010, were up by \$13,600,000, or 5%, with growth in owner occupied commercial real estate and non-real estate secured commercial and industrial loans offsetting continued declines in real estate construction and land development loans. Management has purposely reduced lending to the construction real estate category due to the risk evident in this category. Year to date in 2010, residential real estate secured loans grew \$11,600,000, or 3%, mainly as a result of booking local residential real estate loans for residential and small business purposes.

Most of the Corporation's lending activities are with customers located within southcentral Pennsylvania and in the northern Maryland area that is contiguous to its Pennsylvania retail banking offices. This region currently and historically has lower unemployment than the U.S. as a whole. Included in commercial real estate loans are loans made to lessors of non-residential dwellings that total \$87,000,000, or 13% of total loans, at September 30, 2010. These borrowers are geographically dispersed throughout ACNB's marketplace and are leasing commercial properties to a varied group of tenants including medical offices, retail space, and recreational facilities. Because of the varied nature of the tenants, in aggregate, management believes that these loans do not present any greater risk than commercial loans in general. ACNB does not originate or hold subprime mortgages in its loan portfolio.

*Allowance for Loan Losses*

The allowance for loan losses at September 30, 2010, was \$15,278,000, or 2.28% of loans, as compared to \$10,994,000, or 1.72% of loans, at September 30, 2009, and \$11,981,000, or 1.86% of loans, at December 31, 2009. The ratio of non-performing loans plus foreclosed assets to total assets was 2.08% at September 30, 2010, as compared to 1.44% at September 30, 2009, and 2.23% at December 31, 2009.

Changes in the allowance for loan losses were as follows:

In thousands	September 30, 2010	December 31, 2009	September 30, 2009
Balance, beginning	\$ 11,981	\$ 7,393	\$ 7,393
Provision charged to operations	4,610	4,750	3,550

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Recoveries on charged-off loans		42		186		170
Loans charged-off		(1,355)		(348)		(119)
Balance, ending	\$	15,278	\$	11,981	\$	10,994

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Loans past due 90 days and still accruing were \$1,480,000 and nonaccrual loans were \$11,229,000 as of September 30, 2010. \$1,992,000 of the nonaccrual balance at September 30, 2010, were troubled debt restructured loans. Loans past due 90 days and still accruing were \$1,951,000 at September 30, 2009, while nonaccruals were \$11,397,000. Loans past due 90 days and still accruing were \$2,107,000 at December 31, 2009, while nonaccruals were \$13,308,000. \$2,360,000 of the nonaccrual balance at December 31, 2009, were troubled debt restructured loans. In addition to the non-performing loans disclosed above, total loans classified as substandard at September 30, 2010, September 30, 2009, and December 31, 2009, were approximately \$17,630,000, \$11,831,000 and \$12,071,000, respectively. Substandard loans are considered to be potential problem loans.

The increase in non-performing loans coincided with the onset of the sharp recession in the second half of 2008. A better understanding of the trends of the non-performing loans is obtained by a comparison back to that time period. Information on nonaccrual loans at September 30, 2010, compared to the year-ends of 2009 and 2008, is as follows:

Dollars in thousands	Number of Credit Relationships	Balance	Current Specific Loss Allocations	Current Year Charge-Offs	Location	Originated
<b>SEPTEMBER 30, 2010</b>						
Residential real estate developments	4	\$ 5,457	\$ 1,808		In market	2006-2008
Economic development project *				601	In market	2007
Owner occupied commercial real estate	12	3,483	23	30	In market	1998-2008
Investment/rental commercial real estate	4	1,205	444	178	In market	2004-2007
Commercial & industrial	2	1,084	586		In market	2007
<b>Total</b>	<b>22</b>	<b>\$ 11,229</b>	<b>\$ 2,861</b>	<b>\$ 809</b>		

\* Transferred to other real estate owned in the second quarter of 2010.

Dollars in thousands	Number of Credit Relationships	Balance	Current Specific Loss Allocations	Current Year Charge-Offs	Location	Originated
<b>DECEMBER 31, 2009</b>						
Residential real estate developments	2	\$ 5,419	\$ 1,375		In market	2006
Economic development project	1	1,848	997		In market	2007
Owner occupied commercial real estate	7	3,267	43		In market	1998-2008
Investment/rental commercial real estate	3	1,584	857		In market	2004-2007
Commercial & industrial	2	1,190	675		In market	2007
<b>Total</b>	<b>15</b>	<b>\$ 13,308</b>	<b>\$ 3,947</b>	<b>\$</b>		

**DECEMBER 31, 2008**

Residential real estate developments	2	\$ 5,712	\$ 1,398	\$ 2,765	In market	2006
Owner occupied commercial real estate	2	741			In market	1998-2006



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Commercial & industrial	1		1,270		683		1,000	In market	2007
<b>Total</b>	5	\$	7,723	\$	2,081	\$	3,765		

All nonaccrual impaired loans are to borrowers located within the market area served by the Corporation in southcentral Pennsylvania and nearby areas of northern Maryland. All nonaccrual impaired loans were originated by ACNB's banking subsidiary between 1998 and 2008 for purposes listed in the classifications in the tables above.

At September 30, 2010, the Corporation had four impaired loans to unrelated borrowers totaling \$5,457,000 to finance residential real estate development construction projects in the Corporation's primary trading area of southcentral Pennsylvania. All four are in nonaccrual of interest status. The loans have standard terms and conditions including repayment from the sales of the respective properties. The loans were originated during the first half of 2006 through 2008. One loan, which was extended by receipt of required payments in 2009, was placed in nonaccrual because of the inability of the borrower to fund the necessary infrastructure improvements. On a second loan, foreclosure has been held in abeyance while allowing the borrower to pursue a workout plan to sell individual units of the property. The total outstanding on these two loans is \$5,013,000. The total specific valuation allowance on the two larger unrelated credits is \$1,705,000, which is net of charge-offs of \$2,765,000 taken in 2008. The respective allowances were derived by estimating the cash flow from the sale of the property given the respective stage of completion and/or the zoning without required infrastructure. Two smaller unrelated credits total \$444,000 with specific valuation allowances of \$103,000. The proceeds of these loans were used to build a speculation house in the case of one borrower and to improve infrastructure in the case of the other borrower.

A local economic development corporation loan, originated in the third quarter of 2007 and in the total amount of \$2,172,000, was added to nonaccrual status when the loan matured with various sales agreements and grants pending. Subsequent payment reduced the balance to \$1,847,000. The foreclosure process commenced in the fourth quarter of 2009, and the sheriff sale in the second quarter of 2010 resulted in ACNB protecting its interest with a fair value bid. Subsequently, the resulting other real estate owned property was written down to fair value, less costs to sell, with a charge-off of \$601,000 as determined at the time the property was acquired. The property remained as other real estate owned at September 30, 2010.

Owner occupied commercial real estate includes 12 loan relationships totaling less than \$1,000,000 each in outstanding balance in which the real estate is collateral and is used in connection with a business enterprise that is suffering economic stress or is out of business. These loans were originated between 1998 and 2008. The two largest loans total \$1,760,000 to unrelated business enterprises and each have fair values in excess of the loan amount. In general, these two businesses have been affected by specific factors other than the current economic conditions and these factors were not known until the fourth quarter of 2009 when they became delinquent and announced that further payments would not be made. The plan to foreclose through the sheriff sale process in the first half of 2010 was stayed by the borrower's legal action in one case and the other loan was brought current by the borrower. The sheriff sale was extended by further legal action by the borrower in the third quarter. The other smaller loans in this category are business loans impacted by the general economic downturn. Collection efforts will continue until it is deemed in the best interest of ACNB to initiate foreclosure procedures. Two loans in this category have specific allocations totaling \$23,000 based on the fair value.

Investment/rental commercial real estate includes four unrelated loan relationships totaling less than \$1,000,000 each in outstanding balance in which the real estate is collateral and is used for speculation, rental, or other non-owner occupied uses. These loans were originated between 2004 and 2007, and were affected by the lack of borrower cash flow to continue to service the debt. The plan is to foreclose and subsequently market the real estate if ongoing workout efforts are not successful. Two loans currently in the foreclosure process have specific allocations totaling \$444,000 based on the fair value. A loan previously in this category was settled with a charge-off of \$65,000, during the second quarter of 2010, as compared to a specific allocation in the allowance for loan losses of \$55,000 at December 31, 2009. Another loan previously in this category was moved to other real estate owned with a charge to the allowance for loan losses of \$113,000 based on the fair value less costs to sell. In this case, the previous specific allocation was \$259,000.

Also included in impaired loans are related term loans and a fully-disbursed line of credit, all originated in the second quarter of 2007 for a start-up enterprise in the food industry in southcentral Pennsylvania, that total \$996,000 with a specific valuation allowance of \$568,000 which is net of a \$1,000,000 charge-off taken in 2008. These loans, with standard terms and conditions including repayment from conversion of trade

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assets, are under a forbearance agreement and in nonaccrual status. The valuation allowance on this set of loans was derived by estimating the cash flow from the liquidation of personal and business assets pledged as collateral. Forbearance agreement payments are currently being made in a timely manner. These loan relationships are classified as commercial and industrial loans.

The following is a summary of information pertaining to impaired loans at September 30, 2010, December 31, 2009, and December 31, 2008:

In thousands	September 30, 2010	December 31, 2009	December 31, 2008
Impaired loans with a valuation allowance	\$ 8,219	\$ 8,394	\$ 5,047
Impaired loans without a valuation allowance	\$ 3,010	\$ 4,914	\$ 4,187
Valuation allowance related to impaired loans	\$ 2,861	\$ 3,947	\$ 2,081

At June 30, 2010, ACNB added a commercial loan general pool allowance consisting of participation loans in its calculation of the adequacy of the allowance for loan losses. These loans were previously included in various other commercial loan pools in the calculation. The reason for the change was increased risk represented by these loans based on the geographic locations that are generally in the Harrisburg/Lancaster, Pennsylvania, market and because of the reliance on legal actions and collection efforts of the originating bank at September 30, 2010. The amount of allowance for loan loss was assigned at \$1,744,000 on approximately \$27,000,000 in outstanding balances. The establishment of this pool was a primary reason that the provision for loan losses expense increased to \$4,610,000 year-to-date 2010, as compared to provision expense of \$3,550,000 year-to-date 2009.

As detailed above, the Corporation utilizes a systematic review of its loan portfolio on a quarterly basis in order to determine the adequacy of the allowance for loan losses. In addition, ACNB engages the services of an outside loan review function and sets the timing and coverage of loan reviews during the year. The results of this independent loan review are included in the systematic review of the loan portfolio. The allowance for loan losses includes a component for individual loan impairment, primarily based on the loan's collateral fair value and expected cash flow. A watch list of loans is identified for evaluation based on internal and external loan grading and reviews. Loans other than those determined to be impaired are grouped into pools of loans with similar credit risk characteristics. These loans are evaluated as groups with allocations made to the allowance based on historical loss experience adjusted for current trends in delinquencies, trends in underwriting and oversight, concentrations of credit, and general economic conditions within the Corporation's trading area. Regulatory agencies may require additions to the allowance as part of the examination process.

The allocation of the allowance for loan losses between the various loan categories is consistent with the change in estimated specific losses measured at each period-end and the historical net loss experience in each of the categories. An unallocated portion of the allowance reflects estimated inherent losses within the portfolio that have not been detected. The unallocated portion of this reserve exists due to risk of error in the specific and general reserve allocations, as well as to allow for consumer and small business loans with demonstrated weaknesses where it is not practicable to develop specific allocations, variances in management's assessment of national and local economic conditions, and other internal and external factors that management believes appropriate at the time. While management believes ACNB's allowance for loan losses is adequate based on information currently available, future adjustments to the reserve may be necessary due to changes in economic conditions and management's assumptions as to future delinquencies or loss rates.

#### *Foreclosed Real Estate*

Foreclosed real estate consists of the fair value of real estate acquired through foreclosure on real estate loan collateral or the acceptance of ownership of real estate in lieu of the foreclosure process. Fair values are based on appraisals that consider the sales prices of similar properties in the proximate vicinity less estimated selling costs. At September 30, 2010, ACNB owned \$7,934,000 in foreclosed assets held for resale, as compared to \$6,046,000 and \$585,000 at December 31, 2009, and September 30, 2009, respectively. Of the September 30, 2010 total, \$5,181,000 is a commercial property located in Lancaster, Pennsylvania, on which a valid sales agreement is in place and awaiting funding arrangements to be executed. Another commercial property is valued at \$1,246,000 that was previously the local development corporation project that was acquired through the sheriff sale process in the second quarter of 2010. This property is being marketed to appropriately targeted buyers for such properties. Another \$657,000 is the value of four commercial properties that are being marketed through appropriate means. Four residential real estate properties totaling \$850,000 are being marketed through realtors or ACNB staff as appropriate.

*Deposits*

ACNB continues to rely on deposits as a primary source of funds for lending activities with total deposits of \$764,863,000 as of September 30, 2010. Deposits increased by \$49,538,000, or 7%, from September 30, 2009, to September 30, 2010, and by \$36,340,000, or 5%, from December 31, 2009, to September 30, 2010. ACNB's deposit pricing function employs a disciplined pricing approach based upon alternative funding rates, but also strives to price deposits to be competitive with relevant local competition, including credit unions and larger regional banks. During the ongoing recession, deposit growth mix experienced a shift to transaction accounts as customers put more value in liquidity and FDIC insurance. Products, such as money market accounts and interest-bearing transaction accounts, that had suffered declines in recent years regained balances. With continued low market interest rates in a recession economy, ACNB's ability to maintain and add to its deposit base may be impacted by the reluctance of consumers to accept low rates and by competition willing to pay above market rates to attract market share. Alternatively, if rates rise rapidly and the equity markets improve, funds could leave the Corporation or be priced higher to maintain the deposits.

### *Borrowings*

Short-term borrowings are comprised primarily of securities sold under agreements to repurchase (accounted for as collateralized financing transactions) and short-term borrowings at the Federal Home Loan Bank (FHLB). Investment securities are pledged in sufficient amounts to collateralize repurchase agreements. As of September 30, 2010, short-term borrowings were \$41,785,000, as compared to \$55,291,000 at December 31, 2009, and \$55,369,000 at September 30, 2009. In comparison to year-end 2009, repurchase agreement balances were down \$8,097,000 due to seasonal fluctuations in the business activities of ACNB's commercial customer base and there were no short-term FHLB borrowings at the end of third quarter of 2010 compared to \$5,150,000 at year-end 2009. The decrease from the end of the third quarter of 2009 in short-term borrowings was due to lower FHLB borrowings and lower balances in repurchase agreements. Long-term borrowings consist primarily of advances from the FHLB. Long-term borrowings totaled \$81,611,000 at September 30, 2010, versus \$80,294,000 at December 31, 2009, and \$95,396,000 at September 30, 2009. Compared to December 31, 2009, the Corporation increased long-term borrowings by borrowing FHLB advances for longer, laddered terms between two and six years as a measure of protection against the possibility of higher interest rates in future periods.

### *Capital*

ACNB's capital management strategies have been developed to provide an appropriate rate of return to stockholders, while maintaining higher than a regulatory well-capitalized position. Total stockholders' equity was \$93,824,000 at September 30, 2010, compared to \$88,303,000 at December 31, 2009, and \$89,189,000 at September 30, 2009. Stockholders' equity increased in the first nine months of 2010 by \$5,521,000 due to \$3,412,000 in earnings retained in capital and an increase in accumulated other comprehensive income primarily due to the rise in the fair value of the investment portfolio. Other comprehensive income or loss is mainly caused by fixed-rate investment securities gaining or losing value in different interest rate environments and changes in the net funded position of the defined benefit pension plan.

The primary source of additional capital to ACNB is earnings retention, which represents net income less dividends declared. During the first nine months of 2010, ACNB earned \$6,791,000 and paid dividends of \$3,379,000 for a dividend payout ratio of 50%. During the first nine months of 2009, ACNB earned \$5,447,000 and paid dividends of \$3,386,000 for a dividend payout ratio of 62%.

ACNB is subject to various regulatory capital requirements administered by the federal banking agencies. 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 ACNB. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, ACNB must meet specific capital guidelines that involve quantitative measures of its assets and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Regulators, at their discretion, can impose higher capital requirements.

Quantitative measures established by regulation to ensure capital adequacy require ACNB and its banking subsidiary to maintain minimum amounts and ratios of total and Tier 1 capital to average and risk-weighted assets.

### *Risk-Based Capital*

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The banking subsidiary's capital ratios are as follows:

	September 30, 2010	December 31, 2009	Well Capitalized
Tier 1 leverage ratio (to average assets)	<b>8.18%</b>	8.05%	5.00%
Tier 1 risk-based capital ratio (to risk-weighted assets)	<b>11.92%</b>	11.85%	6.00%
Total risk-based capital ratio	<b>13.18%</b>	13.11%	10.00%

### *Liquidity*

Effective liquidity management ensures the cash flow requirements of depositors and borrowers, as well as the operating cash needs of ACNB, are met.

ACNB's funds are available from a variety of sources, including assets that are readily convertible to cash, maturities and repayments from the securities portfolio, scheduled repayments of loans receivable, the core deposit base, and the ability to borrow from the FHLB. At September 30, 2010, ACNB's banking subsidiary had a borrowing capacity of approximately \$279,010,000 from the FHLB, of which \$200,010,000 was available. Because of various restrictions and requirements on utilizing the available balance, ACNB considers \$61,000,000 to be the practicable additional borrowing capacity, which is considered to be sufficient for operational needs. In addition, ACNB's Liquidity and Contingency Liquidity Policy Statement identifies additional sources of contingency liquidity. Since the second half of 2008, financial institutions have experienced difficulties in bank-to-bank liquidity worldwide. ACNB has been insulated from the freeze in credit markets by its relationship with the FHLB, a government-sponsored enterprise regulated by the Federal Housing Finance Agency. The FHLB system is self-capitalizing, member-owned, and its member banks' stock is not publicly traded. ACNB creates its borrowing capacity with the FHLB by granting a security interest in certain loan assets with requisite credit quality. ACNB has reviewed recent information on the FHLB system and the FHLB of Pittsburgh, and has concluded that they have the capacity and intent to continue to provide both operational and contingency liquidity. In 2009, the FHLB of Pittsburgh instituted a requirement that a member's investment securities must be moved into a safekeeping account under FHLB control to be considered in the calculation of maximum borrowing capacity. The Corporation currently has securities in safekeeping at the FHLB of Pittsburgh; however, the safekeeping account is under the Corporation's control. As better contingent liquidity is maintained by keeping the securities under the Corporation's control, the Corporation has not moved the securities which, in effect, lowers the Corporation's maximum borrowing capacity. However, there is no practical reduction in borrowing capacity as the securities can be moved into the FHLB-controlled account on any day they are needed for borrowing purposes.

Another source of liquidity is securities sold under repurchase agreements to customers of ACNB's banking subsidiary totaling approximately \$41,000,000 and \$49,000,000 at September 30, 2010, and December 31, 2009, respectively. These agreements vary in balance according to the cash flow needs of customers and competing accounts at other financial organizations.

The liquidity of the parent company, ACNB Corporation, also represents an important aspect of liquidity management. The parent company's cash outflows consist principally of dividends to stockholders and corporate expenses. The main source of funding for the parent company is the dividends it receives from its banking subsidiary. Federal and state banking regulations place certain restrictions on dividends paid to the parent company from subsidiary banks. The maximum amount of dividends that may be paid from the subsidiary bank to ACNB was \$6,231,000 at September 30, 2010.

ACNB manages liquidity by monitoring projected cash inflows and outflows on a daily basis, and believes it has sufficient funding sources to maintain sufficient liquidity under varying degrees of business conditions.

In March 2010, the Interagency Policy Statement on Funding and Liquidity Risk Management was issued to be effective in May 2010. This directive, issued jointly by all banking regulators, has an effect on balance sheet management and reporting requirements. Key points of the new policy statement emphasize regulatory expectations of a shift from bank liquidity based off of borrowing capacity to perhaps more holdings of unencumbered liquid assets, depending on the complexity, capital and growth profile of each institution. Funding provided by borrowings needs to be prudent in amount and diversified in source and terms. Finally, liquidity processes need to be managed by bank-specific funding plans and policies, as well as regularly tested. ACNB has studied these directives to analyze any variances from current practices and policies, and concluded the Corporation to be in substantial compliance.

#### *Off-Balance Sheet Arrangements*

The Corporation is party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and, to a lesser extent, standby letters of credit. At September 30, 2010, the Corporation had unfunded outstanding commitments to extend credit of approximately \$120,762,000 and outstanding standby letters



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of credit of approximately \$5,969,000. Because these commitments generally have fixed expiration dates and many will expire without being drawn upon, the total commitment level does not necessarily represent future cash requirements.

### *Market Risks*

Financial institutions can be exposed to several market risks that may impact the value or future earnings capacity of the organization. These risks involve interest rate risk, foreign currency exchange risk, commodity price risk, and equity market price risk. ACNB's primary market risk is interest rate risk. Interest rate risk is inherent because, as a financial institution, ACNB derives a significant amount of its operating revenue from purchasing funds (customer deposits and wholesale borrowings) at various terms and rates. These funds are then invested into earning assets (primarily loans and investments) at various terms and rates.

## RECENT DEVELOPMENTS

**DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT** - On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Act will result in sweeping financial regulatory reform aimed at strengthening the nation's financial services sector.

The Act's provisions that have received the most public attention generally have been those applying to larger institutions or institutions that engage in practices in which the Corporation does not engage. These provisions include growth restrictions, credit exposure limits, higher prudential standards, prohibitions on proprietary trading, and prohibitions on sponsoring and investing in hedge funds and private equity funds.

However, the Act contains numerous other provisions that likely will directly impact ACNB and its banking subsidiary. These include increased fees payable by banks to regulatory agencies, new capital guidelines for banks and bank holding companies, permanently increasing the FDIC insurance coverage from \$100,000 to \$250,000 per depositor, new liquidation procedures for banks, new regulations affecting consumer financial products, new corporate governance disclosures and requirements, and the increased cost of supervision and compliance more generally. Many aspects of the law are subject to rulemaking by various government agencies and will take effect over several years. This timetable, combined with the Act's significant deference to future rulemaking by various regulatory agencies, makes it difficult for us to anticipate the Act's overall financial, competitive and regulatory impact on the Corporation, its customers, and the financial industry more generally. However, the increased cost of compliance with subsequent regulations may have an adverse effect on future operations.

**FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC) INSURANCE ASSESSMENTS** - The subsidiary bank is subject to deposit insurance assessments by the FDIC. The assessments are based on the risk classification of the depository institution. The subsidiary bank was required to pay regular FDIC insurance assessments in 2009 of \$1,743,000 and a special assessment on September 30, 2009, of \$437,000. Furthermore, on December 31, 2009, all insured institutions were required to prepay 3.25 years of regular quarterly premiums. Each institution recorded the entire amount of its prepaid assessment as a prepaid expense (an asset). ACNB recorded its prepaid assessment in the amount of \$3,596,000 as a prepaid expense included in other assets as of December 30, 2009. As of December 31, 2009, and each quarter thereafter, each institution records an expense, as a charge to earnings, for its regular quarterly assessment for the quarter and an offsetting credit to the prepaid assessment until the asset is exhausted. Once the asset is exhausted, the institution records an accrued expense payable each quarter for the assessment payment, which is paid in arrears to the FDIC at the end of the following quarter. If the prepaid assessment is not exhausted by December 30, 2014, any remaining amount will be returned to the depository institution. The FDIC also has adopted a uniform three basis point increase in assessment rates effective January 1, 2011.

**EMERGENCY ECONOMIC STABILIZATION ACT OF 2008 AND AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009** - In response to the financial crises affecting the banking system and financial markets and going concern threats to investment banks and other financial institutions, on October 3, 2008, the Emergency Economic Stabilization Act of 2008 (EESA) was signed into law and subsequently amended by the American Recovery and Reinvestment Act of 2009 on February 17, 2009. Under the authority of the EESA, as amended, the United States Department of the Treasury (Treasury) created the Troubled Asset Relief Program (TARP) Capital Purchase Program and through this program invested in financial institutions by purchasing preferred stock and warrants to purchase either common stock or additional shares of preferred stock. As of December 31, 2009, the Treasury will not make additional investments under the TARP Capital Purchase Program, but is considering continuing a similar program for banks under \$10 billion in assets under a different program.

**FASB PROPOSALS** - On May 26, 2010, the Financial Accounting Standards Board (FASB) issued an exposure draft that proposes to dramatically overhaul financial instrument accounting. The changes would affect how banks account for a wide range of financial instruments, including investments in debt and equity securities, loans, deposits and borrowings. The proposed requirements affect the classification and measurement of financial instruments and the recognition and measurement of impairment losses on financial assets. Financial asset categories

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would be reduced to two categories: (1) fair value through net income and (2) fair value through other comprehensive income (OCI). Financial liabilities would be reduced to four categories: (1) fair value through net income, (2) fair value through OCI, (3) amortized cost and (4) remeasurement value (for core deposit liabilities). Principally all financial assets and most financial liabilities would be measured at fair value on the balance sheet. Further, some financial assets and liabilities would display both amortized cost and fair value amounts on the face of the balance sheet. Loans held to collect contractual cash flows are an example. A separate companion exposure draft proposes to require companies to display net income and OCI on one single statement of comprehensive income. As a result, the income statement would become the statement of comprehensive income (SCI).

Comprehensive income is defined as net income plus OCI. Currently, OCI items bypass net income and are recorded as a separate component of equity in the balance sheet. The effective date for this proposal has not been set. The comment period for the exposure draft ended on September 30, 2010.

ACNB believes that the proposal does not reflect the business cycle of a community bank, it would be implemented inconsistently, and, most importantly, it would negatively affect the ability to serve community bank customers. Loans held to collect contractual cash flows is the primary earning asset of a community bank. These loans are underwritten to the specific attributes of the local market and the specific local customers, which generally cannot be valued efficiently such as is the case with equity and debt securities and more homogeneous loans such as residential mortgages underwritten to be sold into a secondary market. Loans that cannot be valued easily generally will reflect a discount in such measurements. The expected result of the proposal could be a combination of fewer loans written to support local businesses, higher interest rates charged, and shorter fixed-rate terms offered.

### **ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Management monitors and evaluates changes in market conditions on a regular basis. Based upon the most recent review, management has determined that there have been no material changes in market risks since year-end. For further discussion of year-end information, please refer to the Annual Report on Form 10-K for the fiscal year ended December 31, 2009.

### **ITEM 4 - CONTROLS AND PROCEDURES**

#### **EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES**

As of the end of the period covered by this report, the Corporation carried out an evaluation, under the supervision and with the participation of the Corporation's management, including the Corporation's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Corporation's disclosure controls and procedures pursuant to the Securities Exchange Act of 1934 (Exchange Act) Rule 13a-15(e). Based upon that evaluation, the Corporation's Chief Executive Officer along with the Corporation's Chief Financial Officer concluded that the Corporation's disclosure controls and procedures are effective.

Disclosure controls and procedures are Corporation controls and other procedures that are designed to ensure that information required to be disclosed by the Corporation in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

There were no changes in the Corporation's internal control over financial reporting during the fiscal quarter ended September 30, 2010, that has materially affected, or is reasonably likely to materially affect, the internal control over financial reporting.

### **ITEM 4T - CONTROLS AND PROCEDURES**

Not Applicable.

**PART II - OTHER INFORMATION**

**ACNB CORPORATION**

**ITEM 1 - LEGAL PROCEEDINGS**

As of September 30, 2010, there were no material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which ACNB or its subsidiaries are a party or by which any of their property is the subject. In addition, no material proceedings are pending or are known to be threatened or contemplated against the Corporation or its subsidiaries by governmental authorities.

**ITEM 1A - RISK FACTORS**

Management has reviewed the risk factors that were previously disclosed in the Annual Report on Form 10-K for the fiscal year ended December 31, 2009. It was determined that there are no material changes from the risk factors as previously disclosed in the Form 10-K.

**ITEM 2 - UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

On November 3, 2008, the Corporation announced a plan to purchase up to 120,000 shares of its outstanding common stock. There were no treasury shares purchased under this plan during the quarter ended September 30, 2010. The maximum number of shares that may yet be purchased under this stock repurchase plan is 57,400.

On May 5, 2009, stockholders approved and ratified the ACNB Corporation 2009 Restricted Stock Plan, effective as of February 24, 2009, which awards shall not exceed, in the aggregate, 200,000 shares of common stock. As of September 30, 2010, there were no shares of common stock granted as restricted stock awards to either employees or directors.

On May 5, 2009, stockholders approved and adopted the amendment to the Articles of Incorporation of ACNB Corporation to authorize up to 20,000,000 shares of preferred stock, par value \$2.50 per share. As of September 30, 2010, there were no issued or outstanding shares of preferred stock.

**ITEM 3 - DEFAULTS UPON SENIOR SECURITIES - NOTHING TO REPORT.**

**ITEM 4 - (REMOVED AND RESERVED).**

**ITEM 5 - OTHER INFORMATION - NOTHING TO REPORT.**

**ITEM 6 - EXHIBITS**

The following exhibits are included in this report:

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- Exhibit 3(i) Articles of Incorporation of ACNB Corporation, as amended. (Incorporated by reference to Exhibit 3.1 of the Registrant's Current Report on Form 8-K, filed with the Commission on June 2, 2009.)
- Exhibit 3(ii) Bylaws of ACNB Corporation, as amended. (Incorporated by reference to Exhibit 3.2 of the Registrant's Current Report on Form 8-K, filed with the Commission on March 22, 2010.)
- Exhibit 10.1 ACNB Corporation, ACNB Acquisition Subsidiary LLC, and Russell Insurance Group, Inc. Stock Purchase Agreement. (Incorporated by reference to Exhibit 10.2 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2004, filed with the Commission on March 15, 2005.)
- Exhibit 10.2 Salary Continuation Agreement - Applicable to Ronald L. Hankey, Thomas A. Ritter and Lynda L. Glass. (Incorporated by reference to Exhibit 10.2 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2008, filed with the Commission on March 13, 2009.)
- Exhibit 10.3 Executive Supplemental Life Insurance Plan - Applicable to Ronald L. Hankey, Thomas A. Ritter, David W. Cathell and Lynda L. Glass. (Incorporated by reference to Exhibit 10.3 of the Registrant's Quarterly Report on Form 10-Q for the period ended September 30, 2008, filed with the Commission on November 7, 2008.)
- Exhibit 10.4 Director Supplemental Life Insurance Plan - Applicable to Frank Elsner III, James J. Lott, Robert W. Miller, Daniel W. Potts, Marian B. Schultz, David L. Sites, Alan J. Stock, Jennifer L. Weaver, Harry L. Wheeler and James E. Williams. (Incorporated by reference to Exhibit 10.5 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2004, filed with the Commission on March 15, 2005.)
- Exhibit 10.5 Director Deferred Fee Plan - Applicable to Frank Elsner III, James J. Lott, Robert W. Miller, Marian B. Schultz, Alan J. Stock, Jennifer L. Weaver, Harry L. Wheeler and James E. Williams. (Incorporated by reference to Exhibit 99.1 of the Registrant's Current Report on Form 8-K, filed with the Commission on November 27, 2007.)
- Exhibit 10.6 Adams County National Bank Salary Savings Plan. (Incorporated by reference to Exhibit 10.6 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2009, filed with the Commission on March 12, 2010.)
- Exhibit 10.7 Group Pension Plan for Employees of Adams County National Bank. (Incorporated by reference to Exhibit 10.7 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2009, filed with the Commission on March 12, 2010.)
- Exhibit 10.8 Complete Settlement Agreement and General Release made among ACNB Corporation, Adams County National Bank and John W. Krichen effective June 13, 2006. (Incorporated by reference to Exhibit 99.1 of the Registrant's Current Report on Form 8-K, filed with the Commission on June 15, 2006.)
- Exhibit 10.9 Employment Agreement between ACNB Corporation, Adams County National Bank and Thomas A. Ritter dated as of December 31, 2008. (Incorporated by reference to Exhibit 10.9 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2008, filed with the Commission on March 13, 2009.)
- Exhibit 10.10 Employment Agreement between ACNB Corporation, Adams County National Bank and Lynda L. Glass dated as of December 31, 2008. (Incorporated by reference to Exhibit 10.10 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2008, filed with the Commission on March 13, 2009.)



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- Exhibit 10.11 Employment Agreement between ACNB Corporation, Russell Insurance Group, Inc. and Frank C. Russell, Jr. dated as of November 9, 2007. (Incorporated by reference to Exhibit 99.1 of the Registrant's Current Report on Form 8-K, filed with the Commission on November 16, 2007.)
- Exhibit 10.12 Employment Agreement between ACNB Corporation, Adams County National Bank and David W. Cathell dated as of April 17, 2009. (Incorporated by reference to Exhibit 99.1 of the Registrant's Current Report on Form 8-K, filed with the Commission on April 23, 2009.)
- Exhibit 10.13 2009 Restricted Stock Plan. (Incorporated by reference to Appendix C of the Registrant's Proxy Statement on Schedule 14A, filed with the Commission on March 25, 2009.)
- Exhibit 11 Statement re Computation of Earnings. (Incorporated by reference to page 6 of this Form 10-Q.)
- Exhibit 14 Code of Ethics. (Incorporated by reference to Exhibit 14 of the Registrant's Current Report on Form 8-K, filed with the Commission on March 19, 2010.)
- Exhibit 31.1 Chief Executive Officer Certification of Quarterly Report on Form 10-Q.
- Exhibit 31.2 Chief Financial Officer Certification of Quarterly Report on Form 10-Q.
- Exhibit 32.1 Chief Executive Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- Exhibit 32.2 Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**ACNB CORPORATION** (Registrant)

Date: November 5, 2010

/s/ Thomas A. Ritter  
Thomas A. Ritter  
President & Chief Executive Officer

/s/ David W. Cathell  
David W. Cathell  
Executive Vice President, Treasurer &  
Chief Financial Officer (Principal Financial Officer)