EMCLAIRE FINANCIAL CORP
Form 10-K
March 22, 2010

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One):

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended: December 31, 2009

¨TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from: _____ to _____

Commission File Number: 000-18464

EMCLAIRE FINANCIAL CORP.
(Exact name of registrant as specified in its charter)

Pennsylvania	25-1606091
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
612 Main Street, Emlenton, PA	16373
(Address of principal executive office)	(Zip Code)

Registrant's telephone number: (724) 867-2311

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

Common Stock, par value $1.25 per share	NASDAQ Capital Markets (NASDAQ)
(Title of Class)	(Name of exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act: None.

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

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
YES ¨ NO x.

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company.
Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES ¨ NO x.

As of June 30, 2009, the aggregate value of the 1,258,798 shares of Common Stock of the Registrant issued and outstanding on such date, which excludes 172,606 shares held by the directors and officers of the Registrant as a group, was approximately $22.7 million. This figure is based on the last sales price of $18.00 per share of the Registrant's Common Stock on June 30, 2009.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2010 Annual Meeting of Stockholders are incorporated by reference in Part III of this Form 10-K.

EMCLAIRE FINANCIAL CORP.

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SIGNATURES AND CERTIFICATIONS

Discussions of certain matters in this Form 10-K and other related year end documents may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act), and as such, may involve risks and uncertainties. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies, and expectations, are generally identifiable by the use of words or phrases such as “believe”, “plan”, “expect”, “intend”, “anticipate”, “estimate”, “project”, “forecast”, “may increase”, “may fluctuate”, “may improve” and similar expre future or conditional verbs such as “will”, “should”, “would”, and “could”. These forward-looking statements relate to, among other things, expectations of the business environment in which the Corporation operates, projections of future performance, potential future credit experience, perceived opportunities in the market and statements regarding the Corporation’s mission and vision. The Corporation’s actual results, performance and achievements may differ materially from the results, performance, and achievements expressed or implied in such forward-looking statements due to a wide range of factors. These factors include, but are not limited to, changes in interest rates, general economic conditions, the local economy, the demand for the Corporation’s products and services, accounting principles or guidelines, legislative and regulatory changes, monetary and fiscal policies of the U.S. Government, U.S. Treasury, and Federal Reserve, real estate markets, competition in the financial services industry, attracting and retaining key personnel, performance of new employees, regulatory actions, changes in and utilization of new technologies and other risks detailed in the Corporation’s reports filed with the Securities and Exchange Commission (SEC) from time to time. These factors should be considered in evaluating the forward-looking statements, and undue reliance should not be placed on such statements. The Corporation does not undertake, and specifically disclaims any obligation, to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

PART I

Item 1. Business

General

Emclaire Financial Corp. (the Corporation) is a Pennsylvania corporation and financial holding company that provides a full range of retail and commercial financial products and services to customers in western Pennsylvania through its wholly owned subsidiary bank, The Farmers National Bank of Emlenton (the Bank). The Corporation also provides real estate settlement services through its subsidiary, Emclaire Settlement Services, LLC (the Title Company). In addition, the Bank provides investment advisory services through its Farmers National Financial Services division.

The Bank was organized in 1900 as a national banking association and is a financial intermediary whose principal business consists of attracting deposits from the general public and investing such funds in real estate loans secured by liens on residential and commercial property, consumer loans, commercial business loans, marketable securities and interest-earning deposits. The Bank operates through a network of thirteen retail branch offices in Venango, Butler, Clarion, Clearfield, Crawford, Elk, Jefferson and Mercer counties, Pennsylvania. The Corporation and the Bank are headquartered in Emlenton, Pennsylvania.

The Bank is subject to examination and comprehensive regulation by the Office of the Comptroller of the Currency (OCC), which is the Bank’s chartering authority, and the Federal Deposit Insurance Corporation (FDIC), which insures customer deposits held by the Bank to the full extent provided by law. The Bank is a member of the Federal Reserve Bank of Cleveland (FRB) and the Federal Home Loan Bank of Pittsburgh (FHLB). The Corporation is a registered financial holding company pursuant to the Bank Holding Company Act of 1956, as amended (BHCA).

On August 28, 2009, the Bank completed the purchase of a former National City Bank full service branch office in Titusville, Pennsylvania. Through the acquisition of this office, the Bank assumed $90.8 million in deposits in

exchange for $32.6 million in loans, $54.9 million in net cash and certain fixed assets of the office.

On December 23, 2008 the Corporation issued to the U.S. Department of the Treasury (U.S. Treasury), in exchange for aggregate consideration of $7.5 million, 7,500 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A, with a liquidation preference of $1,000, and a ten year warrant to purchase up to 50,111 shares of the Corporation's common stock at an exercise price of $22.45 per share. The preferred securities pay cumulative dividends of 5% a year for the first five years and 9% a year thereafter.

On October 17, 2008, the Corporation completed the acquisition of Elk County Savings and Loan Association (ECSLA) and the merger conversion of ECSLA with and into the Bank. Associated with the merger conversion, the Corporation also conducted a common stock offering to eligible depositors and borrowers of ECSLA and the general public. The merger conversion and the offering generated $4.5 million in additional equity for the Corporation.

At December 31, 2009, the Corporation had $467.5 million in total assets, $37.0 million in stockholders' equity, $292.6 million in loans and $385.3 million in deposits.

Lending Activities

General. The principal lending activities of the Bank are the origination of residential mortgage, commercial mortgage, commercial business and consumer loans. Significantly all of the Bank's loans are originated in and secured by property within the Bank's primary market area.

One-to-Four Family Mortgage Loans. The Bank offers first mortgage loans secured by one-to-four family residences located in the Bank's primary lending area. Typically such residences are single-family owner occupied units. The Bank is an approved, qualified lender for the Federal Home Loan Mortgage Corporation (FHLMC). As a result, the Bank may sell loans to and service loans for the FHLMC in market conditions and circumstances where this is advantageous in managing interest rate risk.

Home Equity Loans. The Bank originates home equity loans secured by single-family residences. These loans may be either a single advance fixed-rate loan with a term of up to 20 years, or a variable rate revolving line of credit. These loans are made only on owner-occupied single-family residences.

Commercial Business and Commercial Real Estate Loans. Commercial lending constitutes a significant portion of the Bank's lending activities. Commercial business and commercial real estate loans amounted to 44.5% of the total loan portfolio at December 31, 2009. Commercial real estate loans generally consist of loans granted for commercial purposes secured by commercial or other nonresidential real estate. Commercial loans consist of secured and unsecured loans for such items as capital assets, inventory, operations and other commercial purposes.

Consumer Loans. Consumer loans generally consist of fixed-rate term loans for automobile purchases, home improvements not secured by real estate, capital and other personal expenditures. The Bank also offers unsecured revolving personal lines of credit and overdraft protection.

Loans to One Borrower. National banks are subject to limits on the amount of credit that they can extend to one borrower. Under current law, loans to one borrower are limited to an amount equal to 15% of unimpaired capital and surplus on an unsecured basis, and an additional amount equal to 10% of unimpaired capital and surplus if the loan is secured by readily marketable collateral. At December 31, 2009, the Bank's loans to one borrower limit based upon 15% of unimpaired capital was $5.6 million. At December 31, 2009, the Bank's largest single lending relationship had an outstanding balance of $7.0 million. Credit granted to this borrower in excess of the legal lending limit is part of the Legal Lending Limit Pilot Program approved by the OCC which allows the Bank to exceed its legal lending limit within certain parameters. The Bank's next largest single lending relationship had an outstanding balance of $4.3 million at December 31, 2009. Both loans were performing in accordance with their loan terms at December 31,

2009.

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Loan Portfolio. The following table sets forth the composition and percentage of the Corporation's loans receivable in dollar amounts and in percentages of the portfolio as of December 31:

(Dollar amounts in thousands)	2009		2008		2007		2006		2005	
	Dollar Amount	%	Dollar Amount	%	Dollar Amount	%	Dollar Amount	%	Dollar Amount	%
gage loans on real estate:										
dential first mortgages	$ 74,099	25.0%	$ 74,130	27.7%	$ 65,706	28.3%	$ 64,662	30.0%	$ 66,011	3
e equity loans and lines of credit	77,284	26.1%	57,454	21.5%	49,426	21.3%	47,330	22.0%	39,933	2
mercial	89,952	30.4%	85,689	32.1%	71,599	30.9%	61,128	28.4%	52,990	2
real estate loans	241,335	81.5%	217,273	81.3%	186,731	80.5%	173,120	80.4%	158,934	8
loans:										
mercial business	41,588	14.1%	40,787	15.2%	35,566	15.3%	34,588	16.0%	27,732	1
umer	12,894	4.4%	9,429	3.5%	9,679	4.2%	7,671	3.6%	7,729	
other loans	54,482	18.5%	50,216	18.7%	45,245	19.5%	42,259	19.6%	35,461	1
loans receivable	295,817	100.0%	267,489	100.0%	231,976	100.0%	215,379	100.0%	194,395	10
vance for loan losses	3,202		2,651		2,157		2,035		1,869	
oans receivable	$ 292,615		$ 264,838		$ 229,819		$ 213,344		$ 192,526	

The following table sets forth the scheduled contractual principal repayments or interest repricing of loans in the Corporation's portfolio as of December 31, 2009. Demand loans having no stated schedule of repayment and no stated maturity are reported as due within one year.

(Dollar amounts in thousands)	Due in one year or less	Due from one to five years	Due from five to ten years	Due after ten years	Total
Residential mortgages	$ 1,523	$ 3,976	$ 13,216	$ 55,384	$ 74,099
Home equity loans and lines of credit	913	6,680	25,475	44,216	77,284
Commercial mortgages	2,428	5,348	13,545	68,631	89,952
Commercial business	3,001	7,939	6,462	24,186	41,588
Consumer	357	6,985	384	5,168	12,894
	$ 8,222	$ 30,928	$ 59,082	$ 197,585	$ 295,817

The following table sets forth the dollar amount of the Corporation's fixed and adjustable rate loans with maturities greater than one year as of December 31, 2009:

(Dollar amounts in thousands)	Fixed rates	Adjustable rates
Residential mortgage	$ 47,778	$ 24,798
Home equity loans and lines of credit	61,058	15,313

Commercial mortgage	39,772	47,752
Commercial business	37,218	1,369
Consumer	12,537	-
	$ 198,363	$ 89,232

Contractual maturities of loans do not reflect the actual term of the Corporation's loan portfolio. The average life of mortgage loans is substantially less than their contractual terms because of loan prepayments and enforcement of due-on-sale clauses, which give the Corporation the right to declare a loan immediately payable in the event, among other things, that the borrower sells the real property subject to the mortgage. Scheduled principal amortization also reduces the average life of the loan portfolio. The average life of mortgage loans tends to increase when current market mortgage rates substantially exceed rates on existing mortgages and conversely, decrease when rates on existing mortgages substantially exceed current market interest rates.

Delinquencies and Classified Assets

Delinquent Loans and Real Estate Acquired Through Foreclosure (REO). Typically, a loan is considered past due and a late charge is assessed when the borrower has not made a payment within fifteen days from the payment due date. When a borrower fails to make a required payment on a loan, the Corporation attempts to cure the deficiency by contacting the borrower. The initial contact with the borrower is made shortly after the seventeenth day following the due date for which a payment was not received. In most cases, delinquencies are cured promptly.

If the delinquency exceeds 60 days, the Corporation works with the borrower to set up a satisfactory repayment schedule. Typically, loans are considered non-accruing upon reaching 90 days delinquent, although the Corporation may be receiving partial payments of interest and partial repayments of principal on such loans. When a loan is placed in non-accrual status, previously accrued but unpaid interest is deducted from interest income. The Corporation institutes foreclosure action on secured loans only if all other remedies have been exhausted. If an action to foreclose is instituted and the loan is not reinstated or paid in full, the property is sold at a judicial or trustee's sale at which the Corporation may be the buyer.

Real estate properties acquired through, or in lieu of, foreclosure are to be sold and are initially recorded at fair value at the date of foreclosure establishing a new cost basis. After foreclosure, management periodically performs valuations and the real estate is carried at the lower of carrying amount or fair value less the cost to sell the property. Revenue and expenses from operations and changes in the valuation allowance are included in loss on foreclosed real estate. The Corporation generally attempts to sell its REO properties as soon as practical upon receipt of clear title.

As of December 31, 2009, the Corporation's non-performing assets, which consist of non-accrual loans, loans delinquent due to maturity, troubled debt restructuring, repossessions and REO, amounted to $2.6 million or 0.56% of the Corporation's total assets compared to $1.1 million or 0.28% of the Corporation's total assets at December 31, 2008. This increase was due to continued pressure on borrowers related to the prevailing poor economic climate. Interest income of $218,000 would have been recorded in 2009 if these loans had been current and performing during the entire period. Interest of $139,000 on these loans was included in income during 2009.

Classified Assets. Regulations applicable to insured institutions require the classification of problem assets as "substandard," "doubtful," or "loss" depending upon the existence of certain characteristics as discussed below. A category designated "special mention" must also be maintained for assets currently not requiring the above classifications but having potential weakness or risk characteristics that could result in future problems. An asset is classified as substandard if not adequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. A substandard asset is characterized by the distinct possibility that the Corporation will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all the weaknesses inherent in those classified as substandard. In addition, these weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable or improbable. Assets classified as loss are considered uncollectible and of such little value that their continuance as assets is not warranted.

The Corporation's classification of assets policy requires the establishment of valuation allowances for loan losses in an amount deemed prudent by management. Valuation allowances represent loss allowances that have been established to recognize the inherent risk associated with lending activities. When the Corporation classifies a problem asset as a loss, the portion of the asset deemed uncollectible is charged off immediately.

The Corporation regularly reviews the problem loans and other assets in its portfolio to determine whether any require classification in accordance with the Corporation's policy and applicable regulations. As of December 31, 2009, the Corporation's classified and criticized assets amounted to $16.6 million or 3.6% of total assets, with $10.2 million

classified as substandard, $180,000 classified as doubtful and $6.3 million identified as special mention.

Included in classified and criticized assets at December 31, 2009 are two separate large loans which have certain credit problems potentially impacting the ability of the borrowers to comply with their present loan repayment terms on a timely basis.

The first loan, with an outstanding balance of $3.0 million at December 31, 2009, was originated for the construction of a hotel, restaurant and retail plaza secured by such property, the borrower's personal residence, a separate residence and a separate farm. The hotel, restaurant and retail plaza are complete and operational. However, cash flows from operations have not been constant and are impacted by the seasonal nature of the hotel. In addition, the borrower does not have other liquid sources of cash flow. As a result, the borrower has listed substantial real estate holdings for sale. Pending such sales, the Bank anticipates that the relationship may continue to have cash flow issues which may impact the timely payment of principal and interest to the Bank. At December 31, 2009, the loan was current but identified as special mention. Ultimately, due to the estimated value of the borrower's significant real estate holdings, the Bank does not currently expect to incur any significant loss on this loan.

The second loan, with an outstanding balance of $2.3 million at December 31, 2009, is a consumer installment loan for the purpose of consolidating various personal debts. This loan is secured by a lien on the primary residence of the first borrower discussed above, an assigned life insurance policy and the assignment of patent royalty income. Due to business difficulties and decreased royalty income, payments on the loan have not always been timely. At December 31, 2009, the loan was performing but was classified as substandard. As a result of the estimated value of the lien on the property owned by the first borrower, the estimated cash flow of royalty income and the borrower's business prospects, the Bank does not currently expect to incur any significant loss on this loan.

The following table sets forth information regarding the Corporation's non-performing assets as of December 31:

(Dollar amounts in thousands)	2009	2008	2007	2006	2005
Non-performing loans	$ 2,418	$ 1,011	$ 952	$ 1,841	$ 1,452
Total as a percentage of gross loans	0.82%	0.38%	0.41%	0.85%	0.75%
Repossessions	40	-	-	-	-
Real estate acquired through foreclosure	173	50	129	98	106
Total as a percentage of total assets	0.05%	0.01%	0.04%	0.03%	0.04%
Total non-performing assets	$ 2,631	$ 1,061	$ 1,081	$ 1,939	$ 1,558
Total non-performing assets as a percentage of total assets	0.56%	0.28%	0.35%	0.65%	0.57%
Allowance for loan losses as a percentage of non-performing loans	132.42%	262.22%	226.58%	110.54%	128.72%

Allowance for Loan Losses. Management establishes allowances for estimated losses on loans based upon its evaluation of the pertinent factors underlying the types and quality of loans; historical loss experience based on volume and types of loans; trend in portfolio volume and composition; level and trend on non-performing assets; detailed analysis of individual loans for which full collectibility may not be assured; determination of the existence and realizable value of the collateral and guarantees securing such loans and the current economic conditions affecting the collectibility of loans in the portfolio. The Corporation analyzes its loan portfolio at least quarterly for valuation purposes and to determine the adequacy of its allowance for losses. Based upon the factors discussed above,

management believes that the Corporation's allowance for losses as of December 31, 2009 of $3.2 million was adequate to cover probable losses inherent in the portfolio at such time.

The following table sets forth an analysis of the allowance for losses on loans receivable for the years ended December 31:

(Dollar amounts in thousands)	2009	2008	2007	2006	2005
Balance at beginning of period	$ 2,651	$ 2,157	$ 2,035	$ 1,869	$ 1,810
Provision for loan losses	1,367	500	256	358	205
Allowance for loan losses of ECSLA	-	206	-	-	-
Charge-offs:					
Residential mortgage loans	(35)	(10)	(48)	(71)	(45)
Commercial mortgage loans	(477)	(82)	(34)	(83)	(1)
Commercial business loans	(264)	-	(22)	(18)	(60)
Consumer loans	(83)	(160)	(60)	(49)	(91)
	(859)	(252)	(164)	(221)	(197)
Recoveries:					
Residential mortgage loans	-	-	1	-	-
Commercial business loans	7	15	16	19	18
Consumer loans	36	25	13	10	33
	43	40	30	29	51
Net charge-offs	(816)	(212)	(134)	(192)	(146)
Balance at end of period	$ 3,202	$ 2,651	$ 2,157	$ 2,035	$ 1,869
Ratio of net charge-offs to average loans outstanding	0.29%	0.08%	0.06%	0.09%	0.08%
Ratio of allowance to total loans at end of period	1.08%	0.99%	0.93%	0.94%	0.96%

The following table provides a breakdown of the allowance for loan losses by major loan category for the years ended December 31:

(Dollar amounts in thousands)	2009		2008		2007		2006		2005	
Loan Categories:	Dollar Amount	Percent of loans in each category to total loans	Dollar Amount	Percent of loans in each category to total loans	Dollar Amount	Percent of loans in each category to total loans	Dollar Amount	Percent of loans in each category to total loans	Dollar Amount	Percent of loans in each category to total loans

Commercial, financial and agricultural	$ 448	14.1%	$ 431	15.2%	$ 387	15.3%	$ 532	16.0%	$ 554	14.2%
Commercial mortgages	1,891	30.4%	1,369	32.1%	1,068	30.9%	820	28.4%	841	27.3%
Residential mortgages	356	25.0%	363	27.7%	309	28.3%	239	30.0%	211	34.0%
Home equity loans	452	26.1%	467	21.5%	368	21.3%	339	22.0%	150	20.5%
Consumer loans	51	4.4%	73	3.5%	79	4.2%	83	3.6%	106	4.0%
Unallocated	4	-	(52)	-	(54)	-	22	-	7	-
	$ 3,202	100%	$ 2,651	100%	$ 2,157	100%	$ 2,035	100%	$ 1,869	100%

Investment Activities

General. The Corporation maintains an investment portfolio of securities such as U.S. government agencies, mortgage-backed securities, municipal and corporate securities and equity securities.

Investment decisions are made within policy guidelines established by the Board of Directors. This policy is aimed at maintaining a diversified investment portfolio, which complements the overall asset/liability and liquidity objectives of the Bank, while limiting the related credit risk to an acceptable level.

The following table sets forth certain information regarding the fair value, weighted average yields and contractual maturities of the Corporation's securities as of December 31, 2009:

(Dollar amounts in thousands)	Due in 1 year or less	Due from 1 to 3 years	Due from 3 to 5 years	Due from 5 to 10 years	Due after 10 years	No scheduled maturity	Total
U.S. Treasury and federal agency	$ -	$ 1,004	$ 993	$ 1,004	$ -	$ -	$ 3,001
U.S. government sponsored entities and agencies	-	27,928	18,926	3,943	-	-	50,797
Mortgage-backed securities: residential	105	277	488	3,928	11,732	-	16,530
Collateralized mortgage obligations	-	-	-	-	5,130	-	5,130
State and political subdivision	-	101	1,014	11,380	14,472	-	26,967
Equity securities	-	-	-	-	-	2,818	2,818
Estimated fair value	$ 105	$ 29,310	$ 21,421	$ 20,255	$ 31,334	$ 2,818	$ 105,243
Weighted average yield (1)	4.09%	1.79%	2.97%	5.15%	5.24%	3.15%	3.74

(1) Taxable equivalent adjustments have been made in calculating yields on state and political subdivision securities.

The following table sets forth the fair value of the Corporation's investment securities as of December 31:

(Dollar amounts in thousands)	2009	2008	2007
U.S. Treasury and federal agency	$ 3,001	$ -	$ -
U.S. government sponsored entities and agencies	50,797	20,077	29,334
Mortgage-backed securities: residential	16,530	17,218	1,884
Collateralized mortgage obligations	5,130	13,162	-
State and political subdivision	26,967	13,808	14,251
Corporate securities	-	3,984	2,939
Equity securities	2,818	3,194	3,511
	$ 105,243	$ 71,443	$ 51,919

For additional information regarding the Corporation's investment portfolio see "Management's Discussion and Analysis of Financial Condition and Results of Operations" in item 7 and "Notes to Consolidated Financial Statements" beginning on page F-7.

Sources of Funds

General. Deposits are the primary source of the Bank's funds for lending and investing activities. Secondary sources of funds are derived from loan repayments, investment maturities and borrowed funds. Loan repayments can be considered a relatively stable funding source, while deposit activity is greatly influenced by interest rates and general market conditions. The Bank also has access to funds through other various sources. For a description of the Bank's sources of funds, see "Management's Discussion and Analysis of Financial Condition and Results of Operations" in item 7.

Deposits. The Bank offers a wide variety of retail deposit account products to both consumer and commercial deposit customers, including time deposits, non-interest bearing and interest bearing demand deposit accounts, savings

deposits and money market accounts.

Deposit products are promoted in periodic newspaper and radio advertisements, along with notices provided in customer account statements. The Bank's marketing strategy is based on its reputation as a community bank that provides quality products and personal customer service.

The Bank pays interest rates on its interest bearing deposit products that are competitive with rates offered by other financial institutions in its market area. Management reviews interest rates on deposits weekly and considers a number of factors, including: (1) the Bank's internal cost of funds; (2) rates offered by competing financial institutions; (3) investing and lending opportunities; and (4) the Bank's liquidity position.

The following table sets forth maturities of the Corporation's certificates of deposit of $100,000 or more at December 31, 2009 by time remaining to maturity:

(Dollar amounts in thousands)	Amount
Less than three months	$ 3,442
Over three months to six months	3,306
Over six months to twelve months	5,020
Over twelve months	37,545
	$ 49,313

Borrowings. Borrowings may be used to compensate for reductions in deposit inflows or net deposit outflows, or to support lending and investment activities. These borrowings include FHLB advances, federal funds, repurchase agreements, advances from the Federal Reserve Discount Window and lines of credit at the Bank and the Corporation with other correspondent banks. The following table summarizes information with respect to borrowings at or for the years ending December 31:

(Dollar amounts in thousands)	2009	2008
Ending balance	$ 40,000	$ 48,188
Average balance	50,611	45,096
Maximum balance	75,000	54,683
Weighted average rate	3.34%	3.89%

For additional information regarding the Corporation's deposit base and borrowed funds, see "Management's Discussion and Analysis of Financial Condition and Results of Operations" in item 7 and "Notes to Consolidated Financial Statements" beginning on page F-7.

Subsidiary Activity

The Corporation has two wholly owned subsidiaries, the Bank, a national association and the Title Company. As of December 31, 2009, the Bank and the Title Company had no subsidiaries.

Personnel

At December 31, 2009, the Bank had 119 full time equivalent employees. There is no collective bargaining agreement between the Bank and its employees, and the Bank believes its relationship with its employees to be satisfactory.

Competition

The Bank competes for loans, deposits and customers with other commercial banks, savings and loan associations, securities and brokerage companies, mortgage companies, insurance companies, finance companies, money market funds, credit unions and other nonbank financial service providers.

Supervision and Regulation

General. Bank holding companies and banks are extensively regulated under both federal and state law. Set forth below is a summary description of certain provisions of certain laws that relate to the regulation of the Corporation and the Bank. The description does not purport to be complete and is qualified in its entirety by reference to the applicable laws and regulations.

The Corporation. The Corporation is a registered bank holding company, and subject to regulation and examination by the FRB under the BHCA. The Corporation is required to file with the FRB periodic reports and such additional information as the FRB may require. Recent changes to the Bank Holding Company rating system emphasizes risk management and evaluation of the potential impact of non-depository entities on safety and soundness.

The FRB may require the Corporation to terminate an activity or terminate control of or liquidate or divest certain subsidiaries, affiliates or investments when the FRB believes the activity or the control of the subsidiary or affiliate constitutes a significant risk to the financial safety, soundness or stability of any of its banking subsidiaries. The FRB also has the authority to regulate provisions of certain bank holding company debt, including the authority to impose interest ceilings and reserve requirements on such debt. Under certain circumstances, the Corporation must file written notice and obtain FRB approval prior to purchasing or redeeming its equity securities.

Further, the Corporation is required by the FRB to maintain certain levels of capital. See “Capital Standards.”

The Corporation is required to obtain prior FRB approval for the acquisition of more than 5% of the outstanding shares of any class of voting securities or substantially all of the assets of any bank or bank holding company. Prior FRB approval is also required for the merger or consolidation of the Corporation and another bank holding company.

The Corporation is prohibited by the BHCA, except in certain statutorily prescribed instances, from acquiring direct or indirect ownership or control of more than 5% of the outstanding voting shares of any company that is not a bank or bank holding company and from engaging directly or indirectly in activities other than those of banking, managing or controlling banks, or furnishing services to its subsidiaries. However, subject to the prior FRB approval, the Corporation may engage in any, or acquire shares of companies engaged in, activities that the FRB deems to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.

Under FRB regulations, the Corporation is required to serve as a source of financial and managerial strength to the Bank and may not conduct operations in an unsafe or unsound manner. In addition, it is the FRB’s policy that a bank holding company should stand ready to use available resources to provide adequate capital funds to its subsidiary banks during periods of financial stress or adversity and should maintain the financial flexibility and capital raising capacity to obtain additional resources for assisting its subsidiary banks. A bank holding company’s failure to meet its obligations to serve as a source of strength to its subsidiary banks will generally be considered by the FRB to be an unsafe and unsound banking practice or a violation of FRB regulations or both.

The Corporation is also a bank holding company within the meaning of the Pennsylvania Banking Code. As such, the Corporation and its subsidiaries are subject to examination by, and may be required to file reports with, the Pennsylvania Department of Banking.

The Corporation’s securities are registered with the SEC under the Exchange Act. As such, the Corporation is subject to the information, proxy solicitation, insider trading, corporate governance, and other requirements and restrictions of the Exchange Act. The public may obtain all forms and information filed with the SEC through their website http://www.sec.gov.

The Bank. As a national banking association, the Bank is subject to primary supervision, examination and regulation by the OCC. The Corporation is also subject to regulations of the FDIC as administrator of the Deposit Insurance Fund (DIF) and the FRB. If, as a result of an examination of the Bank, the OCC should determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity or other aspects of the Corporation's operations are unsatisfactory or that the Bank is violating or has violated any law or regulation, various remedies are available to the OCC. Such remedies include the power to enjoin "unsafe or unsound practices," to require affirmative action to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in capital, to restrict the Bank's growth, to assess civil monetary penalties, and to remove officers and directors. The FDIC has similar enforcement authority, in addition to its authority to terminate the Bank's deposit insurance in the absence of action by the OCC and upon a finding that the Bank is operating in an unsafe or unsound condition, is engaging in unsafe or unsound activities, or that the Corporation's conduct poses a risk to the deposit insurance fund or may prejudice the interest of its depositors.

A national bank may have a financial subsidiary engaged in any activity authorized for national banks directly or certain permissible activities. Generally, a financial subsidiary is permitted to engage in activities that are "financial in nature" or incidental thereto, even though they are not permissible for the national bank itself. The definition of "financial in nature" includes, among other items, underwriting, dealing in or making a market in securities, including, for example, distributing shares of mutual funds. The subsidiary may not, however, engage as principal in underwriting insurance, issue annuities or engage in real estate development or investment or merchant banking.

The Sarbanes-Oxley Act of 2002. The Sarbanes-Oxley Act of 2002 addresses accounting oversight and corporate governance matters, including:

- The prohibition of accounting firms from providing various types of consulting services to public clients and requiring accounting firms to rotate partners among public client assignments every five years;
- Increased penalties for financial crimes and forfeiture of executive bonuses in certain circumstances;
- Required executive certification of financial presentations;
- Increased requirements for board audit committees and their members;
- Enhanced disclosure of controls and procedures and internal control over financial reporting;
- Enhanced controls on, and reporting of, insider trading; and
- Statutory separations between investment bankers and analysts.

The new legislation and its implementing regulations have resulted in increased costs of compliance, including certain outside professional costs. To date these costs have not had a material impact on the Corporation's operations.

USA PATRIOT Act of 2001. The USA PATRIOT Act of 2001 and its implementing regulations significantly expanded the anti-money laundering and financial transparency laws. Under the USA PATRIOT Act, financial institutions are subject to prohibitions regarding specified financial transactions and account relationships, as well as enhanced due diligence and "know your customer" standards in their dealings with foreign financial institutions and foreign customers. For example, the enhanced due diligence policies, procedures and controls generally require financial institutions to take reasonable steps:

- To conduct enhanced scrutiny of account relationships to guard against money laundering and report any suspicious transaction,
- To ascertain the identity of the nominal and beneficial owners of, and the source of funds deposited into, each account as needed to guard against money laundering and report any suspicious transactions,
- To ascertain for any foreign bank, the shares of which are not publicly traded, the identity of the owners of the foreign bank, and the nature and extent of the ownership interest of each such owner, and
- To ascertain whether any foreign bank provides correspondent accounts to other foreign banks and, if so, the identity of those foreign banks and related due diligence information.

Under the USA PATRIOT Act, financial institutions are required to establish and maintain anti-money laundering programs which include:

- The establishment of a customer identification program,
- The development of internal policies, procedures, and controls,
- The designation of a compliance officer,
- An ongoing employee training program, and
- An independent audit function to test the programs.

The Bank has implemented comprehensive policies and procedures to address the requirements of the USA PATRIOT Act.

Privacy. Federal banking rules limit the ability of banks and other financial institutions to disclose non-public information about consumers to nonaffiliated third parties. Pursuant to these rules, financial institutions must provide:

- Initial notices to customers about their privacy policies, describing the conditions under which they may disclose nonpublic personal information to nonaffiliated third parties and affiliates;
- Annual notices of their privacy policies to current customers; and
- A reasonable method for customers to "opt out" of disclosures to nonaffiliated third parties.

These privacy provisions affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors. The Corporation's privacy policies have been implemented in accordance with the law.

Dividends and Other Transfers of Funds. Dividends from the Bank constitute the principal source of income to the Corporation. The Corporation is a legal entity separate and distinct from the Bank. The Bank is subject to various statutory and regulatory restrictions on its ability to pay dividends to the Corporation. In addition, the Bank's regulators have the authority to prohibit the Bank from paying dividends, depending upon the Bank's financial condition, if such payment is deemed to constitute an unsafe or unsound practice.

The Corporation entered into a Securities Purchase Agreement (the Agreement) on December 23, 2008 with the U.S. Treasury in association with its participation in the Capital Purchase Program (CPP) of the Emergency Economic Stabilization Act of 2008 (EESA). As a result of the Corporation's participation in the CPP, the Corporation may not pay a dividend in excess of $0.32 per share until the earlier of December 23, 2011 or the date the preferred shares have been redeemed in whole or transferred to a non-affiliated party.

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Transactions with Affiliates. The Bank is subject to certain restrictions imposed by federal law on any extensions of credit to, or the issuance of a guarantee or letter of credit on behalf of, any affiliates, the purchase of, or investments in, stock or other securities thereof, the taking of such securities as collateral for loans, and the purchase of assets of any affiliates. Such restrictions prevent any affiliates from borrowing from the Bank unless the loans are secured by marketable obligations of designated amounts. Further, such secured loans and investments by the Bank to or in any affiliate are limited, individually, to 10% of the Bank's capital and surplus (as defined by federal regulations), and such secured loans and investments are limited, in the aggregate, to 20% of the Bank's capital and surplus. Some of the entities included in the definition of an affiliate are parent companies, sister banks, sponsored and advised companies, investment companies whereby the Bank or its affiliate serves as investment advisor, and financial subsidiaries of the bank. Additional restrictions on transactions with affiliates may be imposed on the Bank under the prompt corrective action provisions of federal law. See "Prompt Corrective Action and Other Enforcement Mechanisms."

Loans to One Borrower Limitations. With certain limited exceptions, the maximum amount that a national bank may lend to any borrower (including certain related entities of the borrower) at one time may not exceed 15% of the unimpaired capital and surplus of the institution, plus an additional 10% of unimpaired capital and surplus for loans fully secured by readily marketable collateral. At December 31, 2009, the Bank's loans-to-one-borrower limit was $5.6 million based upon the 15% of unimpaired capital and surplus measurement. At December 31, 2009, the Bank's largest single lending relationship had an outstanding balance of $7.0 million. Credit granted to this borrower in excess of the legal lending limit is part of the Legal Lending Limit Pilot Program approved by the OCC which allows the Bank to exceed its legal lending limit within certain parameters. The Bank's next largest single lending relationship had an outstanding balance of $4.3 million at December 31, 2009.

Capital Standards. The federal banking agencies have adopted risk-based minimum capital guidelines intended to provide a measure of capital that reflects the degree of risk associated with a banking organization's operations for both transactions reported on the balance sheet as assets and transactions which are recorded as off-balance sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off-balance sheet items are multiplied by one of several risk adjustment percentages, which range from 0% for assets with low credit risk, such as federal banking agencies, to 100% for assets with relatively high credit risk.

The risk-based capital ratio is determined by classifying assets and certain off-balance sheet financial instruments into weighted categories, with higher levels of capital being required for those categories perceived as representing greater risk. Under the capital guidelines, a banking organization's total capital is divided into tiers. "Tier I capital" consists of (1) common equity, (2) qualifying noncumulative perpetual preferred stock, (3) a limited amount of qualifying cumulative perpetual preferred stock and (4) minority interests in the equity accounts of consolidated subsidiaries (including trust-preferred securities), less goodwill and certain other intangible assets. Not more than 25% of qualifying Tier I capital may consist of trust-preferred securities. "Tier II capital" consists of hybrid capital instruments, perpetual debt, mandatory convertible debt securities, a limited amount of subordinated debt, preferred stock that does not qualify as Tier I capital, a limited amount of the allowance for loan and lease losses and a limited amount of unrealized holding gains on equity securities. "Tier III capital" consists of qualifying unsecured subordinated debt. The sum of Tier II and Tier III capital may not exceed the amount of Tier I capital.

The guidelines require a minimum ratio of qualifying total capital to risk-adjusted assets of 8% and a minimum ratio of Tier 1 capital to risk-adjusted assets of 4%. In addition to the risk-based guidelines, federal banking regulators require banking organizations to maintain a minimum amount of Tier 1 capital to total assets, referred to as the leverage ratio. For a banking organization rated in the highest of the five categories used by regulators to rate banking organizations, the minimum leverage ratio of Tier 1 capital to total assets must be 3%. In addition to these uniform risk-based capital guidelines and leverage ratios that apply across the industry, the regulators have the discretion to set individual minimum capital requirements for specific institutions at rates significantly above the minimum guidelines and ratios.

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In addition, federal banking regulators may set capital requirements higher than the minimums described above for financial institutions whose circumstances warrant it. For example, a financial institution experiencing or anticipating significant growth may be expected to maintain capital positions substantially above the minimum supervisory levels without significant reliance on intangible assets.

Prompt Corrective Action and Other Enforcement Mechanisms. Federal banking agencies possess broad powers to take corrective and other supervisory action to resolve the problems of insured depository institutions, including but not limited to those institutions that fall below one or more prescribed minimum capital ratios. Each federal banking agency has promulgated regulations defining the following five categories in which an insured depository institution will be placed, based on its capital ratios: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized. At December 31, 2009, the Bank exceeded the required ratios for classification as "well capitalized."

An institution that, based upon its capital levels, is classified as well capitalized, adequately capitalized, or undercapitalized may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition or an unsafe or unsound practice warrants such treatment. At each successive lower capital category, an insured depository institution is subject to more restrictions. The federal banking agencies, however, may not treat a significantly undercapitalized institution as critically undercapitalized unless its capital ratio actually warrants such treatment.

In addition to measures taken under the prompt corrective action provisions, commercial banking organizations may be subject to potential enforcement actions by the federal regulators for unsafe or unsound practices in conducting their businesses or for violations of any law, rule, regulation, or any condition imposed in writing by the agency or any written agreement with the agency. Finally, pursuant to an interagency agreement, the FDIC can examine any institution that has a substandard regulatory examination score or is considered undercapitalized – without the express permission of the institution's primary regulator.

Safety and Soundness Standards. The federal banking agencies have adopted guidelines designed to assist the federal banking agencies in identifying and addressing potential safety and soundness concerns before capital becomes impaired. The guidelines set forth operational and managerial standards relating to: (i) internal controls, information systems and internal audit systems, (ii) loan documentation, (iii) credit underwriting, (iv) asset growth, (v) earnings, and (vi) compensation, fees and benefits. In addition, the federal banking agencies have also adopted safety and soundness guidelines with respect to asset quality and earnings standards. These guidelines provide six standards for establishing and maintaining a system to identify problem assets and prevent those assets from deteriorating. Under these standards, an insured depository institution should: (i) conduct periodic asset quality reviews to identify problem assets, (ii) estimate the inherent losses in problem assets and establish reserves that are sufficient to absorb estimated losses, (iii) compare problem asset totals to capital, (iv) take appropriate corrective action to resolve problem assets, (v) consider the size and potential risks of material asset concentrations, and (vi) provide periodic asset quality reports with adequate information for management and the board of directors to assess the level of asset risk. These guidelines also set forth standards for evaluating and monitoring earnings and for ensuring that earnings are sufficient for the maintenance of adequate capital and reserves.

Insurance of Accounts. The deposits of the Bank are insured to the maximum extent permitted by the DIF. The FDIC administers the DIF, which generally insures commercial bank, savings association and state savings bank deposits. The DIF was created as a result of the merger of the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF), pursuant to the Federal Deposit Insurance Reform Act of 2005 (Reform Act).

In October 2008, the maximum amount insured under FDIC deposit insurance was temporarily increased from $100,000 to $250,000 per insured depositor through December 31, 2009. In May 2009, the FDIC extended this

increased insurance level of $250,000 per depositor through December 31, 2013. On January 1, 2014, the standard insurance amount will return to $100,000 per depositor for all account categories except IRAs and certain other retirement accounts.

In October 2008, the FDIC announced its Temporary Liquidity Guarantee Program (TLGP) which provides full coverage for noninterest-bearing transaction deposit accounts at FDIC-insured institutions that agree to participate in the program. The unlimited coverage applies to all personal and business checking deposit accounts that do not earn interest, low-interest NOW accounts (accounts that cannot earn more than 0.5% interest), Official Items and IOLTA accounts. A 10 basis point surcharge is added to a participating institution's current insurance assessment. The Bank elected to participate in the TLGP. This unlimited insurance coverage is temporary and was originally scheduled to expire on December 31, 2009; however, in August 2009, the FDIC extended the program through June 30, 2010. The deposit insurance surcharge was increased from 10 to 25 basis points for institutions electing to participate in the extension.

Under the Reform Act, the FDIC's deposit insurance premiums are assessed through a risk-based system under which all insured depository institutions are placed into one of four categories and assessed insurance premiums based upon their level of capital and risk profile. The FDIC is authorized to establish annual deposit insurance assessment rates for members of the DIF and to increase assessment rates if it determines such increases are appropriate to maintain reserves of the insurance fund. In addition, the FDIC is authorized to levy emergency special assessments on DIF members. The FDIC may terminate deposit insurance if it determines an institution has engaged in or is engaging in unsafe or unsound banking practices, is in an unsafe or unsound condition or has violated applicable laws, regulations or orders. No institution may pay a dividend if it is in default of the federal deposit insurance assessment.

In October 2008, the FDIC published a restoration plan designed to replenish the DIF over a period of five years and to increase the deposit insurance reserve ratio to the statutory minimum of 1.15% of insured deposits by December 31, 2013. In March 2009, the deposit insurance reserve ratio was 0.27%. In order to accomplish this, the FDIC changed both its risk-based assessment system and its base assessment rates. For the first quarter of 2009, the FDIC increased all FDIC deposit assessment rates by 7 basis points. These new rates ranged from 12 to 14 basis points for Risk Category I institutions to 50 basis points for Risk Category IV institutions. Beginning April 1, 2009, the base assessment rates range from 12 to 16 basis points for Risk Category I institutions to 77.5 basis points for Risk Category IV institutions. As of December 31, 2009, the Bank was classified as a Risk Category I institution and as such was assessed an FDIC deposit assessment rate of 13.79 basis points.

In May 2009, the FDIC adopted a final rule imposing a 5 basis point special assessment on each insured depository institution's assets minus Tier 1 capital as of June 30, 2009. The special assessment was collected on September 30, 2009 and totaled $178,000.

In November 2009, the FDIC adopted a final rule requiring insured institutions to prepay three years of estimated insurance assessments. This prepayment strengthened the cash position of the DIF immediately without impacting earnings to financial institutions. Payment of the prepaid assessment for the years endings December 31, 2010, 2011 and 2012 was collected on December 30, 2009 and totaled $2.1 million. This prepayment was based upon assumed increases in insured deposits of 5% annually through 2012 with a three basis point increase in the proposed assessment rate for the years ending December 31, 2011 and 2012.

The FDIC may further increase the assessment rate schedule in order to manage the DIF to prescribed target levels. An increase in the risk category for the Bank or in the assessment rates could have an adverse effect on the Bank's earnings.

In addition, all institutions with deposits insured by the FDIC are required to pay assessments to fund interest payments on bonds issued by the Financing Corporation (FICO), a mixed-ownership government corporation established to recapitalize a predecessor to the DIF. The current annualized assessment rate is 1.06 basis points of insured deposits, or approximately 0.265 basis points per quarter. These assessments will continue until the FICO bonds mature in 2019.

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Interstate Banking and Branching. Banks have the ability, subject to certain State restrictions, to acquire, by acquisition or merger, branches outside its home state. The establishment of new interstate branches is also possible in those states with laws that expressly permit it. Interstate branches are subject to certain laws of the states in which they are located. Competition may increase further as banks branch across state lines and enter new markets.

Consumer Protection Laws and Regulations. The bank regulatory agencies are focusing greater attention on compliance with consumer protection laws and their implementing regulations. Examination and enforcement have become more intense in nature, and insured institutions have been advised to monitor carefully compliance with such laws and regulations. The Bank is subject to many federal consumer protection statutes and regulations, some of which are discussed below.

The Community Reinvestment Act (CRA) is intended to encourage insured depository institutions, while operating safely and soundly, to help meet the credit needs of their communities. The CRA specifically directs the federal regulatory agencies, in examining insured depository institutions, to assess a bank's record of helping meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound banking practices. The CRA further requires the agencies to take a financial institution's record of meeting its community credit needs into account when evaluating applications for, among other things, domestic branches, mergers or acquisitions, or holding company formations. The agencies use the CRA assessment factors in order to provide a rating to the financial institution. The ratings range from a high of "outstanding" to a low of "substantial noncompliance." In its last examination for CRA compliance, as of April 21, 2008, the Bank was rated "satisfactory."

On September 1, 2005, the federal banking agencies amended the CRA regulations to:

- Establish the definition of "Intermediate Small Bank" as an institution with total assets of $250 million to $1 billion, without regard to any holding company; and
- Take into account abusive lending practices by a bank or its affiliates in determining a bank's CRA rating.

The Fair Credit Reporting Act (FCRA), as amended by the Fair and Accurate Credit Transactions Act of 2003 (FACTA), requires financial firms to help deter identity theft, including developing appropriate fraud response programs, and give consumers more control of their credit data. It also reauthorizes a federal ban on state laws that interfere with corporate credit granting and marketing practices. In connection with the FACTA, financial institution regulatory agencies proposed rules that would prohibit an institution from using certain information about a consumer it received from an affiliate to make a solicitation to the consumer, unless the consumer has been notified and given a chance to opt out of such solicitations. A consumer's election to opt out would be applicable for at least five years.

The Federal Trade Commission (FTC), the federal bank regulatory agencies and the National Credit Union Administration (NCUA) have issued regulations (the Red Flag Rules) requiring financial institutions and creditors to develop and implement written identity theft prevention programs as part of the FACTA. The programs were required be in place by May 1, 2009 and must provide for the identification, detection and response to patterns, practices or specific activities – known as red flags – that could indicate identity theft. These red flags may include unusual account activity, fraud alerts on a consumer report or attempted use of suspicious account application documents. The program must also describe appropriate responses that would prevent and mitigate the crime and detail a plan to update the program. The program must be managed by the Board of Directors or senior employees of the institution or creditor, include appropriate staff training and provide oversight of any service providers.

The Check Clearing for the 21st Century Act (Check 21) facilitates check truncation and electronic check exchange by authorizing a new negotiable instrument called a "substitute check," which is the legal equivalent of an original check. Check 21, effective October 28, 2004, does not require banks to create substitute checks or accept checks electronically; however, it does require banks to accept a legally equivalent substitute check in place of an original.

The Equal Credit Opportunity Act (ECOA) generally prohibits discrimination in any credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, age (except in limited circumstances), receipt of income from public assistance programs, or good faith exercise of any rights under the Consumer Credit Protection Act.

The Truth in Lending Act (TILA) is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably. As a result of the TILA, all creditors must use the same credit terminology to express rates and payments, including the annual percentage rate, the finance charge, the amount financed, the total of payments and the payment schedule, among other things.

The Fair Housing Act (FHA) regulates many practices, including making it unlawful for any lender to discriminate in its housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap or familial status. A number of lending practices have been found by the courts to be, or may be considered, illegal under the FHA, including some that are not specifically mentioned in the FHA itself.

The Home Mortgage Disclosure Act (HMDA) grew out of public concern over credit shortages in certain urban neighborhoods and provides public information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. The HMDA also includes a "fair lending" aspect that requires the collection and disclosure of data about applicant and borrower characteristics as a way of identifying possible discriminatory lending patterns and enforcing anti-discrimination statutes.

The term "predatory lending," much like the terms "safety and soundness" and "unfair and deceptive practices," is far-reaching and covers a potentially broad range of behavior. As such, it does not lend itself to a concise or a comprehensive definition. But typically predatory lending involves at least one, and perhaps all three, of the following elements:

- Making unaffordable loans based on the assets of the borrower rather than on the borrower's ability to repay an obligation ("asset-based lending")
- Inducing a borrower to refinance a loan repeatedly in order to charge high points and fees each time the loan is refinanced ("loan flipping")
- Engaging in fraud or deception to conceal the true nature of the loan obligation from an unsuspecting or unsophisticated borrower.

FRB regulations aimed at curbing such lending significantly widen the pool of high-cost home-secured loans covered by the Home Ownership and Equity Protection Act of 1994, a federal law that requires extra disclosures and consumer protections to borrowers. Lenders that violate the rules face cancellation of loans and penalties equal to the finance charges paid.

Effective April 8, 2005, OCC guidelines require national banks and their operating subsidiaries to comply with certain standards when making or purchasing loans to avoid predatory or abusive residential mortgage lending practices. Failure to comply with the guidelines could be deemed an unsafe and unsound or unfair or deceptive practice, subjecting the bank to supervisory enforcement actions.

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Finally, the Real Estate Settlement Procedures Act (RESPA) requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, RESPA prohibits certain abusive practices, such as kickbacks, and places limitations on the amount of escrow accounts. Penalties under the above laws may include fines, reimbursements and other penalties. Due to heightened regulatory concern related to compliance with the CRA, FACTA, TILA, FHA, ECOA, HMDA and RESPA generally, the Bank may incur additional compliance costs or be required to expend additional funds for investments in its local community.

Federal Home Loan Bank System. The Bank is a member of the FHLB. Among other benefits, each FHLB serves as a reserve or central bank for its members within its assigned region. Each FHLB is financed primarily from the sale of consolidated obligations of the FHLB system. Each FHLB makes available loans or advances to its members in compliance with the policies and procedures established by the Board of Directors of the individual FHLB. As an FHLB member, the Bank is required to own a certain amount of capital stock in the FHLB. At December 31, 2009, the Bank was in compliance with the stock requirements.

Federal Reserve System. The FRB requires all depository institutions to maintain noninterest bearing reserves at specified levels against their transaction accounts (primarily checking) and non-personal time deposits. At December 31, 2009, the Bank was in compliance with these requirements.

Item 1A. Risk Factors

Deterioration of economic conditions in our geographic market area could hurt our business.

We are located in western Pennsylvania and our loans are concentrated in Butler, Clarion, Crawford, Jefferson and Venango Counties, Pennsylvania. Although we have diversified our loan portfolio into other Pennsylvania counties, and to a very limited extent, into other states, the vast majority of our loans remain concentrated in the three primary counties. As a result of this geographic concentration, our financial results depend largely upon economic and real estate market conditions in these areas. Deterioration in economic or real estate market conditions in our primary market areas could have a material adverse impact on the quality of our loan portfolio, the demand for our products and services, and our financial condition and results of operations. Non-performing assets increased from $1.1 million or 0.28% of total assets at December 31, 2008 to $2.6 million or 0.56% of total assets at December 31, 2009.

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

We have established an allowance for loan losses that we believe is adequate to offset probable losses on our existing loans. However, experience in the banking industry indicates that a portion of our loans will become delinquent, that some of our loans may only be partially repaid or may never be repaid and we may experience other losses for reasons beyond our control. Despite our underwriting criteria and historical experience, we may be particularly susceptible to losses due to: (1) the geographic concentration of our loans; (2) the concentration of higher risk loans, such as commercial real estate and commercial business loans; and (3) our lack of experience with the loans acquired in the Titusville branch acquisition. As a result, we may not be able to maintain our current levels of nonperforming assets and charge-offs. Although we believe that our allowance for loan losses is maintained at a level adequate to absorb any inherent losses in our loan portfolio, these estimates of loan losses are necessarily subjective and their accuracy depends on the outcome of future events. If we need to make significant and unanticipated increases in our loss allowance in the future, our results of operations and financial condition would be materially adversely affected at that time.

Economic conditions and increased uncertainty in the financial markets could adversely affect our ability to accurately assess the allowance for credit losses. Our ability to assess the creditworthiness of our customers or to estimate the values of our assets and collateral for loans will be reduced if the models and approaches we use become less predictive of future behaviors, valuations, assumptions or estimates. We estimate losses inherent in our loan portfolio, the adequacy of our allowance for loan losses and the values of certain assets by using estimates based on difficult, subjective, and complex judgments, including estimates as to the effects of economic conditions and how these economic conditions might affect the ability of our borrowers to repay their loans or the value of assets.

Further declines in the value of certain investment securities could require write-downs, which would reduce our earnings.

At December 31, 2009, our investment portfolio included $2.8 million of securities in other financial institutions held by us. After our third quarter 2009 evaluation of our investment portfolio, we determined that other-than-temporary impairments existed on three financial institution equity securities. The impairment of these securities were considered to be other-than-temporary due to continued concerns related to the financial condition and near-term prospects of the three financial institutions, economic conditions of the financial services industry and deteriorating market values. These securities were written down to their fair market values as of September 30, 2009 and resulted in impairment losses of $898,000 that we recognized for the year ended December 31, 2009. A number of factors or combinations of factors could cause us to conclude in one or more future reporting periods that an unrealized loss that exists with respect to one or more of these securities or other financial institution securities will constitute an impairment that is other-than temporary. These factors include, but are not limited to, failure to make scheduled interest or dividend payments, an increase in the severity of the unrealized loss on a particular security, an increase in the continuous duration of the unrealized loss without an improvement in value or changes in market conditions and/or industry or issuer specific factors that would render us unable to forecast a full recovery in value. Additional other-than-temporary impairment write-downs could reduce our earnings.

We hold certain intangible assets that could be classified as impaired in the future. If these assets are considered to be either partially or fully impaired in the future, our earnings and the book values of these assets would decrease.

We are required to test our goodwill and core deposit intangible assets for impairment on a periodic basis. The impairment testing process considers a variety of factors, including the current market price of our common shares, the estimated net present value of our assets and liabilities and information concerning the terminal valuation of similarly situated insured depository institutions. It is possible that future impairment testing could result in a partial or full impairment of the value of our goodwill or core deposit intangible assets, or both. If an impairment determination is made in a future reporting period, our earnings and the book value of these intangible assets will be reduced by the amount of the impairment.

Liquidity risk could impair our ability to fund operations and jeopardize our financial condition.

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, and other sources, could have a substantial negative effect on our liquidity. Our access to funding sources in amounts adequate to finance our activities on terms that are acceptable to us could be impaired by factors that affect us specifically or the financial services industry or economy in general. Factors that could negatively impact our access to liquidity sources include a decrease in the level of our business activity as a result of a downturn in the markets in which our loans are concentrated, adverse regulatory action against us, or our inability to attract and retain deposits. Our ability to borrow could be impaired by factors that are not specific to us, such a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry in light of recent turmoil faced by banking organizations and the unstable credit markets.

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Our continued growth depends on our ability to meet minimum regulatory capital levels. Growth and shareholder returns may be adversely affected if sources of capital are not available to help us meet them.

As we grow, we will have to maintain our regulatory capital levels at or above the required minimum levels. If earnings do not meet our current estimates, if we incur unanticipated losses or expenses, or if we grow faster than expected, we may need to obtain additional capital sooner than expected, through borrowing, additional issuances of debt or equity securities, or otherwise. If we do not have continued access to sufficient capital, we may be required to reduce our level of assets or reduce our rate of growth in order to maintain regulatory compliance. Under those circumstances net income and the rate of growth of net income may be adversely affected. Additional issuances of equity securities could have a dilutive effect on existing shareholders.

There can be no assurance that recent legislation and regulatory actions taken by the federal government will help stabilize the financial system in the United States.

Several pieces of federal legislation have been enacted, and the U.S. Treasury, the FRB, the FDIC, and other federal agencies have enacted numerous programs, policies and regulations to address the current liquidity and credit crises. These measures include the EESA, the American Reinvestment and Recovery Act of 2009 (ARRA), and the numerous programs, including the CPP and expanded deposit insurance coverage, enacted thereunder. In addition, the Secretary of the U.S. Treasury has proposed fundamental changes to the regulation of financial institutions, markets and products.

We cannot predict the actual effects of EESA, the ARRA, the proposed regulatory reform measures and various governmental, regulatory, monetary and fiscal initiatives which have been and may be enacted on the financial markets, on us and the Bank. The terms and costs of these activities, or the failure of these actions to help stabilize the financial markets, asset prices, market liquidity and a continuation or worsening of current financial market and economic conditions could materially and adversely affect our business, financial condition, results of operations, and the trading prices of our securities.

We expect to face increased regulation of our industry, including as a result of EESA, the ARRA and related initiatives by the federal government. Compliance with such regulations may increase our costs and limit our ability to pursue business opportunities.

We are subject to additional uncertainties, and potential additional regulatory or compliance burdens, as a result of our participation in the CPP.

We accepted an investment of $7.5 million from the U.S. Treasury under the CPP. The Agreement we (and all other participating institutions) entered into with the U.S. Treasury, provides that the U.S. Treasury may unilaterally amend the agreement to the extent required to comply with any changes after the execution in applicable federal statutes. As a result of this provision, the U.S. Treasury and Congress may impose additional requirements or restrictions on us and the Bank in respect of reporting, compliance, corporate governance, executive or employee compensation, dividend payments, stock repurchases, lending or other business practices, capital requirements or other matters. We may be required to expend additional resources in order to comply with these requirements. Such additional requirements could impair our ability to compete with institutions that are not subject to the restrictions because they did not accept an investment from the U.S. Treasury. To the extent that additional restrictions or limitations on employee compensation are imposed, such as those contained in ARRA and the regulations issued in June 2009, we may be less competitive in attracting and retaining successful incentive compensation based lenders and customer relations personnel, or senior executive officers.

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Additionally, the ability of Congress to utilize the amendment provisions to effect political or public relations goals could result in our being subjected to additional burdens as a result of public perceptions of issues relating to the largest banks, and which are not applicable to community oriented institutions such as us. We may be disadvantaged as a result of these uncertainties.

As a result of the issuance of the Series A Preferred Stock to the U.S. Treasury, we are required to comply with certain restrictions on executive and employee compensation included in the EESA, as amended. Certain of these provisions could limit the amount and the tax deductibility of compensation we pay to our executive officers, and could have an adverse affect on our ability to compete for and retain employees and senior executive officers.

Higher FDIC deposit insurance premiums and assessments could adversely affect our financial condition.

FDIC insurance premiums have increased substantially in 2009 already, and we expect to pay significantly higher FDIC premiums in the future. A large number of bank failures has significantly depleted the deposit insurance fund and reduced the ratio of reserves to insured deposits. The FDIC adopted a revised risk-based deposit insurance assessment schedule on February 27, 2009, which raised deposit insurance premiums. On May 22, 2009, the FDIC also implemented a five basis point special assessment of each insured depository institution's assets minus Tier 1 capital as of June 30, 2009, but no more than 10 basis points times the institution's assessment base for the second quarter of 2009, which was collected on September 30, 2009. Additional special assessments may be imposed by the FDIC in the future, including a possible additional assessment in 2009. We participate in the FDIC's TLGP for noninterest-bearing transaction deposit accounts. Banks that participate in the TLGP pays the FDIC an annual assessment of 10 basis points on the amounts in such accounts above the amounts covered by FDIC deposit insurance. To the extent that these TLGP assessments are insufficient to cover any loss or expenses arising from the TLGP program, the FDIC is authorized to impose an emergency special assessment on all FDIC-insured depository institutions. The FDIC has authority to impose charges for the TLGP program upon depository institution holding companies, as well. The TLGP was originally scheduled to end December 31, 2009, but in August 2009, the FDIC has extended the TLGP to June 30, 2010, but is charging a higher fee to banks that elect to participate in the extension. These changes will cause our deposit insurance expense to increase. These actions could significantly increase our noninterest expense for the foreseeable future.

In November 2009, the FDIC adopted a final rule to recapitalize the DIF by requiring insured institutions to prepay their insurance premiums for the quarter ending December 31, 2009 and for the years ending December 31, 2010, 2011 and 2012. The prepayment was collected on December 30, 2009 and totaled $2.1 million. The FDIC further proposed that assessments for the years ending December 31, 2011 and 2012 would increase by three basis points, and would be based upon assumed increases in insured deposits of 5% annually through 2012. An increase in assessment rates will result in a further increase in our FDIC general insurance premium expense, and the prepayment of insurance premiums increased our non-earning assets.

Changes in interest rates and other factors beyond our control could have an adverse impact on our financial performance and results.

By nature, all financial institutions are impacted by changing interest rates. Among other issues, changes in interest rates may affect the following:

- the demand for new loans;
- the value of our interest-earning assets;
- prepayment speeds experienced on various asset classes, particularly residential mortgage loans;
- credit profiles of existing borrowers;
- rates received on loans and securities;

- our ability to obtain and retain deposits in connection with other available investment alternatives; and
- rates paid on deposits and borrowings.

Significant fluctuations in interest rates may have an adverse effect upon our financial condition and results of operations. The rates that we earn on our assets and the rates that we pay on our liabilities are generally fixed for a contractual period of time. We, like many financial institutions, have liabilities that generally have shorter contractual maturities than our assets. This imbalance can create significant earnings volatility, because market interest rates change over time. In a period of rising interest rates, the interest income earned on our assets may not increase as rapidly as the interest paid on our liabilities. In a period of declining interest rates, the interest income earned on our assets may decrease more rapidly than the interest paid on our liabilities.

In addition, changes in interest rates can also affect the average life of our loans and mortgage-backed and related securities. A reduction in interest rates results in increased prepayments of loans and mortgage-backed and related securities, as borrowers refinance their debt in order to reduce their borrowing cost. This causes reinvestment risk. This means that we may not be able to reinvest prepayments at rates that are comparable to the rates we earned on the prepaid loans or securities.

There are increased risks involved with commercial real estate and commercial business and consumer lending activities.

Our lending activities include loans secured by commercial real estate. Commercial real estate lending generally is considered to involve a higher degree of risk than single-family residential lending due to a variety of factors, including generally larger loan balances and the dependency on successful operation of the project for repayment. Our lending activities also include commercial business loans to small to medium businesses, which generally are secured by various equipment, machinery and other corporate assets, and a wide variety of consumer loans, including home equity and second mortgage loans, automobile loans and unsecured loans. Although commercial business loans and consumer loans generally have shorter terms and higher interest rates than mortgage loans, they generally involve more risk than mortgage loans because of the nature of, or in certain cases the absence of, the collateral which secures such loans.

In addition, we have a concentration of higher balance commercial real estate and commercial business loans with a limited number of borrowers in our market area. As a result, we have a greater risk of a significant loss due to such concentration and a greater risk of loan defaults in the event of an economic downturn in our market area as adverse economic changes may have a negative effect on the ability of our borrowers to make timely repayment of their loans.

Strong competition within our market area may limit our growth and profitability.

Competition in the banking and financial services industry is intense. In our market area, we compete with commercial banks, savings institutions, mortgage brokerage firms, credit unions, finance companies, and other financial intermediaries operating locally and elsewhere. Some of our competitors have greater name recognition and market presence that benefits them in attracting business and offer certain services that we do not provide. In addition, larger competitors may be able to price loans and deposits more aggressively than we do, which could affect our ability to grow and remain profitable on a long term basis. Our profitability depends upon our continued ability to successfully compete in our market area.

Government regulation will significantly affect the Bank's business, and may result in higher costs and lower shareholder returns.

The banking industry is heavily regulated. Banking regulations are primarily intended to protect the federal deposit insurance funds and depositors, not shareholders. We are subject to extensive regulation, supervision and examination by federal, state and local governmental authorities, including the Federal Reserve Board and the Office of the Comptroller of the Currency. The burden imposed by federal and state regulations puts banks at a competitive disadvantage compared to less regulated competitors such as finance companies, mortgage banking companies and leasing companies. Changes in the laws, regulations and regulatory practices affecting the banking industry may increase our costs of doing business or otherwise adversely affect us and create competitive advantages for others. Regulations affecting banks and financial services companies undergo continuous change, and we cannot predict the ultimate effect of these changes, which could have a material adverse effect on our profitability or financial condition. Federal economic and monetary policy may also affect our ability to attract deposits and other funding sources, make loans and investments, and achieve satisfactory interest spreads.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Corporation owns no real property but utilizes the main office of the Bank. The Corporation’s and the Bank’s executive offices are located at 612 Main Street, Emlenton, Pennsylvania. The Corporation pays no rent or other form of consideration for the use of this facility.

The Corporation owns and leases numerous other premises for use in conducting business activities. The Corporation considers these facilities owned or occupied under lease to be adequate. For additional information regarding the Corporation’s properties, see “Notes to Consolidated Financial Statements” beginning on page F-7.

Item 3. Legal Proceedings

Neither the Bank nor the Corporation is involved in any material legal proceedings. The Bank, from time to time, is party to litigation that arises in the ordinary course of business, such as claims to enforce liens, claims involving the origination and servicing of loans, and other issues related to the business of the Bank. In the opinion of management, the resolution of any such issues would not have a material adverse impact on the financial position, results of operation, or liquidity of the Bank or the Corporation.

Item 4. (Removed and Reserved)

PART II

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

Market, Holder and Dividend Information

Emclaire Financial Corp. common stock is traded on NASDAQ Capital Markets (NASDAQ) under the symbol "EMCF". The listed market makers for the Corporation's common stock include:

Boenning and Scattergood, Inc. 4 Tower Bridge, Suite 300 200 Bar Harbor Drive West Conshohocken, PA 19428 Telephone: (800) 889-6440	Janney Montgomery Scott LLC 1801 Market Street Philadelphia, PA 19103-1675 Telephone: (215) 665-6000	Monroe Securities, Inc. 100 North Riverside Plaza Suite 1620 Chicago, IL 60606 Telephone: (312) 327-2530

The Corporation has traditionally paid regular quarterly cash dividends. Future dividends will be determined by the Board of Directors after giving consideration to the Corporation's financial condition, results of operations, tax status, industry standards, economic conditions, regulatory requirements and other factors. As a result of the Corporation's participation in the U.S. Treasury's CPP, the Corporation may not pay a dividend in excess of $0.32 per share until the earlier of December 23, 2011 or the date the preferred shares have been redeemed in whole or transferred to a non-affiliated third party. For additional information regarding the Corporation's participation in the CPP, see "Notes to Consolidated Financial Statements" beginning on page F-7.

The following table sets forth the high and low sale market prices of the Corporation's common stock as well as cash dividends paid for the quarterly periods presented:

	Market Price			Cash
	High	Low	Close	Dividend
2009:				
Fourth quarter	$ 17.10	$ 12.11	$ 13.85	$ 0.14
Third quarter	18.30	15.85	17.10	0.14
Second quarter	23.50	17.50	18.00	0.14
First quarter	23.50	18.00	21.50	0.32
2008:				
Fourth quarter	$ 24.50	$ 20.05	$ 23.50	$ 0.34
Third quarter	26.50	21.00	24.00	0.32
Second quarter	28.00	24.60	25.75	0.32
First quarter	28.35	24.55	26.50	0.32

As of December 31, 2009, there were approximately 720 stockholders of record and 1,431,404 shares of common stock entitled to vote, receive dividends and considered outstanding for financial reporting purposes. The number of stockholders of record does not include the number of persons or entities who hold their stock in nominee or "street" name.

Common stockholders may have Corporation dividends reinvested to purchase additional shares. Participants may also make optional cash purchases of common stock through this plan and pay no brokerage commissions or fees. To

obtain a plan document and authorization card call 800-757-5755.

Purchases of Equity Securities

The Corporation did not repurchase any of its equity securities in the year ended December 31, 2009.

Item 6. Selected Financial Data

Not required as the Corporation is a smaller reporting company.

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

The following discussion and analysis represents a review of the Corporation's consolidated financial condition and results of operations. This review should be read in conjunction with the consolidated financial statements beginning on page F-3.

Overview

The Corporation reported a decrease in net income of $891,000 or 36.7% for 2009 as consolidated net income before accumulated preferred stock dividends and discount accretion amounted to $1.5 million or $0.80 per common share for 2009, compared to net income of $2.4 million or $1.87 per common share for 2008. Net income was impacted by the following:

- Net interest income grew by $1.8 million or 16.7% in 2009. This increase was driven by loan growth through the fourth quarter 2008 acquisition of ECSLA which added $7.3 million to the Corporation's loan portfolio, the extension of three, one-year tax anticipation notes to local municipalities totaling $11.5 million during the first quarter of 2009, and the third quarter 2009 purchase of a branch banking office in Titusville, Pennsylvania from PNC/National City in which $32.6 million of loans were acquired.
- The provision for loan losses increased $867,000 as a result of continued loan growth and pressure on borrowers related to the prevailing poor national economic conditions.
- Impairment charges totaling $898,000 were recognized during the third quarter of 2009 related to three marketable equity securities. Offsetting these impairment charges, the Corporation realized gains on the sale of certain U.S. government agency and mortgage-backed securities totaling $864,000.
- Costs associated with the Titusville branch purchase totaled $592,000 and were recorded during the second and third quarters of 2009. These costs included legal, project management, data conversion and valuation services, printing and mailing costs of required disclosure material, customer check replacement and other conversion costs.
- Stock offering costs totaling $484,000 were recognized during the fourth quarter of 2009 as the Corporation withdrew its common stock offering. These costs were primarily professional fees incurred for legal and accounting services. Also contributing to stock offering costs were fees associated with printing and filing various documents and travel expenses.
- Regular quarterly FDIC insurance premiums increased $402,000 from 2008 to 2009. In addition, the Bank recorded a $178,000 one-time charge during the second quarter of 2009 related to a special assessment that was assessed on all FDIC insured depository institutions.
- The Corporation recorded extraordinary income in 2008 totaling $906,000 associated with the acquisition of ECSLA.
- The Corporation's total assets grew by $91.9 million during 2009, primarily related to the Titusville branch purchase.

Changes in Financial Condition

Total assets increased $91.9 million or 24.5% to $467.5 million at December 31, 2009 from $375.7 million at December 31, 2008. This increase was due primarily to increases in securities available for sale, net loans receivable and cash and equivalents of $33.8 million, $27.8 million and $22.4 million, respectively.

The increase in the Corporation's total assets was primarily funded by increases in total liabilities of $91.0 million or 26.8% and total stockholders' equity of $911,000 or 2.5%. The increase in total liabilities was primarily due to an increase in total deposits of $98.7 million or 34.4%, partially offset by a decrease in borrowed funds of $8.2 million or 17.0%.

Cash and cash equivalents. These accounts increased a combined $22.4 million or 135.1% to $39.0 million at December 31, 2009 from $16.6 million at December 31, 2008. This increase was primarily due to cash received from the Titusville branch office purchase that had not yet been deployed into higher-yielding assets. Typically, cash accounts are increased by net operating results, deposits by customers into savings and checking accounts, loan and security repayments and proceeds from borrowed funds. Decreases result from customer deposit withdrawals, new loan originations or other loan fundings, security purchases, repayments of borrowed funds and cash dividends to stockholders.

Securities. Securities increased $33.8 million or 47.3% to $105.2 million at December 31, 2009 from $71.4 million at December 31, 2008. This increase was primarily related to the partial deployment of cash received from the Titusville branch office purchase into higher-yielding investment securities, offset by security calls, sales and repayments.

Loans receivable. Net loans receivable increased $27.8 million or 10.5% to $292.6 million at December 31, 2009 from $264.8 million at December 31, 2008, primarily related to $32.6 million of loans acquired through the Titusville branch purchase, offset by normal amortization and payoffs. Home equity loans and lines of credit increased $19.8 million or 34.5%, commercial real estate increased $4.3 million or 5.0% and consumer loans increased $3.5 million or 36.7%.

Non-performing assets. Non-performing assets include non-accrual loans, loans 90 days past due and still accruing, repossessions and real estate owned. Non-performing assets were $2.6 million or 0.56% of total assets at December 31, 2009 compared to $1.1 million or 0.28% of total assets at December 31, 2008. Non-performing assets consisted of non-performing loans, repossessions and real estate owned of $2.4 million, $40,000 and $173,000, respectively, at December 31, 2009 and $1.0 million, $0 and $50,000, respectively, at December 31, 2008. This increase in non-performing assets was due to continued pressure on borrowers related to the prevailing poor economic climate. At December 31, 2009, non-performing assets consisted primarily of commercial and residential mortgage loans.

Federal bank stocks. Federal bank stocks were comprised of FHLB stock and FRB stock of $3.5 million and $662,000, respectively, at December 31, 2009. These stocks are purchased and redeemed at par as directed by the federal banks and levels maintained are based primarily on borrowing and other correspondent relationships between the Corporation and the banks. In December 2008, the FHLB notified member banks that it was suspending dividend payments and the repurchase of capital stock. Management evaluated the FHLB stock for impairment and determined that no impairment charge was necessary as of December 31, 2009.

Bank-owned life insurance (BOLI). The Corporation maintains single premium life insurance policies on twenty current and former officers and employees of the Bank. In addition to providing life insurance coverage, whereby the Bank as well as the officers and employees receive life insurance benefits, the appreciation of the cash surrender value of the BOLI will serve to offset and finance existing and future employee benefit costs. Increases in this account during 2009 were associated with an increase in the cash surrender value of the policies, partially offset by certain administrative expenses.

Premises and equipment. Premises and equipment increased $561,000 or 6.5% to $9.2 million at December 31, 2009 from $8.6 million at December 31, 2008. The overall increase in premises and equipment during the year was due to capital expenditures of $1.5 million, partially offset by normal depreciation and amortization of $860,000. Major capital expenditures during the year included the construction of a new building for the Corporation’s East Brady, Pennsylvania branch office and extensive renovations at the Ridgway, Pennsylvania branch office.

Goodwill. Goodwill increased $2.2 million or 157.2% to $3.7 million at December 31, 2009 from $1.4 million at December 31, 2008. In connection with the Titusville branch purchase, the Bank recorded goodwill of $2.2 million. Goodwill represents the excess of the total purchase price paid for the Titusville branch over the fair value of the assets acquired, net of the fair value of the liabilities assumed. The entire amount of goodwill will be tax deductible and amortized over 15 years for income tax purposes. Goodwill will be evaluated for possible impairment at least annually, and more frequently, if events and circumstances indicate that the asset might be impaired.

Core deposit intangible. Core deposit intangible was $2.6 million at December 31, 2009. In connection with the assumption of deposits through the Titusville branch purchase, the Bank recorded a core deposit intangible of $2.8 million. This asset represents the value ascribed to the long-term value of the core deposits acquired. Fair value was determined using a third-party valuation expert specializing in estimating fair values of core deposit intangibles. The fair value was derived using an industry standard financial instrument present value methodology. All-in costs and runoff balances by year were discounted by comparable term FHLB advance rates, used as an alternative cost of funds measure. This intangible asset will be amortized on a double declining balance method of amortization over a weighted average estimated life of nine years. The core deposit intangible asset is not estimated to have a significant residual value. During 2009, the Corporation recorded $203,000 of intangible amortization related to the core deposit intangible.

Deposits. Total deposits increased $98.7 million or 34.4% to $385.3 million at December 31, 2009 from $286.6 million at December 31, 2008. Noninterest bearing deposits increased $10.7 million or 19.0% during the year and interest bearing deposits increased $88.0 million or 38.2%. Overall deposit growth was primarily attributable to the Titusville branch purchase, as deposits assumed with the branch purchase totaled $90.8 million. Organic deposit growth in existing offices totaled $7.9 million or 2.8%.

Borrowed funds. Borrowed funds decreased $8.2 million or 17.0% to $40.0 million at December 31, 2009 from $48.2 million at December 31, 2008 related to a decrease in short-term borrowings.

Stockholders' equity. Stockholders' equity increased $911,000 or 2.5% to $37.0 million at December 31, 2009 from $36.1 million at December 31, 2008 resulting primarily from an increase in retained earnings totaling $127,000 related to net income less preferred and common stock dividends and a decrease in accumulated other comprehensive loss totaling $645,000, resulting primarily from a change in the funded status of the Corporation's defined benefit plan.

Changes in Results of Operations

The Corporation reported net income of $1.5 million and $2.4 million in 2009 and 2008, respectively. The following "Average Balance Sheet and Yield/Rate Analysis" and "Analysis of Changes in Net Interest Income" tables should be utilized in conjunction with the discussion of the net interest income and interest expense components of net income.

Average Balance Sheet and Yield/Rate Analysis. The following table sets forth, for the periods indicated, information concerning the total dollar amounts of interest income from interest-earning assets and the resulting average yields, the total dollar amounts of interest expense on interest-bearing liabilities and the resulting average costs, net interest income, interest rate spread and the net interest margin earned on average interest-earning assets. For purposes of this table, average loan balances include non-accrual loans and exclude the allowance for loan losses and interest income includes accretion of net deferred loan fees. Interest and yields on tax-exempt loans and securities (tax-exempt for federal income tax purposes) are shown on a fully tax equivalent basis. The information is based on average daily balances during the periods presented.

	Year ended December 31,					
	2009			2008		
(Dollar amounts in thousands)	Average Balance	Interest	Yield / Rate	Average Balance	Interest	Yield / Rate
Interest-earning assets:						
Loans, taxable	$ 269,192	$ 16,768	6.23%	$ 240,714	$ 15,906	6.61%
Loans, tax-exempt	14,841	614	4.14%	5,954	370	6.21%
Total loans receivable	284,033	17,382	6.12%	246,668	16,276	6.60%
Securities, taxable	51,227	1,871	3.65%	44,447	1,992	4.48%
Securities, tax-exempt	20,595	1,256	6.10%	14,031	921	6.56%
Total securities	71,822	3,127	4.35%	58,478	2,913	4.98%
Interest-earning deposits with banks	33,107	362	1.09%	7,515	201	2.67%
Federal bank stocks	4,044	28	0.69%	2,868	102	3.56%
Total interest-earning cash equivalents	37,151	390	1.05%	10,383	303	2.92%
Total interest-earning assets	393,006	20,899	5.32%	315,529	19,492	6.18%
Cash and due from banks	2,187			5,512		
Other noninterest-earning assets	18,627			14,928		
Total Assets	$ 413,820			$ 335,969		
Interest-bearing liabilities:						
Interest-bearing demand deposits	$ 125,797	1,049	0.83%	$ 92,208	1,332	1.44%
Time deposits	138,855	4,843	3.49%	121,275	5,083	4.19%
Total interest-bearing deposits	264,652	5,892	2.23%	213,483	6,415	3.00%
Borrowed funds, short-term	15,611	124	0.79%	10,096	182	1.80%
Borrowed funds, long-term	35,000	1,566	4.47%	35,000	1,571	4.49%
Total borrowed funds	50,611	1,690	3.34%	45,096	1,753	3.89%
Total interest-bearing liabilities	315,263	7,582	2.40%	258,579	8,168	3.16%
	58,126	-	-	48,696	-	-

Noninterest-bearing demand deposits						
Funding and cost of funds	373,389	7,582	2.03%	307,275	8,168	2.66%
Other noninterest-bearing liabilities	4,076			2,762		
Total Liabilities	377,465			310,037		
Stockholders' Equity	36,355			25,932		
Total Liabilities and Stockholders' Equity	$ 413,820			$ 335,969		
Net interest income		$ 13,317			$ 11,324	
Interest rate spread (difference between weighted average rate on interest-earning assets and interest-bearing liabilities)			2.92%			3.02%
Net interest margin (net interest income as a percentage of average interest-earning assets)			3.39%			3.59%

Analysis of Changes in Net Interest Income. The following table analyzes the changes in interest income and interest expense in terms of: (1) changes in volume of interest-earning assets and interest-bearing liabilities and (2) changes in yields and rates. The table reflects the extent to which changes in the Corporation's interest income and interest expense are attributable to changes in rate (change in rate multiplied by prior year volume), changes in volume (changes in volume multiplied by prior year rate) and changes attributable to the combined impact of volume/rate (change in rate multiplied by change in volume). The changes attributable to the combined impact of volume/rate are allocated on a consistent basis between the volume and rate variances. Changes in interest income on loans and securities reflect the changes in interest income on a fully tax equivalent basis.

	2009 versus 2008 Increase (decrease) due to		
(Dollar amounts in thousands)	Volume	Rate	Total
Interest income:			
Loans	$ 2,345	$ (1,239)	$ 1,106
Securities	611	(397)	214
Interest-earning deposits with banks	340	(179)	161
Federal bank stocks	30	(104)	(74)
Total interest-earning assets	3,326	(1,919)	1,407
Interest expense:			
Deposits	1,346	(1,869)	(523)
Borrowed funds	200	(263)	(63)
Total interest-bearing liabilities	1,546	(2,132)	(586)
Net interest income	$ 1,780	$ 213	$ 1,993

2009 Results Compared to 2008 Results

The Corporation reported net income before accumulated preferred stock dividends and discount accretion of $1.5 million and $2.4 million for 2009 and 2008, respectively. The $891,000 or 36.6% decrease in net income was attributed to increases in noninterest expense and the provision for loan losses of $1.6 million and $867,000, respectively, partially offset by increases in net interest income and noninterest income of $1.8 million and $343,000, respectively, and a decrease in the provision for income taxes of $298,000. In addition, during 2008, the Corporation recorded extraordinary income totaling $906,000 associated with the ECSLA acquisition.

Net interest income. The primary source of the Corporation's revenue is net interest income. Net interest income is the difference between interest income on earning assets such as loans and securities, and interest expense on liabilities, such as deposits and borrowed funds, used to fund the earning assets. Net interest income is impacted by the volume and composition of interest-earning assets and interest-bearing liabilities, and changes in the level of interest rates. Tax equivalent net interest income increased $2.0 million to $13.3 million for 2009, compared to $11.3 million for 2008. This increase in net interest income can be attributed to an increase in tax equivalent interest income of $1.4 million and a decrease in interest expense of $586,000.

Interest income. Tax equivalent interest income increased $1.4 million or 7.2% to $20.9 million for 2009, compared to $19.5 million for 2008. This increase can be attributed to increases in interest earned on loans, securities and interest-earning deposits of $1.1 million, $214,000, and $161,000, partially offset by a decrease in dividends on federal bank stocks of $74,000.

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Tax equivalent interest earned on loans receivable increased $1.1 million or 6.8% to $17.4 million for 2009, compared to $16.3 million for 2008. During that time, average loans increased $37.4 million or 15.2%, generating $2.3 million of additional loan interest income. The increase in average loans outstanding can primarily be attributable to loans acquired through the Titusville branch purchase. Offsetting this favorable asset growth, the yield on loans decreased 48 basis points to 6.12% for 2009, versus 6.60% for 2008 due to declines in market interest rates throughout 2009 causing a $1.2 million decrease in interest income.

Tax equivalent interest earned on securities increased $214,000 or 7.3% to $3.1 million for 2009, compared to $2.9 million for 2008. During this time, average securities increased $13.3 million or 22.8% accounting for $611,000 in additional security interest income. This increase was primarily related to the deployment of cash received in association with the Titusville branch purchase into higher yielding investment securities. The average yield on securities decreased 63 basis points to 4.35% for 2009, versus 4.98% for 2008 in part due to calls of certain higher rate securities and purchases of shorter term, lower yielding investments.

Interest earned on interest-earning deposit accounts increased $161,000 or 80.1% to $362,000 for 2009, compared to $201,000 for 2008. Average interest-earning deposits increased $25.6 million or 340.6% primarily related to cash received from the Titusville branch purchase and the timing associated with the deployment of that cash. This increase generated $340,000 of additional interest income. Partially offsetting the favorable volume variance, the average yield decreased 158 basis points due primarily to a change in asset mix from primarily certificates of deposit to cash held with the Federal Reserve resulting in a $179,000 decrease in interest income. Interest earned on federal bank stocks decreased $74,000 or 72.6% to $28,000 for 2009, compared to $102,000 for 2008 due to the suspension of dividend payments by the FHLB.

Interest expense. Interest expense decreased $586,000 or 7.2% to $7.6 million for 2009, compared to $8.2 million for 2008. This decrease can be attributed to decreases in interest incurred on interest-bearing deposits and borrowed funds of $523,000 and $63,000, respectively.

Deposit interest expense decreased $523,000 or 8.2% to $5.9 million for 2009, compared to $6.4 million for 2008. Declines in market interest rates caused the rate on interest-bearing deposits to decrease by 77 basis points to 2.23% for 2009 versus 3.00% for 2008 accounting for a $1.9 million decrease in interest expense. Average interest-bearing deposits increased $51.2 million or 24.0%, primarily due to deposits assumed related to the Titusville branch purchase. This increase accounted for $1.3 million in additional interest expense.

Interest expense on borrowed funds decreased $63,000 or 3.6% to $1.7 million for 2009, compared to $1.8 million for 2008. The average rate on borrowed funds decreased 55 basis points to 3.34% for 2009 versus 3.89% for 2008 due to lower short-term borrowing rates in 2009. This decrease in rate accounted for $263,000 of reduced interest expense. Average borrowed funds increased $5.5 million or 12.2% accounting for an increase in interest expense of $200,000.

Provision for loan losses. The Corporation records provisions for loan losses to maintain a level of total allowance for loan losses that management believes, to the best of its knowledge, covers all known and inherent losses that are both probable and reasonably estimable at each reporting date. Management considers historical loss experience, the present and prospective financial condition of borrowers, current conditions (particularly as they relate to markets where the Corporation originates loans), the status of non-performing assets, the estimated underlying value of the collateral and other factors related to the collectability of the loan portfolio.

The provision for loan losses increased $867,000 to $1.4 million for 2009, compared to $500,000 for 2008. The Corporation's allowance for loan losses amounted to $3.2 million or 1.08% of the Corporation's total loan portfolio at December 31, 2009, compared to $2.7 million or 0.99% at December 31, 2008. The allowance for loan losses as a

percentage of non-performing loans at December 31, 2009 and 2008 was 132.4% and 262.2%, respectively. The increase in the provision for loan losses was due to management's estimates of the impact on the loan portfolio of credit defaults related to the continued recessionary economic climate, charge-offs, increases in classified and nonperforming assets and loan growth in general.

Noninterest income. Noninterest income includes revenue that is not related to interest rates, but rather to services rendered and activities conducted in the financial services industry, including fees on depository accounts, general transaction and service fees, commissions on financial services, title premiums, security and loan gains and losses, and earnings on BOLI. Noninterest income increased $343,000 or 13.8% to $2.8 million for 2009, compared to $2.5 million for 2008. This increase was primarily due to a decrease in net losses on securities available for sale. During 2009, the Corporation realized security losses of $898,000 as management determined that three marketable equity securities were impaired. The impairment of these financial industry securities were considered to be other than temporary due to developments in the financial conditions and near-term prospects of the issuers, a downturn of economic conditions of the industry and deteriorating book values of the securities. Offsetting these impairment charges, the Corporation sold several U.S. agency and mortgage-backed securities and realized gains of $864,000. During 2008, the Corporation realized security losses of $391,000 as management determined that two marketable equity securities were impaired.

Noninterest expense. Noninterest expense increased $1.6 million or 14.4% to $12.6 million for 2009, compared to $11.0 million for 2008. This increase in noninterest expense was comprised of increases in premises and equipment, intangible amortization, professional fees, federal deposit insurance and other expenses, partially offset by a decrease in compensation and employee benefits expense.

The largest component of noninterest expense, compensation and employee benefits, decreased $293,000 or 4.6% to $6.1 million for 2009, compared to $6.3 million for 2008. This decrease was primarily due to the elimination of the Corporation's incentive programs as part of its capital management and preservation plan adopted during the first quarter of 2009. In addition, severance charges were recognized in the fourth quarter of 2008, principally associated with the previously disclosed retirement of the Corporation's former Chairman of the Board, President and Chief Executive Officer.

Premises and equipment expense increased $185,000 or 10.8% to $1.9 million for 2009, compared to $1.7 million for 2008, primarily related to costs associated with the Titusville branch purchase.

The Corporation recognized $203,000 of intangible amortization associated with a core deposit intangible asset of $2.8 million that was recorded related to the Titusville branch purchase transaction.

Professional fees increased $791,000 to $1.3 million for 2009, compared to $501,000 for 2008. This increase is attributable to the aforementioned branch purchase and stock offering. Professional fees related to the branch purchase totaled $376,000 and included legal fees, project management fees and conversion assistance costs. Professional fees associated with the stock offering, consisting mainly of legal and accounting fees, were $399,000.

FDIC expense increased $580,000 to $662,000 for 2009, compared to $82,000 for 2008. This was the result of increases in base assessment rates for FDIC insurance premiums and a special assessment that was assessed on all FDIC insured depository institutions in 2009. The special assessment totaled $178,000 and was recognized during the second quarter of 2009.

Other noninterest expense increased $120,000 or 5.0% to $2.5 million for 2009, compared to $2.4 million for 2008 due primarily to $216,000 of costs related to the branch purchase. These included costs associated with customer check and debit card replacement and the printing and mailing of required legal disclosures to affected customers. In addition, $85,000 of costs were recognized related to the stock offering consisting of printing and filing fees, NASDAQ listing fees and travel and other expenses.

The provision for income taxes decreased $298,000 or 83.7% to $58,000 for 2009, compared to $356,000 for 2008 due to lower pre-tax income with an increased portion of pre-tax income being generated from tax-exempt investment securities and loans.

Market Risk Management

Market risk for the Corporation consists primarily of interest rate risk exposure and liquidity risk. The Corporation is not subject to currency exchange risk or commodity price risk, and has no trading portfolio, and therefore, is not subject to any trading risk. In addition, the Corporation does not participate in hedging transactions such as interest rate swaps and caps. Changes in interest rates will impact both income and expense recorded and also the market value of long-term interest-earning assets.

The primary objective of the Corporation's asset liability management function is to maximize the Corporation's net interest income while simultaneously maintaining an acceptable level of interest rate risk given the Corporation's operating environment, capital and liquidity requirements, balance sheet mix, performance objectives and overall business focus. One of the primary measures of the exposure of the Corporation's earnings to interest rate risk is the timing difference between the repricing or maturity of interest-earning assets and the repricing or maturity of its interest-bearing liabilities.

The Corporation's Board of Directors has established a Finance Committee, consisting of four outside directors, the President and Chief Executive Officer (CEO) and the Principal Accounting Officer (PAO), to monitor market risk, including primarily interest rate risk. This committee, which meets at least quarterly, generally establishes and monitors the investment, interest rate risk and asset liability management policies established by the Corporation.

In order to minimize the potential for adverse affects of material and prolonged changes in interest rates on the Corporation's results of operations, the Corporation's management has implemented and continues to monitor asset liability management policies to better match the maturities and repricing terms of the Corporation's interest-earning assets and interest-bearing liabilities. Such policies have consisted primarily of (i) originating adjustable-rate mortgage loans; (ii) originating short-term secured commercial loans with the rate on the loan tied to the prime rate or reset features in which the rate changes at determined intervals; (iii) emphasizing investment in shorter-term (15 years or less) investment securities; (iv) selling longer-term (30-year) fixed-rate residential mortgage loans in the secondary market; (v) maintaining a high level of liquid assets (including securities classified as available for sale) that can be readily reinvested in higher yielding investments should interest rates rise; (vi) emphasizing the retention of lower-costing savings accounts and other core deposits; and (vii) lengthening liabilities and locking in lower borrowing rates with longer terms whenever possible.

Interest Rate Sensitivity Gap Analysis

The implementation of asset and liability initiatives and strategies and compliance with related policies, combined with other external factors such as demand for the Corporation's products and economic and interest rate environments in general, has resulted in the Corporation maintaining a one-year cumulative interest rate sensitivity gap ranging between a positive and negative 20% of total assets. The one-year interest rate sensitivity gap is identified as the difference between the Corporation's interest-earning assets that are scheduled to mature or reprice within one year and its interest-bearing liabilities that are scheduled to mature or reprice within one year.

The interest rate sensitivity gap is defined as the difference between the amount of interest-earning assets maturing or repricing within a specific time period and the amount of interest-bearing liabilities maturing or repricing within that time period. A gap is considered positive when the amount of interest rate-sensitive assets exceeds the amount of interest rate-sensitive liabilities, and is considered negative when the amount of interest rate-sensitive liabilities exceeds the amount of interest rate-sensitive assets. Generally, during a period of rising interest rates, a negative gap would adversely affect net interest income while a positive gap would result in an increase in net interest income. Conversely, during a period of falling interest rates, a negative gap would result in an increase in net interest income and a positive gap would adversely affect net interest income. The closer to zero, or more neutral, that gap is

maintained, generally, the lesser the impact of market interest rate changes on net interest income.

Based on certain assumptions provided by a federal regulatory agency, which management believes most accurately represents the sensitivity of the Corporation's assets and liabilities to interest rate changes, at December 31, 2009, the Corporation's interest-earning assets maturing or repricing within one year totaled $141.0 million while the Corporation's interest-bearing liabilities maturing or repricing within one-year totaled $136.3 million, providing an excess of interest-earning assets over interest-bearing liabilities of $4.8 million or 1.0% of total assets. At December 31, 2009, the percentage of the Corporation's assets to liabilities maturing or repricing within one year was 103.5%.

The following table presents the amounts of interest-earning assets and interest-bearing liabilities outstanding as of December 31, 2009 which are expected to mature, prepay or reprice in each of the future time periods presented:

(Dollar amounts in thousands)	Due in six months or less	Due within six months to one year	Due within one to three years	Due within three to five years	Due in over five years	Total
Total interest-earning assets	$ 108,606	$ 32,399	$ 129,331	$ 81,372	$ 82,653	$ 434,361
Total interest-bearing liabilities	86,715	49,538	92,557	74,712	116,860	420,382
Maturity or repricing gap during the period	$ 21,891	$ (17,139)	$ 36,774	$ 6,660	$ (34,207)	$ 13,979
Cumulative gap	$ 21,891	$ 4,752	$ 41,526	$ 48,186	$ 13,979	
Ratio of gap during the period to total assets	4.68%	(3.67)%	7.87%	1.42%	(7.32)%	
Ratio of cumulative gap to total assets	4.68%	1.02%	8.88%	10.31%	2.99%	
Total assets						$ 467,526

Although certain assets and liabilities may have similar maturities or periods of repricing, they may react in different degrees to changes in market interest rates. The interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types of assets and liabilities may lag behind changes in market interest rates. In the event of a change in interest rates, prepayment and early withdrawal levels would likely deviate significantly from those assumed in calculating the table. The ability of many borrowers to service their debt may decrease in the event of an interest rate increase.

The one-year interest rate sensitivity gap has been the most common industry standard used to measure an institution's interest rate risk position regarding maturities, repricing and prepayments. In recent years, in addition to utilizing interest rate sensitivity gap analysis, the Corporation has increased its emphasis on the utilization of interest rate sensitivity simulation analysis to evaluate and manage interest rate risk.

Interest Rate Sensitivity Simulation Analysis

The Corporation also utilizes income simulation modeling in measuring its interest rate risk and managing its interest rate sensitivity. The Finance Committee of the Corporation believes that simulation modeling enables the Corporation to more accurately evaluate and manage the possible effects on net interest income due to the exposure to changing market interest rates, the slope of the yield curve and different loan and security prepayment and deposit decay

assumptions under various interest rate scenarios.

As with gap analysis and earnings simulation modeling, assumptions about the timing and variability of cash flows are critical in net portfolio equity valuation analysis. Particularly important are the assumptions driving mortgage prepayments and the assumptions about expected attrition of the core deposit portfolios. These assumptions are based on the Corporation's historical experience and industry standards and are applied consistently across the different rate risk measures.

The Corporation has established the following guidelines for assessing interest rate risk:

Net interest income simulation. Given a 200 basis point parallel and gradual increase or decrease in market interest rates, net interest income may not change by more than 25% for a one-year period.

Portfolio equity simulation. Portfolio equity is the net present value of the Corporation's existing assets and liabilities. Given a 200 basis point immediate and permanent increase or decrease in market interest rates, portfolio equity may not correspondingly decrease or increase by more than 30% of stockholders' equity.

These guidelines take into consideration the current interest rate environment, the Corporation's financial asset and financial liability product mix and characteristics and liquidity sources among other factors. Given the current rate environment, a drop in short-term market interest rates of 200 basis points immediately or over a one-year horizon would seem unlikely. This should be considered in evaluating modeling results outlined in the table below.

The following table presents the simulated impact of a 100 basis point or 200 basis point upward or downward shift of market interest rates on net interest income, for the years ended December 31, 2009 and 2008, respectively. This analysis was done assuming that the interest-earning asset and interest-bearing liability levels at December 31, 2009 remained constant. The impact of the market rate movements on net interest income was developed by simulating the effects of rates changing gradually during a one-year period from the December 31, 2009 levels for net interest income.

	Increase		Decrease	
	+100 BP	+200 BP	-100 BP	-200 BP
2009 Net interest income - increase (decrease)	2.64%	4.42%	(5.87)%	(11.02)%
2008 Net interest income - increase (decrease)	2.71%	3.37%	(4.42)%	(7.52)%

Impact of Inflation and Changing Prices

The consolidated financial statements of the Corporation and related notes presented herein have been prepared in accordance with accounting principles generally accepted in the United States of America which require the measurement of financial condition and operating results in terms of historical dollars, without considering changes in the relative purchasing power of money over time due to inflation.

Unlike most industrial companies, substantially all of the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates have a more significant impact on a financial institution's performance than the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services since such prices are affected by inflation to a larger degree than interest rates. In the current interest rate environment, liquidity and the maturity structure of the Corporation's assets and liabilities are critical to the maintenance of acceptable performance levels.

Capital Resources

Total stockholders' equity increased $911,000 or 2.5% to $37.0 million at December 31, 2009 from $36.1 million at December 31, 2008. Net income of $1.5 million in 2009 represented a decrease in earnings of $891,000 or 36.7% compared to 2008. Returns on average equity and assets were 4.23% and 0.37%, respectively, for 2009.

The Corporation has maintained a strong capital position with a capital to assets ratio of 7.9% at December 31, 2009. In an effort to sustain this strong capital position, regular cash dividends on common stock decreased to $1.1 million in 2009 from $1.7 million in 2008. Stockholders have taken part in the Corporation's dividend reinvestment plan introduced during 2003 with 47% of registered shareholder accounts active in the plan at December 31, 2009.

Capital adequacy is intended to enhance the Corporation's ability to support growth while protecting the interest of shareholders and depositors and to ensure that capital ratios are in compliance with regulatory minimum requirements. Regulatory agencies have developed certain capital ratio requirements that are used to assist them in monitoring the safety and soundness of financial institutions. At December 31, 2009, the Corporation and the Bank were in excess of all regulatory capital requirements.

Liquidity

The Corporation's primary sources of funds generally have been deposits obtained through the offices of the Bank, borrowings from the FHLB, and amortization and prepayments of outstanding loans and maturing securities. During 2009, the Corporation used its sources of funds primarily to fund loan commitments. As of December 31, 2009, the Corporation had outstanding loan commitments, including undisbursed loans and amounts available under credit lines, totaling $46.1 million, and standby letters of credit totaling $1.5 million. The Bank is required by the OCC to establish policies to monitor and manage liquidity levels to ensure the Bank's ability to meet demands for customer withdrawals and the repayment of short-term borrowings, and the Bank is currently in compliance with all liquidity policy limits.

At December 31, 2009, time deposits amounted to $164.2 million or 42.6% of the Corporation's total consolidated deposits, including approximately $53.0 million, which are scheduled to mature within the next year. Management of the Corporation believes that the Corporation has adequate resources to fund all of its commitments, that all of its commitments will be funded as required by related maturity dates and that, based upon past experience and current pricing policies, it can adjust the rates of time deposits to retain a substantial portion of maturing liabilities.

Aside from liquidity available from customer deposits or through sales and maturities of securities, the Corporation has alternative sources of funds such as a line of credit and term borrowing capacity from the FHLB and, to a more limited extent, through the sale of loans. At December 31, 2009, the Corporation's borrowing capacity with the FHLB, net of funds borrowed, was $130.3 million.

The Corporation paid quarterly cash dividends over the past two years and determined to reduce the quarterly cash dividend from $0.32 per share to $0.14 per share effective for the second quarter of 2009. The determination of future dividends on the Corporation's common stock will depend on conditions existing at that time with consideration given to the Corporation's earnings, capital and liquidity needs, among other factors.

Management is not aware of any conditions, including any regulatory recommendations or requirements, that would adversely impact its liquidity or its ability to meet funding needs in the ordinary course of business.

Critical Accounting Policies

The Corporation's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and follow general practices within the industry in which it operates. Application of these principles requires management to make estimates or judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates or judgments. Certain policies inherently have a greater reliance on the use of estimates, and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates or judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment write-down or valuation reserve to be established or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by third-party sources, when available. When third-party information is not available, valuation adjustments are estimated in good faith by management primarily though the use of internal cash flow modeling techniques.

The most significant accounting policies followed by the Corporation are presented in Note 1 to the consolidated financial statements. These policies, along with the disclosures presented in the other financial statement notes provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Management views critical accounting policies to be those which are highly dependent on subjective or complex judgments, estimates and assumptions and where changes in those estimates and assumptions could have a significant impact on the financial statements. Management has identified the following as critical accounting policies.

Allowance for loan losses. The Corporation considers that the determination of the allowance for loan losses involves a higher degree of judgment and complexity than its other significant accounting policies. The balance in the allowance for loan losses is determined based on management's review and evaluation of the loan portfolio in relation to past loss experience, the size and composition of the portfolio, current economic events and conditions and other pertinent factors, including management's assumptions as to future delinquencies, recoveries and losses. All of these factors may be susceptible to significant change. Among the many factors affecting the allowance for loan losses, some are quantitative while others require qualitative judgment. Although management believes its process for determining the allowance adequately considers all of the potential factors that could potentially result in credit losses, the process includes subjective elements and may be susceptible to significant change. To the extent actual outcomes differ from management's estimates, additional provisions for loan losses may be required that would adversely impact the Corporation's financial condition or earnings in future periods.

Other-than-temporary impairment. Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic, market or other concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near term prospects of the issuer, (3) the intent of the Corporation to sell a security, and (4) whether it is more likely than not the Corporation will have to sell the security before recovery of its cost basis.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Information required by this item is included in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in item 7.

Item 8. Financial Statements and Supplementary Data

Information required by this item is included herein beginning on page F-1.

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

On February 17, 2010, the Corporation's Board of Directors dismissed its independent auditors, ParenteBeard LLC (ParenteBeard). ParenteBeard will complete its engagement as independent auditor for the Corporation's fiscal year ended December 31, 2009 upon the filing of the Corporation's Form 10-K for the year ended December 31, 2009. ParenteBeard's report on the Corporation's consolidated financial statements during the two most recent fiscal years preceding the date hereof contained no adverse opinion or a disclaimer of opinions, and was not qualified or modified as to uncertainty, audit scope or accounting principles. The decision to change accountants was approved by the Corporation's Audit Committee. During the last two fiscal years and the subsequent interim period to the date hereof, there were no disagreements between the Corporation and ParenteBeard on any matters of accounting principles or practices, financial statement disclosure, or auditing scope or principles, which disagreement(s), if not resolved to the satisfaction of ParenteBeard, would have caused it to make a reference to the subject matter of the disagreement(s) in connection with its reports. None of the "reportable events" described in Item 304(a)(1)(v) of Regulation S-K occurred with respect to the Corporation within the last two fiscal years and the subsequent interim period to the date hereof.

Effective February 17, 2010, the Corporation engaged Crowe Horwath LLP (Crowe Horwath) as its independent auditors for the fiscal year ending December 31, 2010. The Corporation engaged Crowe Horwath to perform limited non-audit services related to the years ending December 31, 2009 and 2008. The services performed during this period included preparation of consolidated federal and state tax returns, assisting management with quarterly estimated tax payments, effective tax rates, deferred tax inventory, tax related journal entries and discussions on tax matters related to a branch acquisition. On occasion, Crowe Horwath also informally discussed with management of the Corporation general accounting topics and/or issues.

The nature of Crowe Horwath's involvement with the Corporation as indicated above did not result in any conclusion on the type of audit opinion(s) rendered or to be rendered, views expressed, management's final decisions as to the accounting, auditing or financial reporting requirements nor a disagreement or reportable event.

Item 9A(T). Controls and Procedures

The Corporation maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Corporation's Exchange Act reports is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Corporation's management, including its CEO and PAO, as appropriate, to allow timely decisions regarding required disclosure based on the definition of "disclosure controls and procedures" in Rule 13a-15(e).

As of December 31, 2009, the Corporation carried out an evaluation, under the supervision and with the participation of the Corporation's management, including the Corporation's CEO and PAO, of the effectiveness of the design and operation of the Corporation's disclosure controls and procedures. Based on the foregoing, the Corporation's CEO and PAO concluded that the Corporation's disclosure controls and procedures were effective.

There have been no significant changes in the Corporation's internal controls or in other factors that could significantly affect the internal controls subsequent to the date the Corporation completed its valuation.

During the fourth quarter of fiscal year 2009, there has been no change made in the Corporation's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Corporation's internal control over financial reporting.

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Corporation. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Management completed an assessment of the Corporation's internal control over financial reporting as of December 31, 2009. This assessment was based on criteria for evaluating internal control over financial reporting established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management concluded that the Corporation's internal control over financial reporting was effective as of December 31, 2009.

This annual report does not include an attestation report of the Corporation's registered public accounting firm regarding internal control over financial reporting. The Corporation's internal control over financial reporting was not subject to attestation by the Corporation's registered public accounting firm pursuant to temporary rules of the SEC that permit the Corporation to provide only management's report in this annual report.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

The information required by this item is incorporated herein by reference to the sections captioned "Principal Beneficial Owners of the Corporation's Common Stock", "Section 16(a) Beneficial Ownership Reporting Compliance" and "Information With Respect to Nominees For Director, Continuing Director and Executive Officers" in the Corporation's definitive proxy statement for the Corporation's Annual Meeting of Stockholders to be held on April 28, 2010 (the Proxy Statement) which will be filed no later than 120 days following the Corporation's fiscal year end.

The Corporation maintains a Code of Personal and Business Conduct and Ethics (the Code) that applies to all employees, including the CEO and the PAO. A copy of the Code has previously been filed with the SEC and is posted on our website at www.farmersnb.com. Any waiver of the Code with respect to the CEO and the PAO will be publicly disclosed in accordance with applicable regulations.

Item 11. Executive Compensation

The information required by this item is incorporated herein by reference to the section captioned "Executive Compensation" in the Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by this item is incorporated herein by reference to the section captioned "Principal Beneficial Owners of the Corporation's Common Stock" in the Proxy Statement.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required by this item is incorporated herein by reference to the sections captioned "Information With Respect to Nominees For Director, Continuing Directors and Executive Officers" and "Executive Compensation" in the Proxy Statement.

Item 14. Principal Accountant Fees and Services

The information required by this item is incorporated herein by reference to the section captioned “Relationship With Independent Registered Public Accounting Firm” in the Proxy Statement.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a)(1)-(2) Financial Statements and Schedules:

(i) The financial statements required in response to this item are incorporated by reference from Item 8 of this report.

(3) Management Contracts or Compensatory Plans:

(i) Exhibits 10.1-10.6 listed below in (b) identify management contracts or compensatory plans or arrangements required to be filed as exhibits to this report, and such listing is incorporated herein by reference.

(b) Exhibits are either attached as part of this Report or incorporated herein by reference.

2.1	Agreement and Plan of Merger by and between Emclaire Financial Corp. and Elk County Savings and Loan Association. (1)
3.1	Articles of Incorporation of Emclaire Financial Corp. (2)
3.2	Bylaws of Emclaire Financial Corp. (2)
3.3	Statement with respect to shares for Preferred Stock. (3)
4.0	Specimen Stock Certificate of Emclaire Financial Corp. (4)
4.1	Form of certificate for Preferred Stock. (3)
4.2	Warrant for purchase of shares of Common Stock. (3)
10.1	Employment Agreement between Emclaire Financial Corp., the Farmers National Bank of Emlenton and certain executive officers, dated as of July 1, 2007. (5)
10.2	Change in Control Agreement between Emclaire Financial Corp., the Farmers National Bank of Emlenton and certain executive officers, dated as of July 1, 2007. (5)
10.3	Change in Control Agreement between Emclaire Financial Corp., the Farmers National Bank of Emlenton and certain executive officer, dated as of May 12, 2008.
10.4	Group Term Carve-Out Plan between the Farmers National Bank of Emlenton and 20 Officers and Employees. (6)
10.5	Supplemental Executive Retirement Plan Agreement between the Farmers National Bank of Emlenton and Six Officers. (6)
10.6	Adoption of Farmers National Bank of Emlenton Deferred Compensation Plan. (7)
10.7	Letter Agreement, dated December 23, 2008 between the Corporation and the U.S. Department of the Treasury. (3)

11.0 Statement regarding computation of earnings per share (see Note 1 of the Notes to Consolidated Financial Statements in the Annual Report).

13.0	Annual Report to Stockholders for the fiscal year ended December 31, 2009.
14.0	Code of Personal and Business Conduct and Ethics. (8)
20.0	Emclaire Financial Corp. Dividend Reinvestment and Stock Purchase Plan. (9)
21.0	Subsidiaries of the Registrant (see information contained herein under “Item 1. Description of Business - Subsidiary Activity”).
31.1	Principal Executive Officer 302 Certification.
31.2	Principal Accounting Officer 302 Certification.
32.1	Principal Executive Officer 906 Certification.
32.2	Principal Accounting Officer 906 Certification.
99.1	Principal Executive Officer 111 Certification.
99.2	Principal Financial Officer 111 Certification.

(1) Incorporated by reference to the Registrant’s Current Report on Form 8-K dated October 20, 2008.
(2) Incorporated by reference to the Registrant’s Registration Statement on Form SB-2, as amended, (File No. 333-11773) declared effective by the SEC on October 25, 1996.
(3) Incorporated by reference to the Registrant’s Current Report on Form 8-K dated December 23, 2008.
(4) Incorporated by reference to the Registrant’s Annual Report on Form 10-K for the year ended December 31, 1997.
(5) Incorporated by reference to the Registrant’s Current Report on Form 8-K dated June 21, 2007.
(6) Incorporated by reference to the Registrant’s Annual Report on Form 10-K for the year ended December 31, 2002.
(7) Incorporated by reference to the Registrant’s Current Report on Form 8-K dated December 15, 2008.
(8) Incorporated by reference to the Registrant’s Annual Report on Form 10-K for the year ended December 31, 2004.
(9) Incorporated by reference to the Registrant’s Annual Report on Form 10-K for the year ended December 31, 2001.

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.

EMCLAIRE FINANCIAL CORP.

Dated: March 22, 2010

By: /s/ William C. Marsh
William C. Marsh
Chairman, Chief Executive Officer, President and Director
(Duly Authorized Representative)

Pursuant to the requirement of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

By: /s/ William C. Marsh
William C. Marsh
Chairman of the Board
Chief Executive Officer
President
Director
(Principal Executive Officer)

Date: March 22, 2010

By: /s/ Amanda L. Engles
Amanda L. Engles
Treasurer
(Principal Accounting Officer)

Date: March 22, 2010

By: /s/ Ronald L. Ashbaugh
Ronald L. Ashbaugh
Director

Date: March 22, 2010

By: /s/ David L. Cox
David L. Cox
Director

Date: March 22, 2010

By: /s/ James M. Crooks
James M. Crooks
Director

Date: March 22, 2010

By: /s/ George W. Freeman
George W. Freeman
Director

Date: March 22, 2010

By: /s/ Mark A. Freemer
Mark A. Freemer
Director

Date: March 22, 2010

By: /s/ Robert L. Hunter
Robert L. Hunter
Director

Date: March 22, 2010

By: /s/ John B. Mason
John B. Mason
Director

Date: March 22, 2010

By: /s/ Brian C. McCarrier
Brian C. McCarrier
Director

Date: March 22, 2010

Financial Statements
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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Emclaire Financial Corp.
Emlenton, Pennsylvania

We have audited the accompanying consolidated balance sheets of Emclaire Financial Corp. and subsidiaries (the "Corporation") as of December 31, 2009 and 2008, and the related consolidated statements of income, changes in stockholders' equity and comprehensive income, and cash flows for each of the years in the two-year period ended December 31, 2009. Emclaire Financial Corp.'s management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Corporation is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Emclaire Financial Corp. and subsidiaries as of December 31, 2009 and 2008, and the results of their operations and their cash flows for each of the years in the two-year period ended December 31, 2009, in conformity with accounting principles generally accepted in the United States of America.

/s/ ParenteBeard LLC
Pittsburgh, Pennsylvania
March 22, 2010

Consolidated Balance Sheets

(Dollar amounts in thousands, except share data)

	December 31, 2009	2008
Assets		
Cash and due from banks	$ 2,822	$ 4,292
Interest earning deposits with banks	36,130	12,279
Total cash and cash equivalents	38,952	16,571
Securities available for sale, at fair value	105,243	71,443
Loans receivable, net of allowance for loan losses of $3,202 and $2,651	292,615	264,838
Federal bank stocks, at cost	4,125	3,797
Bank-owned life insurance	5,388	5,186
Accrued interest receivable	1,574	1,519
Premises and equipment, net	9,170	8,609
Goodwill	3,657	1,422
Core deposit intangible	2,585	-
Prepaid expenses and other assets	4,217	2,279
Total Assets	$ 467,526	$ 375,664
Liabilities and Stockholders' Equity		
Liabilities		
Deposits:		
Non-interest bearing	$ 67,033	$ 56,351
Interest bearing	318,292	230,296
Total deposits	385,325	286,647
Borrowed funds:		
Short-term	5,000	13,188
Long-term	35,000	35,000
Total borrowed funds	40,000	48,188
Accrued interest payable	711	761
Accrued expenses and other liabilities	4,456	3,945
Total Liabilities	430,492	339,541
Commitments and Contingencies	-	-
Stockholders' Equity		
Preferred stock, $1.00 par value, 3,000,000 shares authorized; 7,500 shares issued and outstanding	7,430	7,412
Warrants	88	88
Common stock, $1.25 par value, 12,000,000 shares authorized; 1,559,421 shares issued; 1,431,404 shares outstanding	1,949	1,949
Additional paid-in capital	14,685	14,564
Treasury stock, at cost; 128,017 shares	(2,653)	(2,653)
Retained earnings	15,967	15,840
Accumulated other comprehensive loss	(432)	(1,077)
Total Stockholders' Equity	37,034	36,123
Total Liabilities and Stockholders' Equity	$ 467,526	$ 375,664

See accompanying notes to consolidated financial statements.

Consolidated Statements of Income

(Dollar amounts in thousands, except share data)

	Year ended December 31, 2009	2008
Interest and dividend income		
Loans receivable, including fees	$ 17,203	$ 16,162
Securities:		
Taxable	1,871	1,992
Exempt from federal income tax	870	636
Federal bank stocks	28	102
Deposits with banks	362	201
Total interest and dividend income	20,334	19,093
Interest expense		
Deposits	5,892	6,415
Short-term borrowed funds	124	182
Long-term borrowed funds	1,566	1,571
Total interest expense	7,582	8,168
Net interest income	12,752	10,925
Provision for loan losses	1,367	500
Net interest income after provision for loan losses	11,385	10,425
Noninterest income		
Fees and service charges	1,495	1,638
Commissions on financial services	389	449
Title premiums	62	-
Other-than-temporary impairment losses on equity securities	(898)	(391)
Net gain on sales of loans	4	6
Net gain on sales of available for sale securities	864	-
Earnings on bank-owned life insurance	232	227
Other	682	558
Total noninterest income	2,830	2,487
Noninterest expense		
Compensation and employee benefits	6,054	6,347
Premises and equipment	1,899	1,714
Intangible asset amortization	203	-
Professional fees	1,292	501
Federal deposit insurance	662	82
Other	2,508	2,388
Total noninterest expense	12,618	11,032
Income before provision for income taxes and extraordinary item	1,597	1,880
Provision for income taxes	58	356
Income before extraordinary item	1,539	1,524
Extraordinary item, gain on business combination	-	906
Net income	1,539	2,430
Accumulated preferred stock dividends and discount accretion	393	-
Net income available to common stockholders	$ 1,146	$ 2,430
Earnings per common share		
Net income before extraordinary item	$ 0.80	$ 1.17

Extraordinary item, gain on business combination		-		0.70
Net income (basic)	$	0.80	$	1.87
Net income (diluted)	$	0.80	$	1.87

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Stockholders' Equity

(Dollar amounts in thousands, except share data)

	Preferred Stock	Warrants	Common Stock	Additional Paid-in Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance at January 1, 2008	$ -	$ -	$ 1,745	$ 10,902	$ (2,653)	$ 15,114	$ (405)	$ 24,703
Comprehensive income:								
Net income						2,430		2,430
Change in net unrealized losses on securities available for sale, net of taxes of $129							251	251
Change in funded status of defined benefit plan, net of taxes of ($475)							(923)	(923)
Comprehensive income								1,758
Issuance of common stock			204	3,549				3,753
Issuance of preferred stock	7,412							7,412
Issuance of warrants		88						88
Stock compensation expense				113				113
Cash dividends declared on common stock ($1.30 per share)						(1,704)		(1,704)
Balance at December 31, 2008	7,412	88	1,949	14,564	(2,653)	15,840	(1,077)	36,123
Comprehensive income:								
Net income						1,539		1,539
Change in net unrealized losses on securities available for sale, for which a portion of an other than temporary impairment has been recognized in earnings, net of taxes of $145							280	280
Change in net unrealized losses on securities available for sale, net of taxes of ($70)							(135)	(135)
Change in funded status of defined benefit plan, net of taxes of $258							500	500
Comprehensive income								2,184
Stock compensation expense				121				121

Preferred dividends and amortization of discount						(353)		(335)
Cash dividends declared on common stock ($0.74 per share)						(1,059)		(1,059)
Balance at December 31, 2009	$ 7,430	$ 88	$ 1,949	$ 14,685	$ (2,653)	$ 15,967	$ (432)	$ 37,034

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(Dollar amounts in thousands, except share data)

	Year ended December 31,	
	2009	2008
Cash flows from operating activities		
Net income	$ 1,539	$ 2,430
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of premises and equipment	860	737
Provision for loan losses	1,367	500
Amortization of premiums and (accretion of discounts), net	176	(161)
Amortization of intangible assets and mortgage servicing rights	220	17
Securities impairment loss recognized in earnings	898	391
Realized gains on sales of available for sale securities, net	(864)	-
Net gains on sales of loans	(4)	(6)
Net (gains) losses on foreclosed real estate	4	(96)
Net gains on sales of bank premises and equipment	(16)	-
Originations of loans sold	(159)	(1,209)
Proceeds from the sale of loans	163	1,215
Restricted stock and stock option compensation	121	113
Increase in bank-owned life insurance, net	(202)	(199)
(Increase) decrease in accrued interest receivable	88	(154)
Increase in deferred taxes	(286)	(433)
Increase in prepaid expenses and other assets	(1,627)	(913)
Decrease in accrued interest payable	(50)	(10)
Increase in accrued expenses and other liabilities	1,011	1,438
Net cash provided by operating activities	3,239	3,660
Cash flows from investing activities		
Loan originations and principal collections, net	2,784	(35,818)
Available for sale securities:		
Sales	20,513	-
Maturities, repayments and calls	40,697	70,999
Purchases	(94,720)	(90,361)
Purchase of federal bank stocks	(328)	(1,135)
Proceeds from the sale of bank premises and equipment	203	-
Proceeds from the sale of foreclosed real estate	99	463
Net cash received in branch acquisition	54,923	-
Purchases of premises and equipment	(1,530)	(1,442)
Net cash provided by (used in) investing activities	22,641	(57,294)
Cash flows from financing activities		
Net increase in deposits	6,083	42,385
Net change in short-term borrowings	(8,188)	7,788
Proceeds from sale of preferred stock	-	7,412
Issuance of warrants	-	88
Proceeds from sale of common stock	-	3,753
Dividends paid	(1,394)	(1,704)
Net cash provided by (used in) financing activities	(3,499)	59,722
Net increase in cash and cash equivalents	22,381	6,088
Cash and cash equivalents at beginning of period	16,571	10,483

Cash and cash equivalents at end of period	$ 38,952	$ 16,571
Supplemental information:		
Interest paid	$ 7,632	$ 8,178
Income taxes paid	183	805
Supplemental noncash disclosures:		
Transfers from loans to foreclosed real estate	227	288
Summary of branch acquisition:		
Fair value of deposits assumed	92,596	-
Less: Fair value of tangible assets acquired	32,673	-
Cash received in acquisition	54,923	-
Goodwill and other intangibles recorded	$ 5,000	$ -

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies

Basis of Presentation and Consolidation. The consolidated financial statements include the accounts of Emclaire Financial Corp. (the Corporation) and its wholly owned subsidiaries, the Farmers National Bank of Emlenton (the Bank) and Emclaire Settlement Services, LLC (the Title Company). All significant intercompany balances and transactions have been eliminated in consolidation.

Nature of Operations. The Corporation provides a variety of financial services to individuals and businesses through its offices in Western Pennsylvania. Its primary deposit products are checking, savings and term certificate accounts and its primary lending products are residential and commercial mortgages, commercial business loans and consumer loans.

Use of Estimates and Classifications. In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP), management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, fair value of financial instruments, goodwill, the valuation of deferred tax assets and other than temporary impairment charges. Certain amounts previously reported may have been reclassified to conform to the current year financial statement presentation. Such reclassifications did not affect net income or stockholders' equity.

Significant Group Concentrations of Credit Risk. Most of the Corporation's activities are with customers located within the Western Pennsylvania region of the country. Note 4 discusses the type of securities that the Corporation invests in. Note 5 discusses the types of lending the Corporation engages in. The Corporation does not have any significant concentrations to any one industry or customer.

Cash Equivalents. For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash on hand, cash items, interest-earning deposits with other financial institutions and federal funds sold and due from correspondent banks. Interest-earning deposits mature within one year and are carried at cost. Federal funds are generally sold or purchased for one day periods. Net cash flows are reported for loan and deposit transactions.

Restrictions on Cash. Cash on hand or on deposit with the Federal Reserve Bank of Cleveland (FRB) of approximately $60,000 was required to meet regulatory reserve and clearing requirements at December 31, 2009 and 2008. Both required and excess reserves earn interest.

Securities. Debt securities are classified as available for sale when they might be sold before maturity. Equity securities with readily determinable fair values are classified as available for sale. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized using the interest method over the term of the securities. Gains and losses on sales are recorded on the trade date and determined using the specific identification method.

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Securities (continued). Management evaluates securities for other-than-temporary impairment (OTTI) at least on a quarterly basis, and more frequently when economic or market conditions warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near term prospects of the issuer, (3) the intent of the Corporation to sell a security, and (4) whether it is more likely than not the Corporation will have to sell the security before recovery of its cost basis. If the Corporation intends to sell an impaired security, or if it is more likely than not the Corporation will have to sell the security before recovery of its cost basis, the Corporation records an other-than-temporary loss in an amount equal to the entire difference between fair value and amortized cost. Otherwise, only the credit portion of the estimated loss on debt securities is recognized in earnings, with the other portion of the loss recognized in other comprehensive income.

Loans Held for Sale. Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income. Loans held for sale are generally sold with servicing rights retained. The carrying value of such loans sold is reduced by the cost allocated to the servicing rights. Gains and losses on sales of mortgage loans are based on the difference between the selling price and the carrying value of the related loan sold.

Loans Receivable. The Corporation grants mortgage, commercial and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans throughout Western Pennsylvania. The ability of the Corporation's debtors to honor their contracts is dependent upon real estate and general economic conditions in this area.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or net pay-off generally are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans or premiums or discounts on purchased loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, and premiums and discounts are deferred and recognized as an adjustment of the related loan yield using the interest method.

The accrual of interest on loans is typically discontinued at the time the loan is 90 days past due unless the credit is well secured and in the process of collection. Loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual status or charged-off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan Losses. The allowance for loan losses is established for probable credit losses through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are typically credited to the allowance.

1. Summary of Significant Accounting Policies (continued)

Allowance for Loan Losses (continued). The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of loans in light of historic experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as doubtful, substandard or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

A loan is considered impaired when, based on current information and events, it is probable that the Corporation will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial loans by either the present value of expected future cash flows discounted at the loans effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Large groups of small balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Corporation does not separately identify individual consumer and residential mortgage loans for impairment disclosures, unless such loans are the subject of a restructuring agreement.

Federal Bank Stocks. The Bank is a member of the Federal Home Loan Bank of Pittsburgh (FHLB) and the FRB. As a member of these federal banking systems, the Bank maintains an investment in the capital stock of the respective regional banks, at cost. These stocks are purchased and redeemed at par as directed by the federal banks and levels maintained are based primarily on borrowing and other correspondent relationships.

Bank-Owned Life Insurance (BOLI). The Bank purchased life insurance policies on certain key officers and employees. BOLI is recorded at its cash surrender value, or the amount that can be realized.

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Premises and Equipment. Land is carried at cost. Premises, furniture and equipment, and leasehold improvements are carried at cost less accumulated depreciation or amortization. Depreciation is calculated on a straight-line basis over the estimated useful lives of the related assets, which are twenty-five to fifty years for buildings and three to ten years for furniture and equipment. Amortization of leasehold improvements is computed using the straight-line method over the shorter of their estimated useful life or the expected term of the leases. Expected terms include lease option periods to the extent that the exercise of such option is reasonably assured. Premises and equipment are reviewed for impairment when events indicate their carrying amount may not be recoverable from future undiscounted cash flows. If impaired, assets are recorded at fair value.

Goodwill and Intangible Assets. Goodwill results from business acquisitions and represents the excess of the purchase price over the fair value of acquired assets and liabilities. Core deposit intangible assets arise from whole bank or branch acquisitions and are measured at fair value and then are amortized over their estimated lives, generally less than ten years. Customer relationship intangible assets arise from the purchase of a customer list from another company or individual and then are amortized on a straight-line basis over two years. Goodwill is not amortized and is assessed at least annually for impairment and any such impairment will be recognized in the period identified.

Servicing Assets. Servicing assets represent the allocated value of retained servicing rights on loans sold. Servicing assets are expensed in proportion to, and over the period of, estimated net servicing revenues. Impairment is evaluated based on the fair value of the assets, using groupings of the underlying loans as to interest rates. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. Any impairment of a grouping is reported as a valuation allowance, to the extent that fair value is less than the capitalized amount for a grouping.

Real Estate Acquired Through Foreclosure (REO). Real estate properties acquired through foreclosure are initially recorded at fair value less cost to sell at the date of foreclosure, establishing a new cost basis. After foreclosure, valuations are periodically performed by management and the real estate is carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations of the properties, gains and losses on sales and additions to the valuation allowance are included in operating results. Real estate acquired through foreclosure is classified in prepaid expenses and other assets and totaled $173,000 and $50,000 at December 31, 2009 and 2008, respectively.

Treasury Stock. Common stock purchased for treasury is recorded at cost. At the date of subsequent reissue, the treasury stock account is reduced by the cost of such stock on the first-in, first-out basis.

Income Taxes. Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the temporary differences between the book and tax basis of the various balance sheet assets and liabilities and gives current recognition to changes in tax rate and laws.

1. Summary of Significant Accounting Policies (continued)

Earnings Per Common Share (EPS). EPS on income before extraordinary income is computed by dividing income before extraordinary item by the weighted average number of common shares outstanding during the period and EPS on the extraordinary item is computed by dividing the extraordinary item by the weighted average number of common shares outstanding during the period. Basic EPS excludes dilution and is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted EPS reflects the potential dilution that could occur if securities or contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Corporation. Options and restricted stock awards of 107,500 shares of common stock and warrants to purchase 50,111 shares of common stock were not included in computing diluted earnings per share because their effects were not dilutive.

Comprehensive Income. Comprehensive income includes net income from operating results and the net change in accumulated other comprehensive income. Accumulated other comprehensive income (loss) is comprised of unrealized holding gains and losses on securities available for sale and the over funded or under funded status of pension and other postretirement benefit plans on the balance sheet. The effects of other comprehensive income are presented as part of the statement of changes in stockholders' equity.

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

Retirement Plans. The Corporation maintains a noncontributory defined benefit plan covering substantially all employees and officers. Effective January 1, 2009 the plan was closed to new participants. The plan calls for benefits to be paid to eligible employees at retirement based primarily on years of service and compensation rates near retirement. The Corporation also maintains a 401(k) plan, which covers substantially all employees, and a supplemental executive retirement plan for key executive officers.

Stock Compensation Plans. The Corporation follows guidance issued by the Financial Accounting Standards Board (FASB) requiring that the compensation cost relating to share-based payment transactions be recognized in financial statements. The cost is measured based on the fair value of the equity or liability instruments issued. The guidance covers a wide range of share-based compensation arrangements including stock options, restricted share plans, performance-based awards, share appreciation rights and employee share purchase plans. An entity is required to measure the cost of employee services received in exchange for the stock options based on the grant-date fair value of the award, and to recognize the cost over the period the employee is required to provide services for the award. An entity may use any option-pricing model that meets the fair value objective of the guidance.

Transfers of Financial Assets. Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Corporation, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Corporation does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

1. Summary of Significant Accounting Policies (continued)

Off-Balance Sheet Financial Instruments. In the ordinary course of business, the Corporation has entered into off-balance sheet financial instruments, consisting of commitments to extend credit, commitments under line of credit lending arrangements and letters of credit. Such financial instruments are recorded in the financial statements when they are funded or related fees are received.

Fair Value of Financial Instruments. Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Recently Adopted Accounting Standards. In June 2009, the FASB replaced The Hierarchy of Generally Accepted Accounting Principles, with the FASB Accounting Standards Codification (the Codification) as the single source of authoritative GAAP recognized by the FASB to be applied by nongovernmental entities. The Codification reorganizes all previous GAAP pronouncements into roughly 90 accounting topics and displays all topics using a consistent structure. All existing standards that were used to create the Codification have been superseded, replacing the previous references to specific Statements of Financial Accounting Standards (SFAS) with numbers used in the Codification's structural organization. The guidance was effective for interim and annual periods ending after September 15, 2009. After September 15, 2009, only one level of authoritative GAAP exists, other than guidance issued by the Securities and Exchange Commission (SEC). All other accounting literature excluded from the Codification is considered non-authoritative. The adoption of the Codification does not have a material impact on the Corporation's consolidated financial statements.

In September 2006, the FASB issued guidance that defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This guidance also establishes a fair value hierarchy about the assumptions used to measure fair value and clarifies assumptions about risk and the effect of a restriction on the sale or use of an asset. The guidance was effective for fiscal years beginning after November 15, 2007. In February 2008, the FASB issued guidance that delayed the effective date of this fair value guidance for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value on a recurring basis to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years. The adoption of this guidance did not have a material impact on the Corporation's consolidated financial statements.

In December 2007, the FASB issued guidance that requires an acquirer to recognize assets acquired, liabilities assumed, and any noncontrolling interest in the acquiree at the acquisition date, measured at their fair values as of that date. The guidance requires prospective application for business combinations consummated in fiscal years beginning on or after December 15, 2009. The branch purchase described in Note 2 was accounted for under this guidance.

In December 2008, the FASB issued guidance requiring additional disclosures about plan assets in an employer's defined benefit pension and other postretirement plans. The required disclosures have been included in Note 14.

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Recently Adopted Accounting Standards (continued). In April 2009, the FASB issued guidance amending the previous OTTI guidance for debt securities and included additional presentation and disclosure requirements for both debt and equity securities. The guidance was effective for interim reporting periods ending after June 15, 2009. The adoption of this guidance requires an adjustment to retained earnings and other comprehensive income in the period of adoption to reclassify non-credit related impairment to other comprehensive income for debt securities that the Corporation does not have the intent to sell and will not more likely than not be required to sell. The adoption of this guidance did not have a material impact on the Corporation's consolidated financial statements.

In April 2009, the FASB issued guidance that emphasizes that the objective of a fair value measurement does not change even when market activity for the asset or liability has decreased significantly. Fair value is the price that would be received for an asset sold or paid to transfer a 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. When observable transactions or quoted prices are not considered orderly, then little, if any, weight should be assigned to the indication of the asset or liability's fair value. Adjustments to those transactions or prices should be applied to determine the appropriate fair value. The adoption of this guidance was effective for interim and annual reporting periods ending after June 15, 2009 and did not have a material impact on the Corporation's consolidated financial statements.

In May 2009, the FASB issued guidance that establishes general standards of accounting for and disclosure of subsequent events. Subsequent events are events that occur after the balance sheet date but before financial statements are issued or are available to be issued. Events occurring subsequent to the date of the balance sheet have been evaluated for potential recognition or disclosure in the consolidated financial statements through the date of the filing of the consolidated financial statements with the SEC. In February 2010, the FASB issued amendments to this guidance clarifying which entities are required to evaluate subsequent events through the date the financial statements are issued and the scope of subsequent events disclosures. This amendment removes the requirement for an SEC filer to disclose the date through which subsequent events have been evaluated in both issued and revised financial statements. Except as noted in the guidance, all amendments or additions to this guidance were effective upon issuance. The adoption of this guidance did not have a material impact on the Corporation's consolidated financial statements.

In August 2009, the FASB amended existing guidance related to the measurement of liabilities that are recognized or disclosed at fair value on a recurring basis. This amendment clarifies how a corporation should measure the fair value of liabilities and that restrictions preventing the transfer of a liability should not be considered as a factor in the measurement of liabilities. The adoption of this guidance did not have a material impact on the Corporation's consolidated financial statements.

2. Business Combinations

On April 6, 2009, the Bank entered into a Purchase and Assumption Agreement with National City Bank (National City) and PNC Financial Services Group, Inc. (PNC) where the Bank agreed to acquire certain assets and assume certain liabilities of one National City branch office located in Titusville, Pennsylvania. The Board of Governors of the Federal Reserve System and U.S. Department of Justice required National City to divest of this and other branch locations in connection with of its acquisition by PNC.

The primary purpose of the Titusville branch acquisition was to expand the Bank's presence into a new market with demographics consistent with its current market area. The deposits assumed through the Titusville branch acquisition have a favorable composition mix and the loans acquired currently present limited risk since none of these loans are presently greater than thirty days past due. The Titusville branch acquisition is expected to result in increased earnings and provide additional liquidity that has been used to payoff certain short-term borrowings and to fund future loan and securities growth.

On August 28, 2009, the Bank completed the Titusville branch acquisition and assumed $90.8 million of deposits and acquired $32.6 million of loans and $58.0 million in cash, as well as certain fixed assets associated with the branch office. The Bank retained all existing employees of the office.

The $90.8 million of deposits assumed in the branch acquisition consisted of, approximately $47.9 million of certificates of deposit, or 53% of the deposits assumed, $23.9 million of interest bearing checking, savings and money market accounts, or 26% of the deposits assumed, and $19.0 million of non-interest bearing accounts, or 21% of the deposits assumed. The interest rates on interest bearing checking, savings and money market accounts were adjusted to the Bank's current deposit rates. The interest rates and maturities on the certificates of deposit were assumed at stated contractual terms. Also at the closing of the acquisition, the Bank assumed the obligations under the Titusville branch property lease.

In connection with the assumption of deposits, the Bank recorded a core deposit intangible of $2.8 million. This asset represents the value ascribed to the long-term value of the core deposits acquired. Fair value was determined using a third-party valuation expert specializing in estimating fair values of core deposit intangibles. The fair value was derived using an industry standard financial instrument present value methodology. All-in costs and runoff balances by year were discounted by comparable term FHLB advance rates, used as an alternative cost of funds measure. This intangible asset will be amortized on a double declining balance method of amortization over a weighted average estimated life of nine years. The core deposit intangible asset is not estimated to have a significant residual value.

The $32.6 million of loans acquired consisted of approximately $20.3 million of home equity loans, or 63% of the loans acquired, $9.9 million of commercial loans, or 30% of the loans acquired and $2.4 million of consumer loans, or 7% of the loans acquired. Of the loans acquired, approximately 50% are fixed rate loans and 50% are variable rate loans. The Bank did not acquire any subprime loans and generally did not receive any loans that had a delinquency status of greater than 30 days as of the date of closing.

The Bank's payment of the 3.4% premium on the assumed deposits and the purchase price for the acquired loans and other assets of the Titusville branch office was made through a reduction of the cash received from National City to fund the deposits assumed by the Bank. Net of this premium paid, the Bank received a cash settlement amount of approximately $54.9 million from National City.

Notes to Consolidated Financial Statements (continued)

2. Business Combinations (continued)

In connection with the branch acquisition, the Bank recorded goodwill of $2.2 million. Goodwill represents the excess of the total purchase price paid for the Titusville branch over the fair value of the assets acquired, net of the fair value of the liabilities assumed. The entire amount of goodwill will be tax deductible and amortized over 15 years for income tax purposes. Goodwill will be evaluated for possible impairment at least annually, and more frequently, if events and circumstances indicate that the asset might be impaired.

The Corporation recorded the following assets and liabilities in connection with the branch purchase as of August 28, 2009:

(Dollar amounts in thousands)	Assets Acquired and Liabilities Assumed	Acquisition Adjustments
Assets:		
Cash and cash equivalents	$ 58,017	$ (3,094)(1)
Loans receivable, net of allowance for loan losses	32,553	(101)(2)
Premises and equipment, net	78	-
Goodwill	-	2,213(3)
Other intangible assets	-	2,787(4)
Prepaid expenses and other assets	143	-
	$ 90,791	$ 1,805
Liabilities and Stockholders' Equity:		
Deposits		
Non-interest bearing	$ 18,974	$ -
Interest bearing	71,817	1,805(5)
	$ 90,791	$ 1,805

(1) Represents a deposit premium paid of approxiamtely 3.4% of the average daily balance of the assumed deposits for the thirty calendar day period ending on and including the second business day prior to the closing date.
(2) The purchase accounting adjustment on loans relates to the fair value adjustment that includes an interest rate component and a credit adjustment for estimated lifetime losses.
(3) The goodwill adjustment relates to the recording of acquired assets and assumed liabilities at fair value.
(4) Represents the estimated fair value of the core deposit intangible asset (approximately 6.5% of core deposits) associated with deposits assumed. The core deposit intangible is being amortized using the double declining balance method of amortization over nine years.
(5) The purchase accounting adjustment on deposits relates to the fair value adjustment of the certificates of deposit.

On October 17, 2008, the Corporation completed an acquisition of Elk County Savings and Loan Association (ECSLA), a Pennsylvania-chartered savings association located in Ridgway, Pennsylvania. ECSLA converted from the mutual to the stock form of organization and immediately issued all of its capital stock to the Corporation and merged with and into the Bank. In connection with the merger, the Corporation issued 163,569 shares of its common stock at a price of $21.15 per share, resulting in proceeds of $3,459,484, net of discount on common stock of $293,279.

Notes to Consolidated Financial Statements (continued)

2. Business Combinations (continued)

The Corporation recorded the following assets and liabilities of ECSLA as of October 17, 2008. These amounts represent the carrying value of ECSLA's assets and liabilities adjusted to reflect the fair value at the date of the acquisition. The discounts and premiums resulting from the fair value adjustments are being accreted and amortized on a level yield basis over the anticipated lives of the underlying financial assets or liabilities. This amortization of premiums and discounts did not have a material impact on the Corporation's results of operations and is not projected to have a material impact on future periods.

(Dollar amounts in thousands)		Acquired on October 17, 2008
Assets		
Cash and cash equivalents	$	504
Securities available for sale		283
Loans receivable, net of allowance for loan losses of $206		7,321
Federal bank stocks, at cost		44
Other assets		47
Total assets acquired	$	8,199
Liabilities		
Deposits	$	6,221
Other liabilities		119
Total liabilities assumed	$	6,340

The excess fair value of assets acquired over liabilities assumed, less transaction costs incurred, resulted in negative goodwill of $906,000. This negative goodwill is reflected as an extraordinary item in the Corporation's consolidated financial statements.

The primary purpose of the ECSLA acquisition was to expand the Corporation's deposit market share in Ridgway and to provide additional capital to the Bank. The Corporation's deposit market share approximately doubled and capital was added through the negative goodwill generated and the issuance of common stock.

3. Participation in the U.S. Department of the Treasury (U.S. Treasury) Capital Purchase Program (CPP)

The Corporation entered into a Securities Purchase Agreement (the Agreement) on December 23, 2008 with the U.S. Treasury In association with its participation in the CPP of the Emergency Economic Stabilization Act of 2008 (EESA). Pursuant to the agreement, the Corporation sold 7,500 shares of Senior Perpetual Preferred Stock, par value $1.00 per share, having a liquidation amount equal to $1,000.00 per share, with an attached warrant to purchase 50,111 shares of the Corporation's common stock, par value $1.25 per share, for the aggregate price of $7.5 million, to the U.S. Treasury.

The preferred stock qualifies as Tier 1 capital and will pay cumulative dividends at a rate of 5% per year, for the first five years, and 9% per year thereafter. Under the terms of the CPP, the preferred stock may be redeemed with the approval of the Federal Reserve in the first three years with the proceeds from the issuance of certain qualifying Tier 1 capital or after three years at par value plus accrued and unpaid dividends.

The warrant has a 10-year term with an exercise price equal to $22.45 per share of common stock.

Notes to Consolidated Financial Statements (continued)

4. Securities

The following table summarizes the Corporation's securities as of December 31:

(Dollar amounts in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale:				
December 31, 2009:				
U.S. Treasury and federal agency	$ 2,976	$ 25	$ -	$ 3,001
U.S. government sponsored entities and agencies	50,953	113	(269)	50,797
Mortgage-backed securities: residential	16,459	109	(38)	16,530
Collateralized mortgage obligations	5,130	4	(4)	5,130
State and political subdivision	26,271	696	-	26,967
Equity securities	3,003	-	(185)	2,818
	$ 104,792	$ 947	$ (496)	$ 105,243
December 31, 2008:				
U.S. government sponsored entities and agencies	$ 19,985	$ 139	$ (47)	$ 20,077
Mortgage-backed securities: residential	16,672	546	-	17,218
Collateralized mortgage obligations	13,134	40	(12)	13,162
State and political subdivision	13,543	270	(5)	13,808
Corporate securities	3,984	-	-	3,984
Equity securities	3,893	-	(699)	3,194
	$ 71,211	$ 995	$ (763)	$ 71,443

Gains on sales of available for sale securities for the years ended December 31 were as follows:

(Dollar amounts in thousands)	2009	2008
Proceeds	$ 20,513	$ -
Gross gains	864	-
Tax provision related to gains	294	-

The following table summarizes scheduled maturities of the Corporation's securities as of December 31, 2009:

(Dollar amounts in thousands)	Available for sale	
	Amortized Cost	Fair Value
Due in one year or less	$ 104	$ 105
Due after one year through five years	50,787	50,731
Due after five through ten years	19,921	20,255
Due after ten years	30,977	31,334

No scheduled maturity	3,003	2,818
	$ 104,792	$ 105,243

Notes to Consolidated Financial Statements (continued)

4. Securities (continued)

Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

Securities with carrying values of $20.7 million and $13.0 million as of December 31, 2009 and 2008, respectively, were pledged to secure public deposits and for other purposes required or permitted by law.

Information pertaining to securities with gross unrealized losses at December 31, 2009 and 2008 aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

(Dollar amounts in thousands)	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
December 31, 2009:						
U.S. government sponsored entities and agencies	$ 32,716	$ (269)	$ -	$ -	$ 32,716	$ (269)
Mortgage-backed securities: residential	1,961	(38)	-	-	1,961	(38)
Collateralized mortgage obligations	1,275	(2)	910	(2)	2,185	(4)
Equity securities	1,341	(110)	686	(75)	2,027	(185)
	$ 37,293	$ (419)	$ 1,596	$ (77)	$ 38,889	$ (496)
December 31, 2008:						
U.S. government sponsored entities and agencies	$ 6,452	$ (47)	$ -	$ -	$ 6,452	$ (47)
Collateralized mortgage obligations	9,185	(12)	-	-	9,185	(12)
State and political subdivision	2,352	(5)	-	-	2,352	(5)
Equity securities	-	-	3,128	(699)	3,128	(699)
	$ 17,989	$ (64)	$ 3,128	$ (699)	$ 21,117	$ (763)

Management evaluates securities for OTTI at least on a quarterly basis, and more frequently when economic, market or other concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near term prospects of the issuer, (3) the intent of the Corporation to sell a security, and (4) whether it is more likely than not the Corporation will have to sell the security before recovery of its cost basis.

During 2009, after evaluation of the securities portfolio, management determined that other-than-temporary impairments existed on three financial institution equity securities. The impairment of these securities was considered to be other-than-temporary due to continued concerns related to the financial condition and near-term prospects of the issuers, economic conditions of the financial services industry and deteriorating market values. These securities were written down to their fair market values as of September 30, 2009 and the resulting impairment losses of $898,000 were recognized in earnings during the third quarter of 2009.

During 2008, management evaluated the Corporation's investment portfolio and determined that OTTI existed on Fannie Mae and Freddie Mac stocks. The impairment of these securities was considered to be other-than-temporary due to continued concerns related to the financial condition and near-term prospects of the issuers, economic conditions of the financial services industry and deteriorating market values. These securities were written down to their fair market value as of June 30, 2008 and again as of September 30, 2008. The resulting impairment losses of $391,000 were recognized in earnings during the second and third quarters of 2008.

4. Securities (continued)

The following table presents information related to the Corporation's gains and losses on the sales of equity and debt securities, and losses recognized for the OTTI of investments:

(Dollar amounts in thousands)	Gross Realized Gains	Gross Realized Losses	Other-than-temporary Impairment Losses	Net Gains (Losses)
Year ended December 31, 2009:				
Equity securities	$ -	$ -	$ (898)	$ (898)
Debt securities	864	-	-	864
	$ 864	$ -	$ (898)	$ (34)
Year ended December 31, 2008:				
Equity securities	$ -	$ -	$ (391)	$ (391)
Debt securities	-	-	-	-
	$ -	$ -	$ (391)	$ (391)

After realizing the impairment charges on the aforementioned equity securities, there were 33 debt securities and seven equity securities in an unrealized loss position as of December 31, 2009. For investments in equity securities, in addition to the general factors mentioned above for determining whether the decline in market value is other-than-temporary, the analysis of whether an equity security is other-than-temporarily impaired includes review of the profitability and the capital adequacy and all information available to determine the credit quality of each issuer. Based on that evaluation, and given that the Corporation's current intention is not to sell any impaired securities and it is more likely than not it will not be required to sell these securities before the recovery of its amortized cost basis, the Corporation does not consider those seven equity securities with unrealized losses as of December 31, 2009 to be other-than-temporarily impaired.

For debt securities, an additional and critical component of the evaluation for OTTI is the identification of credit impaired securities where it is likely that the Corporation will not receive cash flows sufficient to recover the entire amortized cost basis of the security. Based on that evaluation and other general considerations, and given that the Corporation's current intention is not to sell any impaired securities and it is more likely than not it will not be required to sell these securities before the recovery of its amortized cost basis, the Corporation does not consider those 33 debt securities with unrealized losses as of December 31, 2009 to be other-than-temporarily impaired.

Notes to Consolidated Financial Statements (continued)

5. Loans Receivable

The following table summarizes the Corporation's loans receivable as of December 31:

(Dollar amounts in thousands)	2009	2008
Mortgage loans on real estate:		
Residential first mortgages	$ 74,099	$ 74,130
Home equity loans and lines of credit	77,284	57,454
Commercial real estate	89,952	85,689
	241,335	217,273
Other loans:		
Commercial business	41,588	40,787
Consumer	12,894	9,429
	54,482	50,216
Total loans, gross	295,817	267,489
Less allowance for loan losses	3,202	2,651
Total loans, net	$ 292,615	$ 264,838

Following is an analysis of the changes in the allowance for loan losses for the years ended December 31:

(Dollar amounts in thousands)	2009	2008
Balance at the beginning of the year	$ 2,651	$ 2,157
Allowance for loan losses of ECSLA	-	206
Provision for loan losses	1,367	500
Charge-offs	(859)	(252)
Recoveries	43	40
Balance at the end of the year	$ 3,202	$ 2,651

Non-performing loans, which include primarily non-accrual loans, were $2.4 million and $1.0 million at December 31, 2009 and 2008, respectively. The Corporation is not committed to lend significant additional funds to debtors whose loans are on non-accrual status. At December 31, 2009, the recorded investment in loans considered to be impaired was $740,000. Of the impaired loans at December 31, 2009, loans with a recorded investment of $590,000 required a specific valuation allowance of $128,000. During 2009, impaired loans averaged $533,000. The Corporation recognized interest income on impaired loans of approximately $71,000 on a cash basis, during 2009. The Corporation did not have any impaired loans during the year ending December 31, 2008. Nonperforming loans and impaired loans are defined differently. Some loans may be included in both categories whereas other loans may be included in only one category.

The Corporation is required to maintain qualifying collateral with the FHLB to secure all outstanding loans. Loans with book values of $135.4 million and $140.0 million as of December 31, 2009 and 2008, respectively, were pledged as qualifying collateral. The Corporation was in compliance with all FHLB credit policies at December 31, 2009.

Notes to Consolidated Financial Statements (continued)

5. Loans Receivable (continued)

The Corporation was servicing residential mortgage loans with unpaid principal balances of $6.7 million and $7.9 million at December 31, 2009 and 2008, respectively, for a third party investor. In addition, the Corporation was servicing commercial loans with unpaid principal balances of $2.7 million and $4.8 million at December 2009 and 2008, respectively, for third party investors. Such loans are not reflected in the consolidated balance sheet and servicing operations result in the generation of annual fee income of approximately 0.25% of the unpaid principal balances of such loans.

6. Federal Bank Stocks

The Bank is a member of the FHLB and the FRB. As a member of these federal banking systems, the Bank maintains an investment in the capital stock of the respective regional banks, at cost. These stocks are purchased and redeemed at par as directed by the federal banks and levels maintained are based primarily on borrowing and other correspondent relationships. The Bank's investment in FHLB and FRB stocks was $3.5 million and $662,000, respectively, at December 31, 2009, and $3.5 million and $333,000, respectively, at December 31, 2008. In December 2008, the FHLB notified member banks that it was suspending dividend payments and the repurchase of capital stock.

Management evaluated the FHLB capital stock for impairment in accordance with relevant accounting guidance. Management's determination of whether these investments are impaired is based on their assessment of the ultimate recoverability of their cost rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of their cost is influenced by criteria such as: (1) the significance of the decline in net assets of the FHLB as compared to the capital stock amount for the FHLB and the length of time this situation has persisted, (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB, and (3) the impact of legislative and regulatory changes on institutions and, accordingly, on the customer base of the FHLB.

Management believes no impairment charge is necessary related to the FHLB capital stock as of December 31, 2009.

7. Premises and Equipment

Premises and equipment at December 31 are summarized by major classification as follows:

(Dollar amounts in thousands)	2009	2008
Land	$ 1,623	$ 1,403
Buildings and improvements	7,364	6,710
Leasehold improvements	750	744
Furniture, fixtures and equipment	5,056	4,757
Software	2,342	2,105
Construction in progress	537	714
	17,672	16,432
Less accumulated depreciation and amortization	8,502	7,823
	$ 9,170	$ 8,609

Notes to Consolidated Financial Statements (continued)

7. Premises and Equipment (continued)

Depreciation and amortization expense for the years ended December 31, 2009 and 2008 were $860,000 and $737,000, respectively.

Rent expense under non-cancelable operating lease agreements for the years ended December 31, 2009 and 2008 was $146,000 and $120,000, respectively. Rent commitments under non-cancelable long-term operating lease agreements for certain branch offices for the years ended December 31, are as follows, before considering renewal options that are generally present:

(Dollar amounts in thousands)	Amount
2010	$ 197
2011	172
2012	124
2013	96
2014	96
Thereafter	11
	$ 696

8. Goodwill and Intangible Assets

The following table summarizes the Corporation's acquired goodwill and intangible assets as of December 31:

(Dollar amounts in thousands)	2009		2008	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Goodwill	$ 3,657	$ -	$ 1,422	$ -
Core deposit intangibles	4,027	1,443	1,240	1,240
Other customer relationship intangibles	20	20	20	20
Total	$ 7,704	$ 1,463	$ 2,682	$ 1,260

As discussed in Note 2, the Bank completed a branch purchase transaction during the third quarter of 2009. In connection with the branch purchase, the Bank recorded initial goodwill of $2.2 million. After the initial goodwill was recorded, the Corporation recorded $23,000 of additional credit adjustments on certain loans acquired and adjusted the goodwill related to the branch purchase. Goodwill represents the excess of the total purchase price paid for the Titusville branch purchase over the fair value of the assets acquired, net of the fair value of the liabilities assumed. Goodwill is not amortized but is evaluated for impairment on an annual basis or whenever events or changes in circumstances indicate the carrying value may not be recoverable. No goodwill impairment charges were recorded in 2009.

Also, in connection with the assumption of deposits, the Bank recorded a core deposit intangible of $2.8 million. This intangible asset will be amortized using the double declining balance method over a weighted average estimated life of nine years. The core deposit intangible asset is not estimated to have a significant residual value. During 2009, the Corporation recorded intangible amortization expense totaling $203,000.

Notes to Consolidated Financial Statements (continued)

8. Goodwill and Intangible Assets (continued)

The estimated amortization expense of the core deposit intangible for the years ending December 31, are as follows:

(Dollar amounts in thousands)	Amortization Expense
2010	$ 564
2011	441
2012	345
2013	271
2014	217
Thereafter	746
	$ 2,584

9. Related Party Balances and Transactions

In the ordinary course of business, the Bank maintains loan and deposit relationships with employees, principal officers and directors. The Bank has granted loans to principal officers and directors and their affiliates amounting to $1.3 million and $1.1 million at December 31, 2009 and 2008, respectively. During 2009, total principal additions and total principal repayments associated with these loans were $379,000 and $156,000, respectively. Deposits from principal officers and directors held by the Bank at December 31, 2009 and 2008 totaled $2.3 million and $1.6 million, respectively.

In addition, directors and their affiliates may provide certain professional and other services to the Corporation and the Bank in the ordinary course of business at market fee rates. During 2009 and 2008, amounts paid to affiliates for such services totaled $51,000 and $174,000, respectively.

10. Deposits

The following table summarizes the Corporation's deposits as of December 31:

(Dollar amounts in thousands)	2009			2008		
Type of accounts	Weighted average rate	Amount	%	Weighted average rate	Amount	%
Non-interest bearing deposits	-	$ 67,033	17.4%	-	$ 56,351	19.7%
Interest bearing demand deposits	0.56%	154,085	40.0%	1.31%	106,042	37.0%
Time deposits	3.25%	164,207	42.6%	3.97%	124,254	43.3%
	1.61%	$ 385,325	100.0%	2.21%	$ 286,647	100.0%

The Corporation had a total of $49.3 million and $38.8 million in time deposits of $100,000 or more at December 31, 2009 and 2008, respectively.

Notes to Consolidated Financial Statements (continued)

10. Deposits (continued)

Scheduled maturities of time deposits for the next five years are as follows:

(Dollar amounts in thousands)	Amount	%
2010	$ 53,007	32.3%
2011	32,521	19.8%
2012	20,370	12.4%
2013	39,620	24.1%
2014	16,084	9.8%
Thereafter	2,604	1.6%
	$ 164,207	100.0%

11. Borrowed Funds

The following table summarizes the Corporation's borrowed funds as of and for the year ended December 31:

(Dollar amounts in thousands)	2009				2008			
	Balance	Average Balance	Average Rate	Weighted average rate	Balance	Average Balance	Average Rate	Weighted average rate
Due within 12 months	$ 5,000	$ 15,611	2.69%	0.79%	$ 13,188	$ 10,096	2.20%	1.80%
Due beyond 12 months but within 5 years	15,000	15,000	4.13%	4.19%	15,000	15,000	4.13%	4.19%
Due beyond 5 years but within 10 years	20,000	20,000	4.64%	4.69%	20,000	20,000	4.64%	4.71%
	$ 40,000	$ 50,611			$ 48,188	$ 45,096		

Short-term borrowed funds at December 31, 2009 consisted of a $5.0 million advance on a line of credit with Atlantic Central Bankers Bank. The line of credit has an interest rate equal to the greater of 4.75% or prime plus 0.5%.

Long-term borrowed funds at December 31, 2009 consist of seven, $5.0 million term advances. The term advances mature between November 2011 and October 2017. If these advances convert to adjustable rate borrowings, the Corporation has the opportunity to repay the advances without penalty at or after the conversion date. All borrowings from the FHLB are secured by a blanket lien of qualified collateral.

The initial three $5.0 million borrowings have rates of 4.61%, 3.74% and 4.04%, respectively, although the rates may adjust quarterly at the option of the FHLB to the then three month LIBOR plus 20, 22 or 25 basis points, respectively, but only if the three month LIBOR exceeds 8.0%.

Notes to Consolidated Financial Statements (continued)

11. Borrowed Funds (continued)

In addition, the Corporation borrowed four additional $5.0 million 10 year term advances at initial interest rates of 4.98%, 4.83%,4.68% and 4.09%, respectively. Two of these borrowings are fixed for the first two years of the term after which the rates may adjust at the option of the FHLB to the then three month LIBOR rate plus 24 basis points. The third borrowing is also fixed for the first two years of the initial term after which the rates may adjust at the option of the FHLB to the then three month LIBOR plus 24 basis points, but only if the three month LIBOR exceeds 6.0%. The final borrowing is fixed for the first three years of the term after which the rates may adjust at the option of the FHLB to the then three month LIBOR rate plus 13 basis points.

Scheduled maturities of borrowed funds for the next five years are as follows:

(Dollar amounts in thousands)	Amount
2010	$ 5,000
2011	5,000
2012	5,000
2013	5,000
2014	-
Thereafter	20,000
	$ 40,000

The Bank maintains a credit arrangement with the FHLB as a source of additional liquidity. The total maximum borrowing capacity with the FHLB, excluding loans outstanding, at December 31, 2009 was $130.3 million. In addition, the Corporation has $500,000 and the Bank has $2.0 million of funds available on unused lines of credit through another correspondent bank.

12. Insurance of Accounts and Regulatory Matters

Insurance of Accounts

The deposits of the Bank have historically been insured by the Federal Deposit Insurance Corporation (FDIC) up to $100,000 per insured depositor, except certain types of retirement accounts, which are insured up to $250,000 per insured depositor. On October 3, 2008, the maximum amount insured under FDIC deposit insurance was temporarily increased from $100,000 to $250,000 per insured depositor through December 31, 2009. In May 2009, the FDIC extended this increased insurance level of $250,000 per depositor through December 31, 2013. After December 31, 2013, the standard insurance amount will return to $100,000 for all deposit categories except certain retirement accounts, which will continue to be insured up to $250,000 per insured depositor. To provide this insurance, the Bank must pay an annual premium and is required to maintain certain minimum levels of regulatory capital as outlined below.

Additionally, the Bank has elected to participate in the FDIC's Temporary Liquidity Guarantee Program. Under this program, all noninterest bearing deposit transaction accounts, lawyers' trust accounts and NOW accounts that pay interest rates equal to or less than 50 basis points and public funds held in noninterest bearing accounts with balances over $250,000 will also be fully insured through June 30, 2010.

Notes to Consolidated Financial Statements (continued)

12. Insurance of Accounts and Regulatory Matters (continued)

Restrictions on Dividends, Loans and Advances

The Bank is subject to a regulatory dividend restriction that generally limits the amount of dividends that can be paid by the Bank to the Corporation. Prior regulatory approval is required if the total of all dividends declared in any calendar year exceeds net profits (as defined in the regulations) for the year combined with net retained earnings (as defined) for the two preceding calendar years. In addition, dividends paid by the Bank to the Corporation would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum capital requirements. As of December 31, 2009, $2.0 million of undistributed earnings of the Corporation was available for distribution of dividends without prior regulatory approval.

Loans or advances from the Bank to the Corporation are limited to 10% of the Bank's capital stock and surplus on a secured basis. Funds available for loans or advances by the Bank to the Corporation amounted to approximately $2.7 million. The Corporation has a $2.2 million commercial line of credit available at the Bank for the primary purpose of purchasing qualified equity investments. At December 31, 2009, the Corporation had an outstanding balance on this line of $1.1 million.

Minimum Regulatory Capital Requirements

The Corporation (on a consolidated basis) and the Bank are 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 the Corporation's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Corporation and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Quantitative measures established by regulation to ensure capital adequacy require the Corporation and the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined).

As of December 31, 2009, the most recent notification from the FDIC categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following table. There are no conditions or events since the notification that management believes have changed the Bank's category.

Notes to Consolidated Financial Statements (continued)

12. Insurance of Accounts and Regulatory Matters (continued)

The following table sets forth certain information concerning regulatory capital of the consolidated Corporation and the Bank as of the dates presented:

(Dollar amounts in thousands)	December 31, 2009				December 31, 2008			
	Consolidated		Bank		Consolidated		Bank	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital to risk-weighted assets:								
Actual	$ 34,838	12.53%	$ 37,224	13.54%	$ 38,727	13.85%	$ 36,069	13.01%
For capital adequacy purposes	22,242	8.00%	21,987	8.00%	22,369	8.00%	22,174	8.00%
To be well capitalized	N/A	N/A	27,484	10.00%	N/A	N/A	27,718	10.00%
Tier 1 capital to risk-weighted assets:								
Actual	$ 31,636	11.38%	$ 34,022	12.38%	$ 36,386	13.01%	$ 33,422	12.06%
For capital adequacy purposes	11,121	4.00%	10,994	4.00%	11,184	4.00%	11,087	4.00%
To be well capitalized	N/A	N/A	16,491	6.00%	N/A	N/A	16,631	6.00%
Tier 1 capital to average assets:								
Actual	$ 31,636	6.91%	$ 34,022	7.48%	$ 36,386	10.88%	$ 33,422	9.21%
For capital adequacy purposes	18,320	4.00%	18,186	4.00%	13,382	4.00%	14,523	4.00%
To be well capitalized	N/A	N/A	22,732	5.00%	N/A	N/A	18,154	5.00%

13. Commitments and Legal Contingencies

In the ordinary course of business, the Corporation has various outstanding commitments and contingent liabilities that are not reflected in the accompanying consolidated financial statements. In addition, the Corporation is involved in certain claims and legal actions arising in the ordinary course of business. The outcome of these claims and actions are not presently determinable; however, in the opinion of the Corporation's management, after consulting legal counsel, the ultimate disposition of these matters will not have a material adverse effect on the consolidated financial statements.

14. Income Taxes

The Corporation and the Bank file a consolidated federal income tax return. The provision for income taxes for the years ended December 31 is comprised of the following:

(Dollar amounts in thousands)	2009	2008
Current	$ 344	$ 789
Deferred	(286)	(433)
	$ 58	$ 356

Notes to Consolidated Financial Statements (continued)

14. Income Taxes (continued)

A reconciliation between the provision for income taxes and the amount computed by multiplying operating results before income taxes by the statutory federal income tax rate of 34% for the years ended December 31 is as follows:

(Dollar amounts in thousands)	2009		2008	
	Amount	% Pre-tax Income	Amount	% Pre-tax Income
Provision at statutory tax rate	$ 543	34.0%	$ 947	34.0%
Increase (decrease) resulting from:				
Tax free interest, net of disallowance	(396)	(24.8)%	(270)	(9.7)%
Earnings on BOLI	(69)	(4.3)%	(68)	(2.4)%
Effect of extraordinary gain	-	0.0%	(308)	(11.1)%
Other, net	(20)	(1.3)%	55	2.0%
Provision	$ 58	3.6%	$ 356	12.8%

The tax effects of temporary differences between the financial reporting basis and income tax basis of assets and liabilities that are included in the net deferred tax asset as of December 31 relate to the following:

(Dollar amounts in thousands)	2009	2008
Deferred tax assets:		
Allowance for loan losses	$ 990	$ 848
Securities impairment	438	133
SFAS 158 pension accrual	376	633
Intangible assets	183	87
Other	104	6
Accrued pension cost	79	252
Stock options	77	49
Nonaccrual loan interest income	52	-
Accrued contract termination fees	-	122
Gross deferred tax assets	2,299	2,130
Deferred tax liabilities:		
	-	-
Depreciation	567	446
Stock gain	172	172
Net unrealized gains on securities	153	79
Prepaid expenses	123	91
Deferred loan fees	63	57
Purchase accounting adjustments	62	75
Loan servicing	14	20
Gross deferred tax liabilities	1,154	940
Net deferred tax asset	$ 1,145	$ 1,190

Notes to Consolidated Financial Statements (continued)

14. Income Taxes (continued)

In accordance with relevant accounting guidance, the Corporation determined that it was not required to establish a valuation allowance for deferred tax assets since it is more likely than not that the deferred tax asset will be realized through carry-back to taxable income in prior years, future reversals of existing taxable temporary differences, tax strategies and, to a lesser extent, future taxable income. The Corporation's net deferred tax asset is recorded in the consolidated financial statements as a component of other assets.

At December 31, 2009 and December 31, 2008, the Corporation had no unrecognized tax benefits recorded. The Corporation does not expect the total amount of unrecognized tax benefits to significantly increase within the next twelve months. The Corporation recognizes interest and penalties on unrecognized tax benefits in income taxes expense in its Consolidated Statements of Income.

The Corporation and the Bank are subject to U.S. federal income tax as well as a capital-based franchise tax in the Commonwealth of Pennsylvania. The Corporation and the Bank are no longer subject to examination by taxing authorities for years before 2006.

Notes to Consolidated Financial Statements (continued)

15. Employee Benefit Plans

Defined Benefit Plan

The Corporation provides pension benefits for eligible employees through a defined benefit pension plan. Substantially all employees participate in the retirement plan on a non-contributing basis, and are fully vested after three years of service. Effective January 1, 2009, the plan was closed to new participants. The Corporation uses December 31 as the measurement date for its plan. Information pertaining to changes in obligations and funded status of the defined benefit pension plan for the years ended December 31 is as follows:

(Dollar amounts in thousands)	2009	2008
Change in plan assets:		
Fair value of plan assets at beginning of year	$ 3,226	$ 3,883
Actual (loss) return on plan assets	673	(727)
Employer contribution	350	335
Benefits paid	(262)	(265)
Fair value of plan assets at end of year	3,987	3,226
Change in benefit obligation:		
Benefit obligation at beginning of year	5,115	4,508
Service cost	296	233
Interest cost	281	285
Actuarial loss	-	8
Effect of change in assumptions	(299)	346
Benefits paid	(262)	(265)
Benefit obligation at end of year	5,131	5,115
Funded status (plan assets less benefit obligation)	(1,144)	(1,889)
Unrecognized prior service cost	(210)	(241)
Unrecognized net actuarial gain	1,314	2,104
Accrued pension cost	$ (40)	$ (26)
Amounts recognized in accumulated other comprehensive loss, net of tax, consists of:		
Accumulated net actuarial loss	$ 867	$ 1,388
Accumulated prior service benefit	(138)	(159)
Amount recognized, end of year	$ 729	$ 1,229

The following table presents the Corporation's pension plan assets measured and recorded at estimated fair value on a recurring basis and their level within the estimated fair value hierarchy as described in Note 17 as of December 31, 2009:

(Dollar amounts in thousands) Description	Total	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
Cash and cash equivalents	$ 545	$ 545	$ -	$ -
Fixed income	1,660	-	1,660	-

Equity mutual funds - domestic	1,581	1,581	-	-
Equity mutual funds - international	201	201	-	-
	$ 3,987	$ 2,327	$ 1,660	$ -

Notes to Consolidated Financial Statements (continued)

15. Employee Benefit Plans (continued)

Amounts recognized in balance sheet as of December 31 consist of:

(Dollar amounts in thousands)	Pension Benefits	
	2009	2008
Accrued benefit cost	$ (40)	$ (26)
Accumulated other comprehensive loss	(1,104)	(1,863)
Net amount recognized	$ (1,144)	$ (1,889)

The accumulated benefit obligation for the defined benefit pension plan was $5.1 million at both December 31, 2009 and 2008.

The components of the periodic pension costs for the years ended December 31 are as follows:

(Dollar amounts in thousands)	2009	2008
Service cost	$ 296	$ 233
Interest cost	281	285
Expected return on plan assets	(258)	(305)
Amortization of prior service cost and actuarial expense	44	(12)
Net periodic pension cost	$ 363	$ 201

Weighted-average actuarial assumptions for the years ended December 31 include the following:

	2009	2008
Discount rate for net periodic benefit cost	6.00%	6.50%
Discount rate for benefit obligations	6.00%	6.00%
Rate of increase in future compensation levels	3.50%	3.50%
Expected rate of return on plan assets	7.75%	7.75%

The Corporation’s pension plan asset allocation at December 31, 2009 and 2008, target allocation for 2010, and expected long-term rate of return by asset category are as follows:

Asset Category	Target Allocation 2010	Percentage of Plan Assets at Year End 2009	2008	Weighted-Average Expected Long-Term Rate of Return 2009
Equity Securities	43%	43%	47%	5.5%
Debt Securities	43%	43%	24%	1.8%
Other	14%	14%	29%	0.5%
	100%	100%	100%	7.75%

Notes to Consolidated Financial Statements (continued)

15. Employee Benefit Plans (continued)

The intent of the Plan is to provide a range of investment options for building a diversified asset allocation strategy that will provide the highest likelihood of meeting the aggregate actuarial projections. In selecting the options and asset allocation strategy, the Corporation has determined that the benefits of reduced portfolio risk are best received through asset style diversification. The following asset classes or investment categories are utilized to meet the Plan's objectives: Small company stock, International stock, Mid-cap stock, Large company stock, Diversified bond, Money Market/Stable Value and Cash.

The Corporation expects to contribute approximately $425,000 to its pension plan in 2010.

Estimated future benefit payments, which reflect expected future service, as appropriate, are as follows:

(Dollar amounts in thousands) For year ended December 31,	Pension Benefits
2010	$ 203
2011	184
2012	209
2013	223
2014	213
2015-2019	1,471
Thereafter	2,628
Benefit Obligation	$ 5,131

Certain accounting guidance requires an employer to recognize the funded status of its defined benefit pension plan as a net asset or liability in its consolidated balance sheet with an offsetting amount in accumulated other comprehensive income, and to recognize changes in that funded status in the year in which changes occur through comprehensive income. As of December 31, 2009, the Corporation's liability under this guidance was $1.1 million and the charge to accumulated other comprehensive income was $729,000, net of taxes. Additionally, the guidance requires an employer to measure the funded status of its defined benefit pension plan as of the date of its year-end financial statements. The Corporation measures the funded status at December 31.

Defined Contribution Plan

The Corporation maintains a defined contribution 401(k) Plan. Employees are eligible to participate by providing tax-deferred contributions up to 20% of qualified compensation. Employee contributions are vested at all times. The Corporation provides a matching contribution of up to 4% of the participant's salary. Matching contributions for 2009 and 2008 were $153,000 and $150,000, respectively.

Notes to Consolidated Financial Statements (continued)

15. Employee Benefit Plans (continued)

Supplemental Executive Retirement Plan

During 2003, the Corporation established a Supplemental Executive Retirement Plan (SERP) to provide certain additional retirement benefits to participating executive officers. The SERP was adopted in order to provide benefits to such executives whose benefits are reduced under the Corporation's tax-qualified benefit plans pursuant to limitations under the Internal Revenue Code. The SERP is subject to certain vesting provisions and provides that the executives shall receive a supplemental retirement benefit if the executive's employment is terminated after reaching the normal retirement age of 65. As of December 31, 2009 and 2008, the Corporation's SERP liability was $417,000 and $285,000, respectively. For the years ended December 31, 2009 and 2008, the Corporation recognized SERP expense of $132,000 and $69,000, respectively.

16. Stock Compensation Plans

The Corporation's 2007 Stock Incentive Plan and Trust (the Plan), which is shareholder-approved, permits the grant of restricted stock awards and options to its directors, officers and employees for up to 177,496 shares of common stock. Incentive stock options, non-incentive or compensatory stock options and share awards may be granted under the Plan. The exercise price of each option shall at least equal the market price of a share of common stock on the date of grant and have a contractual term of ten years. Options shall vest and become exercisable at the rate, to the extent and subject to such limitations as may be specified by the Corporation. Compensation cost related to share-based payment transactions must be recognized in the financial statements with measurement based upon the fair value of the equity or liability instruments issued. During 2009 and 2008, 6,750 and 14,500 options were granted under the plan, respectively. In addition, during 2009 and 2008, the Corporation granted restricted stock awards of 6,750 and 4,500 shares, respectively, with a face value of $91,000 and $101,000, respectively, based on the grant date stock prices of $13.50 and $22.50, respectively. These options and restricted stock awards are 100% vested on the third anniversary of the date of grant. For the year ended December 31, 2009 and 2008, the Corporation recognized $121,000 and $113,000, respectively, in stock compensation expense.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

Weighted-average for the year ended December 31,	2009	2008
Dividend yield	4.15%	5.28%
Expected life	10 years	10 years
Expected volatility	17.87%	12.40%
Risk-free interest rate	3.47%	4.05%

The expected volatility is based on historical stock price fluctuations. The risk-free interest rates for periods within the contractual life of the awards are based on the U.S. Treasury yield curve in effect at the time of the grant. The expected life is based on the maximum term of the options. The dividend yield assumption is based on the Corporation's history and expectation of dividend payouts.

Notes to Consolidated Financial Statements (continued)

16. Stock Compensation Plans (continued)

A summary of option activity under the Plan as of December 31, 2009, and changes during the period then ended is presented below:

	Options	Weighted-Average Exercise Price	Aggregate Intrinsic Value	Weighted-Average Remaining Term (in years)
Outstanding as of January 1, 2009	94,000	$ 25.66		8.7
Granted	6,750	13.50		10.0
Forfeited	(4,500)	26.00		-
Outstanding as of December 31, 2009	96,250	$ 24.79	$ -	7.8
Exercisable as of December 31, 2009	-	$ -	$ -	-

A summary of the status of the Corporation's nonvested option shares as of December 31, 2009, and changes during the period then ended is presented below:

	Options	Weighted-Average Grant-date Fair Value
Nonvested at January 1, 2009	94,000	$ 3.13
Granted	6,750	1.75
Forfeited	(4,500)	3.39
Nonvested as of December 31, 2009	96,250	$ 3.02

As of December 31, 2009, there was $218,000 of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the Plan. That cost is expected to be recognized over the next three years.

17. Fair Values of Financial Instruments

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 sale transaction on the dated indicated. The estimated fair value amounts have been measured as of their respective year-ends and have not been re-evaluated or updated for purposes of these 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 year-end.

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair value.

Notes to Consolidated Financial Statements (continued)

17. Fair Values of Financial Instruments (continued)

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.

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).

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

The Corporation used the following methods and significant assumptions to estimate the fair value of each type of financial instrument:

Available for sales securities – Fair value on available for sale securities were determined by a third party pricing service using quoted prices for identical instruments or similar instruments. In some instances, the fair value of certain securities cannot be determined using these techniques due to the lack of relevant market data. As such, these securities are valued using an alternative technique utilizing other observable inputs and are classified within Level 2 of the fair value hierarchy.

Impaired loans – Fair value on impaired loans is measured using the estimate fair market value of the collateral less the estimate costs to sell. Fair value of the loan's collateral is typically determined by appraisals or independent valuation. Management's ongoing review of appraisal information may result in additional discounts or adjustments to valuation based upon more recent market sales activity or more current appraisal information derived from properties of similar type and/or locale. As of December 31, 2009 the fair value consists of loan balances of $590,000, net of a valuation allowance of $128,000. Additional provision for loan losses of $128,000 was recorded during the year ended December 31, 2009.

Notes to Consolidated Financial Statements (continued)

17. Fair Values of Financial Instruments (continued)

For assets measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy are as follows:

(Dollar amounts in thousands) Description	Total	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
December 31, 2009:				
U.S. Treasury and federal agency	$ 3,001	$ -	$ 3,001	$ -
U.S. government sponsored entities and agencies	50,797	-	50,797	-
Mortgage-backed securities: residential	16,530	-	16,530	-
Collateralized mortgage obligations	5,130	-	5,130	-
State and political subdivision	26,967	-	26,967	-
Equity securities	2,818	2,093	725	-
	$ 105,243	$ 2,093	$ 103,150	$ -
December 31, 2008:				
U.S. government sponsored entities and agencies	$ 20,077	$ -	$ 20,077	$ -
Mortgage-backed securities: residential	17,218	-	17,218	-
Collateralized mortgage obligations	13,162	-	13,162	-
State and political subdivision	13,808	-	13,808	-
Corporate securities	3,984	-	3,984	-
Equity securities	3,194	3,194	-	-
	$ 71,443	$ 3,194	$ 68,249	$ -

For assets measured at fair value on a non-recurring basis, the fair value measurements by level within the fair value hierarchy are as follows:

(Dollar amounts in thousands) Description	Total	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
December 31, 2009:				
Impaired loans	$ 462	$ -	$ -	$ 462
	$ 462	$ -	$ -	$ 462
December 31, 2008:				
Impaired loans	$ -	$ -	$ -	$ -
	$ -	$ -	$ -	$ -

Notes to Consolidated Financial Statements (continued)

17. Fair Values of Financial Instruments (continued)

The following table sets forth the carrying amount and fair value of the Corporation's financial instruments included in the consolidated balance sheet as of December 31:

(Dollar amounts in thousands)	2009		2008	
	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets:				
Cash and cash equivalents	$ 38,952	$ 38,952	$ 16,571	$ 16,571
Securities	105,243	105,243	71,443	71,443
Loans receivable	292,615	298,197	264,838	272,662
Federal bank stocks	4,125	4,125	3,797	3,797
Accrued interest receivable	1,574	1,574	1,519	1,519
Financial liabilities:				
Deposits	385,325	389,443	286,647	290,533
Borrowed funds	40,000	43,258	48,188	52,510
Accrued interest payable	711	711	761	761
Off-balance sheet commitments	-	-	-	-

This 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 fair values of the Corporation's financial instruments at December 31, 2009 and 2008:

Carrying amount is the estimated fair value for cash and cash equivalents, securities, federal bank stocks, accrued interest receivable and payable, demand deposits, borrowed funds, and variable rate loans or deposits that reprice frequently and fully. For fixed rate loans or deposits and for variable rate loans or deposits with infrequent repricing or repricing limits, fair value is based on discounted cash flows using current market rates applied to the estimated life and credit risk. Fair value of debt is based on current rates for similar financing.

Estimates of the fair value of off-balance sheet items were not made because of the short-term nature of these arrangements and the credit standing of the counterparties. Also, unfunded loan commitments relate principally to variable rate commercial loans.

Notes to Consolidated Financial Statements (continued)

17. Fair Values of Financial Instruments (continued)

Off-Balance Sheet Financial Instruments

The Corporation is party to credit related 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 commercial letters of credit. Commitments to extend credit involve, to a varying degree, elements of credit and interest rate risk in excess of amounts recognized in the consolidated balance sheets. The Corporation's exposure to credit loss in the event of non-performance by the other party for commitments to extend credit is represented by the contractual amount of these commitments, less any collateral value obtained. The Corporation uses the same credit policies in making commitments as for on-balance sheet instruments. The Corporation's distribution of commitments to extend credit approximates the distribution of loans receivable outstanding.

The following table presents the notional amount of the Corporation's off-balance sheet commitment financial instruments as of December 31:

(Dollar amounts in thousands)	2009		2008	
	Fixed Rate	Variable Rate	Fixed Rate	Variable Rate
Commitments to make loans	$ 2,436	$ 2,592	$ 596	$ 1,664
Unused lines of credit	5,386	35,697	1,367	18,636
	$ 7,822	$ 38,289	$ 1,963	$ 20,300

Commitments to make loans are generally made for periods of 30 days or less. The fixed rate loan commitments have interest rates ranging from 4.00% to 11.25% and maturities ranging from 5 to 30 years at both year end dates. Commitments to extend credit include agreements to lend to a customer as long as there is no violation of any condition established in the contract. These commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Commitments to extend credit also include unfunded commitments under commercial and consumer lines of credit, revolving credit lines and overdraft protection agreements. These lines of credit may be collateralized and usually do not contain a specified maturity date and may be drawn upon to the total extent to which the Corporation is committed.

Standby letters of credit are conditional commitments issued by the Corporation usually for commercial customers to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Corporation generally holds collateral supporting those commitments if deemed necessary. Standby letters of credit were $1.5 million and $1.1 million at December 31, 2009 and 2008, respectively. The current amount of the liability as of December 31, 2009 and 2008 for guarantees under standby letters of credit issued is not material.

Notes to Consolidated Financial Statements (continued)

18. Emclaire Financial Corp. – Condensed Financial Statements, Parent Corporation Only

Following are condensed financial statements for the parent company as of and for the years ended December 31:

Condensed Balance Sheets (Dollar amounts in thousands)	2009	2008
Assets:		
Cash and cash equivalents	$ 58	$ 68
Securities available for sale	2,758	3,138
Equity in net assets of subsidiary bank	39,994	34,222
Other assets	426	7
Total Assets	$ 43,236	$ 37,435
Liabilities and Stockholders' Equity:		
Short-term borrowed funds with affiliated subsidiary	$ 1,100	$ 1,100
Other short-term borrowed funds	5,000	-
Accrued expenses and other liabilities	102	212
Stockholders' equity	37,034	36,123
Total Liabilities and Stockholders' Equity	$ 43,236	$ 37,435

Condensed Statements of Income (Dollar amounts in thousands)	2009	2008
Income:		
Dividends from subsidiary bank	$ 2,195	$ 2,555
Investment income	105	149
Total income	2,300	2,704
Expense:		
Interest expense	118	68
Noninterest expense	1,675	331
Total expense	1,793	399
Net income before income taxes and equity in undistributed operating results of subsidiary	507	2,305
Equity in undistributed net income of subsidiary	456	1,113
Net income before income taxes and extraordinary item	963	3,418
Provision for income taxes	(576)	(59)

Net income before extraordinary item		1,539		3,477
Extraordinary item, loss on business combination		-		(1,047)
Net income	$	1,539	$	2,430

Notes to Consolidated Financial Statements (continued)

18. Emclaire Financial Corp. – Condensed Financial Statements, Parent Corporation Only (continued)

Condensed Statements of Cash Flows (Dollar amounts in thousands)	2009	2008
Operating activities:		
Net income	$ 1,539	$ 2,430
Adjustments to reconcile net income to net cash provided by operating activities:		
Equity in undistributed operating results of subsidiary	(456)	(1,113)
Securities impairment loss recognized in earnings	898	-
Other, net	(589)	501
Net cash provided by operating activities	1,392	1,818
Investing activities:		
Purchases of securities	(8)	(129)
Investment in subsidiaries	(5,000)	(11,253)
Net cash used in investing activities	(5,008)	(11,382)
Financing activities:		
Net change in borrowings	5,000	-
Proceeds from sale of preferred stock	-	7,412
Issuance of warrants	-	88
Proceeds from sale of common stock	-	3,753
Dividends paid	(1,394)	(1,704)
Net cash provided by financing activities	3,606	9,549
Decrease in cash and cash equivalents	(10)	(15)
Cash and cash equivalents at beginning of period	68	83
Cash and cash equivalents at end of period	$ 58	$ 68

19. Other Comprehensive Income (Loss)

Other comprehensive income (loss) components and related taxes for the years ended December 31 were as follows:

(Dollar amounts in thousands)	2009	2008
Unrealized holding gains (losses) on available for sale securities	$ 185	$ (11)
Reclassification adjustment for losses recognized in income, net	34	391
Amortization of pension prior service cost	(31)	(30)
Amortization of pension net actuarial gain (loss)	790	(1,368)
Net unrealized gains (losses)	978	(1,018)
Tax expense (benefit)	(333)	346
Other comprehensive income (loss)	$ 645	$ (672)

Notes to Consolidated Financial Statements (continued)

20. Other Noninterest Income and Expense

Other noninterest income includes customer bank card processing fee income of $403,000 and $292,000 for 2009 and 2008, respectively.

The following summarizes the Corporation's other noninterest expenses for the years ended December 31:

(Dollar amounts in thousands)	2009	2008
Printing and supplies	$ 352	$ 213
Customer bank card processing	274	256
Telephone and data communications	196	143
Travel, entertainment and conferences	192	176
Internet banking and bill pay	186	125
Postage and freight	180	185
Pennsylvania shares and use taxes	176	147
Contributions	171	140
Correspondent bank and courier fees	156	165
Subscriptions	145	121
Marketing and advertising	130	150
Examinations	104	93
Contract termination fee	-	360
Other	246	114
Total other noninterest expenses	$ 2,508	$ 2,388

Notes to Consolidated Financial Statements (continued)

21. Quarterly Financial Data (unaudited)

The following is a summary of selected quarterly data for the years ended December 31:

(Dollar amounts in thousands, except share data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2009:				
Interest income	$ 5,011	$ 4,789	$ 5,112	$ 5,422
Interest expense	1,950	1,810	1,860	1,962
Net interest income	3,061	2,979	3,252	3,460
Provision for loan losses	297	540	240	290
Net interest income after provision for loan losses	2,764	2,439	3,012	3,170
Noninterest income	720	919	12	1,179
Noninterest expense	2,622	2,896	3,255	3,845
Income (loss) before income taxes	862	462	(231)	504
Provision for (benefit from) income taxes	194	54	(221)	31
Net income (loss)	668	408	(10)	473
Accumulated preferred stock dividends and discount accretion	98	98	98	99
Net income available to common stockholders	$ 570	$ 310	$ (108)	$ 374
Basic earnings per common share	$ 0.40	$ 0.22	$ (0.08)	$ 0.26
2008:				
Interest income	$ 4,520	$ 4,563	$ 4,847	$ 5,163
Interest expense	1,977	1,999	2,117	2,075
Net interest income	2,543	2,564	2,730	3,088
Provision for loan losses	60	85	140	215
Net interest income after provision for loan losses	2,483	2,479	2,590	2,873
Noninterest income	660	496	620	711
Noninterest expense	2,413	2,293	2,296	4,030
Income (loss) before income taxes and extraordinary item	730	682	914	(446)
Provision for (benefit from) income taxes	171	141	198	(154)
Income (loss) before extraordinary item	559	541	716	(292)
Extraordinary item, gain on business combination	-	-	-	906
Net income	$ 559	$ 541	$ 716	$ 614
Basic earnings per common share	$ 0.44	$ 0.43	$ 0.56	$ 0.43

Increased noninterest expense during the third and fourth quarters of 2009 was primarily related to costs associated with the Titusville branch purchase as discussed in Note 2 and the Corporation's proposed stock offering that was withdrawn.

The increase in noninterest expense between the third and fourth quarters of 2008 was primarily related to severance charges totaling $590,000 recorded in the fourth quarter of 2008, principally associated with the retirement of the Corporation's former Chairman of the Board, President and Chief Executive Officer and contract termination fees of $360,000 recognized in the fourth quarter of 2008 in connection with an ATM processing conversion completed during 2009.