FIRST NATIONAL COMMUNITY BANCORP INC
Form 10-Q
May 08, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2015

OR

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

For the transition period from to

Commission File No. 000-53869

FIRST NATIONAL COMMUNITY BANCORP, INC.

(Exact Name of Registrant as Specified in Its Charter)

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

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

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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 Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES x NO ¨

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

Large Accelerated Filer o	Accelerated Filer x
Non-Accelerated Filer o	Smaller reporting company o

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

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

Common Stock, $1.25 par value	**16,500,945 shares**
(Title of Class)	(Outstanding at May 8, 2015)

Contents

PART I. Financial Information

Item 1. Financial Statements

FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(unaudited)

(in thousands, except share data)	March 31, 2015	December 31, 2014
Assets		
Cash and cash equivalents:		
Cash and due from banks	$ 19,985	$ 22,657
Interest-bearing deposits in other banks	17,390	13,010
Total cash and cash equivalents	37,375	35,667
Securities available for sale, at fair value	204,635	218,989
Stock in Federal Home Loan Bank of Pittsburgh, at cost	3,061	2,803
Loans held for sale	-	603
Loans, net of allowance for loan and lease losses of $10,944 and $11,520	661,221	658,747
Bank premises and equipment, net	11,221	11,003
Accrued interest receivable	2,118	2,075
Intangible assets	261	302
Bank-owned life insurance	28,952	28,817
Other real estate owned	2,369	2,255
Other assets	9,028	8,768
Total assets	$ 960,241	$ 970,029
Liabilities		
Deposits:		
Demand (non-interest-bearing)	$ 134,993	$ 124,064
Interest-bearing	640,118	671,272
Total deposits	775,111	795,336
Borrowed funds:		
Federal Home Loan Bank of Pittsburgh advances	67,612	61,194
Subordinated debentures	25,000	25,000
Junior subordinated debentures	10,310	10,310
Total borrowed funds	102,922	96,504
Accrued interest payable	10,788	10,262
Other liabilities	15,678	16,529
Total liabilities	904,499	918,631
Shareholders' equity		

Preferred shares ($1.25 par)		
Authorized: 20,000,000 shares at March 31, 2015 and December 31, 2014		
Issued and outstanding: 0 shares at March 31, 2015 and December 31, 2014	-	-
Common shares ($1.25 par)		
Authorized: 50,000,000 shares at March 31, 2015 and December 31, 2014		
Issued and outstanding: 16,500,945 shares, March 31, 2015 and 16,484,419 shares, December 31, 2014	20,626	20,605
Additional paid-in capital	61,801	61,781
Accumulated deficit	(28,651)	(32,126)
Accumulated other comprehensive income	1,966	1,138
Total shareholders' equity	55,742	51,398
Total Liabilities and shareholders’ equity	$ 960,241	$ 970,029

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

FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(unaudited)

	Three months ended March 31,	
(in thousands, except share data)	2015	2014
Interest income		
Interest and fees on loans	$6,472	$6,494
Interest and dividends on securities		
U.S. government agencies	971	743
State and political subdivisions, tax-free	50	710
State and political subdivisions, taxable	26	98
Other securities	157	56
Total interest and dividends on securities	1,204	1,607
Interest on interest-bearing deposits in other banks	21	23
Total interest income	7,697	8,124
Interest expense		
Interest on deposits	683	865
Interest on borrowed funds		
Interest on Federal Home Loan Bank of Pittsburgh advances	120	96
Interest on subordinated debentures	563	563
Interest on junior subordinated debentures	49	49
Total interest on borrowed funds	732	708
Total interest expense	1,415	1,573
Net interest income before credit for loan and lease losses	6,282	6,551
Credit for loan and lease losses	(494)	(1,570)
Net interest income after credit for loan and lease losses	6,776	8,121
Non-interest income		
Deposit service charges	674	690
Net gain on the sale of securities	2,224	1,568
Net gain on the sale of mortgage loans held for sale	40	75
Net loss on the sale of education loans	-	(13)
Net gain on the sale of other real estate owned	5	29
Gain on branch divestitures	-	607
Loan-related fees	90	93
Income from bank-owned life insurance	135	167
Other	251	237
Total non-interest income	3,419	3,453
Non-interest expense		
Salaries and employee benefits	3,139	3,400
Occupancy expense	633	644
Equipment expense	384	356
Data processing expense	448	522

Regulatory assessments	409	673
Bank shares tax	217	176
Expense of other real estate owned	100	163
Legal expense	163	647
Professional fees	301	450
Insurance expense	198	282
Other operating expenses	790	678
Total non-interest expense	6,782	7,991
Income before income taxes	3,413	3,583
Provision for income taxes	(62)	70
Net income	$3,475	$3,513
Earnings per share:		
Basic	$0.21	$0.21
Diluted	$0.21	$0.21
Cash dividends declared per common share	$-	$-
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING:		
Basic	16,490,111	16,471,569
Diluted	16,490,111	16,472,435

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

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(unaudited)

	Three months ended March 31,	
(in thousands)	2015	2014
Net income	$ 3,475	$ 3,513
Other comprehensive income:		
Unrealized gains on securities available for sale	3,478	6,404
Taxes	(1,182)	(2,177)
Net of tax amount	2,296	4,227
Reclassification adjustment for gains included in net income	(2,224)	(1,200)
Taxes	756	408
Net of tax amount	(1,468)	(792)
Total other comprehensive income	828	3,435
Comprehensive income	$ 4,303	$ 6,948

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

FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

For the Three Months Ended March 31, 2015 and 2014

(unaudited)

(in thousands, except per share data)	Number of Common Shares	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive (Loss) Income	Total Shareholders' Equity
BALANCES, DECEMBER 31, 2013	16,471,569	$ 20,589	$ 61,627	$ (45,546)	$ (3,092)	$ 33,578
Net income for the period	-	-	-	3,513	-	3,513
Restricted stock awards	-	-	10	-	-	10
Other comprehensive income, net of tax of $1,769	-	-	-	-	3,435	3,435
Balances, March 31, 2014	16,471,569	$ 20,589	$ 61,637	$ (42,033)	$ 343	$ 40,536
BALANCES, DECEMBER 31, 2014	16,484,419	$ 20,605	$ 61,781	$ (32,126)	$ 1,138	$ 51,398
Net income for the period	-	-	-	3,475	-	3,475
Common shares issued under long-term incentive compensation plan	16,526	21	(21)	-	-	-
Restricted stock awards	-	-	41	-	-	41
Other comprehensive income, net of tax of $426	-			-	828	828
Balances, March 31, 2015	16,500,945	$ 20,626	$ 61,801	$ (28,651)	$ 1,966	$ 55,742

FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

(in thousands)	Three Months Ended March 31, 2015	2014
Operating activities:		
Net income	$3,475	$3,513
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Investment securities amortization (accretion), net	463	295
Equity in trust	(1)	(1)
Depreciation and amortization	360	382
Stock-based compensation	41	10
Credit for loan and lease losses	(494)	(1,570)
Valuation adjustment for off-balance sheet commitments	(21)	(113)
Gain on the sale of available-for-sale securities	(2,224)	(1,200)
Gain on the sale of held-to-maturity securities	-	(368)
Gain on the sale of loans held for sale	(40)	(75)
Loss on the sale of education loans	-	13
Gain on branch divestiture	-	(607)
Gain on the sale of other real estate owned	(5)	(29)
Valuation adjustment of other real estate owned	12	53
Income from bank-owned life insurance	(135)	(167)
Proceeds from the sale of loans held for sale	1,085	2,524
Funds used to originate loans held for sale	(442)	(1,698)
Increase in interest receivable	(43)	(399)
Increase in prepaid expenses and other assets	(324)	(453)
Increase in interest payable	526	568
(Decrease) increase in accrued expenses and other liabilities	(2,278)	4,822
Total adjustments	(3,520)	1,987
Net cash (used in) provided by operating activities	(45)	5,500
Cash flows from investing activities:		
Maturities, calls and principal payments of available-for-sale securities	2,236	1,502
Proceeds from the sale of available-for-sale securities	35,948	11,062
Proceeds from the sale of held-to-maturity securities	-	2,686
Purchases of available-for-sale securities	(19,802)	(37,129)
Net purchase of Federal Home Loan Bank of Pittsburgh stock	(258)	(396)
Proceeds from the sale of education loans	-	2,537
Net increase in loans to customers	(2,083)	(12,606)
Proceeds from the sale of other real estate owned	37	798
Proceeds from the sale of bank premises and equipment through branch divestitures	-	2,504
Purchases of property and equipment	(518)	(380)

Net cash provided by (used in) investing activities	15,560	(29,422)
Cash flows from financing activities:		
Net decrease in deposits	(20,225)	(49,065)
Proceeds from Federal Home Loan Bank of Pittsburgh advances	6,512	17,500
Repayment of Federal Home Loan Bank of Pittsburgh advances	(94)	(10,089)
Net cash used in financing activities	(13,807)	(41,654)
Net increase (decrease) in cash and cash equivalents	1,708	(65,576)
Cash and cash equivalents at beginning of period	35,667	103,556
Cash and cash equivalents at end of period	$37,375	$37,980
Supplemental cash flow information		
Cash paid during the period for:		
Interest	$889	$1,005
Income taxes	-	25
Other transactions:		
Available-for-sale securities purchased, not settled	(1,013)	-
Principal balance of loans transferred to OREO	149	-
Change in deferred gain on sale of other real estate owned	(9)	2

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

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FIRST NATIONAL COMMUNITY BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Basis of Presentation

The consolidated financial statements are comprised of the accounts of First National Community Bancorp, Inc., and its wholly owned subsidiary, First National Community Bank (the “Bank”), as well as the Bank’s wholly owned subsidiaries (collectively, the “Company”). The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America (“GAAP”) and general practices within the banking industry. In the opinion of management, all adjustments necessary for a fair presentation of the results for the quarterly period ended March 31, 2015 have been included in the consolidated financial statements. All intercompany balances and transactions have been eliminated in consolidation. Prior period amounts have been reclassified when necessary to conform to the current period’s presentation. These reclassifications did not have an impact on the operating results or financial position of the Company. The operating results and financial position of the Company for the three months ended March 31, 2015, may not be indicative of future results of operations and financial position.

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to change in the near term are the allowance for loan and lease losses (“ALLL”), investment security valuations, the evaluation of investment securities and other real estate owned (“OREO”) for impairment, and the evaluation of deferred income taxes.

These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s audited financial statements, included in its Annual Report filed on Form 10-K as of and for the year ended December 31, 2014.

Note 2. New Authoritative Accounting Guidance

ASU 2014-04, Receivables-Troubled Debt Restructurings by Creditors (Subtopic 310-40): “Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure,” clarifies that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (a) the creditor obtaining legal title to residential real estate property upon completion of a foreclosure or (b) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additionally, the amendments require interim and annual disclosure of both the amount of foreclosed residential real estate property held by the creditor and the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to local requirements of the applicable jurisdiction. The adoption of this guidance on January 1, 2015 did not have a material effect on the operating results or financial position of the Company.

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

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

ASU 2014-14, Receivables – Troubled Debt Restructurings by Creditors (Subtopic 310-40): “Classification of Certain Government-Guaranteed Mortgage Loans Upon Foreclosure,” requires that a mortgage loan be derecognized and that a separate other receivable be recognized upon foreclosure if the following conditions are met: (1) the loan has a government guarantee that is not separable from the loan before foreclosure; (2) at the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim; and (3) at the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. The adoption of this guidance on January 1, 2015 did not have a material effect on the operating results or financial position of the Company.

Accounting Guidance to be Adopted in Future Periods

ASU 2014-09, Revenue from Contracts with Customers (Topic 606): Section A, “Summary and Amendments That Create Revenue from Contracts with Customers (Topic 606) and Other Assets and Deferred Costs-Contract with Customers (Subtopic 340-40);” Section B, “Conforming Amendments to Other Topics and Subtopics in the Codification and Status Tables;” and Section C, “Background Information and Basis for Conclusions,” provides a robust framework for addressing revenue recognition issues, and upon its effective date, replaces almost all existing revenue recognition guidance, including industry specific guidance, in current GAAP. The core principle of ASU 2014-09 is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. ASU 2014-09 will also result in enhanced interim and annual disclosures, both qualitative and quantitative, about revenue in order to help financial statement users understand the nature, amount, timing and uncertainty of revenue and related cash flows. ASU 2014-09 is effective in annual reporting periods beginning after December 15, 2016 and the interim periods within that year for public business entities, not-for-profit entities that have issued, or are conduit bond obligors for, securities that are traded, listed or quoted on an exchange or over-the-counter market and employee benefit plans that file or furnish financial statements to the SEC. On April 29, 2015, the FASB issued for public comment a proposed ASU that would defer the effective date of ASU 2014-09 for both public and private entities for one year. A final decision is subject to the FASB’s due process requirement. The Company will adopt this guidance in accordance with the final outcome of the FASB’s extension proposal, and is currently evaluating the effect this guidance may have on its operating results or financial position.

ASU 2014-12, Compensation – Stock Compensation (Topic 718): “Accounting for Share-Based Payments When the Terms of an Award Provide that a Performance Target Could be Achieved after the Requisite Service Period,” requires a performance target that affects vesting and that can be achieved after the requisite service period to be treated as a performance condition. To account for such awards, an entity should apply existing guidance as it relates to awards with performance conditions that affect vesting. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent compensation cost attributable to the period(s) for which the requisite service already has been rendered. If the performance target becomes probable of being achieved before the end of the requisite service period, the remaining unrecognized compensation cost should be recognized prospectively over the remaining requisite service periods. The total amount of compensation cost should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest. ASU 2014-12 is effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. The adoption of this guidance on January 1, 2016 is not expected to have a material effect on the operating results or financial position of the Company.

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

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

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

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

ASU 2015-05, Intangibles – Goodwill and Other Internal-Use Software (Subtopic 350-40): "Customer's Accounting for Fees Paid in a Cloud Computing Arrangement," provides explicit guidance on a customer's accounting for fees paid in a cloud computing environment. Specifically, the amendments in this ASU provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. ASU 2015-05 is effective for public entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption of this guidance is permitted. The adoption of this guidance on January 1, 2016 is not expected to have a material effect on the operating results or financial position of the Company.

Note 3. Regulatory Matters

The Bank was under a Consent Order (the "Order") from the Office of the Comptroller of the Currency ("OCC") dated September 1, 2010. On March 25, 2015, after meeting all of the requirements of the Order, the Bank was fully and completely released from the Order. The Company has been, and continues to be, subject to a Written Agreement (the "Agreement") with the Federal Reserve Bank of Philadelphia (the "Reserve Bank") dated November 24, 2010.

Federal Reserve Agreement. The Agreement requires the Company to undertake certain actions within designated timeframes, and to operate in compliance with the provisions thereof during its term. The material provisions of the Agreement are set forth below with a description of the status of the Company's efforts to comply with such provisions:

(i) the Company's Board was required to take appropriate steps to fully utilize the Company's financial and managerial resources to serve as a source of strength to the Bank, including taking steps to ensure that the Bank complied with its Consent Order entered into with the OCC;

The Company has taken, and continues to take, steps the Board of Directors believes are appropriate to use the Company's financial and managerial resources to serve as a source of strength to the Bank.

(ii) the Company may not declare or pay any dividends without the prior written approval of the Reserve Bank and the Director of the Division of Banking Supervision and Regulation (the "Director") of the Federal Reserve Board;

The Company has acknowledged the prohibition on payment of dividends without the prior written consent of the Reserve Bank and Director. The Company has not paid any dividends since the effective date of the Agreement.

(iii) the Company may not take dividends or other payments representing a reduction of the Bank's capital without the prior written approval of the Reserve Bank;

The Company has acknowledged the prohibition on taking dividends or any other capital distributions from the Bank without the prior written consent of the Reserve Bank. On September 8, 2014, the Company sent a request to the Reserve Bank to approve a dividend from the Bank in the amount of $1.0 million. The dividend was to be used to cure the interest deferral on the junior subordinated debentures. The Company received written non-objection to allow the $1.0 million dividend payment from the Bank and cure of the interest deferral on the junior subordinated debentures in the amount of $921 thousand. The $1.0 million dividend payment from the Bank to the Company and the interest deferral payment on the junior subordinated debentures were completed in December 2014. The Company made a subsequent request for and has received approval from the Reserve Bank to permit payment of the quarterly interest payment on the junior subordinated debentures, which was due and paid by the Company on March 15, 2015. In April 2015, the Company made an additional request to the Reserve Bank to approve a dividend from the Bank to the Company related to interest payments on the junior subordinated debentures and principal payments on the subordinated debentures.

(iv) the Company and its nonbank subsidiary may not make any payment of interest, principal or other amounts on the Company's subordinated debentures or junior subordinated debentures without the prior written approval of the Reserve Bank and the Director;

The Company has acknowledged the prohibition on any payment related to the Company's subordinated debentures and junior subordinated debentures without the written approval of the Reserve Bank and Director. Previously, the Company has not made any payments of interest, principal or other amounts on either of the Company's debentures or junior subordinated debentures since the effective date of the Agreement.

On September 8, 2014, the Company sent to the Reserve Bank requests for approval for the Company to receive a $1.0 million capital distribution from the Bank, and to make a distribution on the junior subordinated debentures to cure the interest deferral. The Company received approval from the Reserve Bank in November 2014 to cure and pay the interest deferral. On December 15, 2014, the Company paid all deferred and currently payable accrued interest totaling $921 thousand. On February 2, 2015, the Company received approval from the Reserve Bank to pay the regular quarterly interest payment, which was due and paid on March 15, 2015. In April 2015, the Company made an additional request to the Reserve Bank to approve a dividend from the Bank to the Company related to interest payments on the junior subordinated debentures and principal payments on the subordinated debentures.

(v) the Company may not make any payment of interest, principal or other amounts on debt owed to insiders of the Company without the prior written approval of the Reserve Bank and Director;

The Company has acknowledged the prohibition on any payment related to the debt owed to insiders of the Company without the written approval of the Reserve Bank and Director. The Company has not made any payments related to debt owed to insiders since the effective date of the Agreement. In April 2015, the Company made a request to the Reserve Bank to receive a dividend from the Bank and make pro-rata principal payments on the subordinated debentures including those debentures held by insiders of the Company.

(vi) the Company and its nonbank subsidiary may not incur, increase or guarantee any debt without the prior written approval of the Reserve Bank;

The Company has acknowledged the prohibition on incurring, increasing or guaranteeing any debt without the written approval of the Reserve Bank other than permitted borrowings by the Bank from the Federal Home Loan Bank (“FHLB”). The Company has not incurred, increased or guaranteed any debt since the effective date of the Agreement.

(vii) the Company may not purchase or redeem any shares of its stock without the prior written approval of the Reserve Bank;

The Company has acknowledged the prohibition on purchasing or redeeming any shares of its stock without the written approval of the Reserve Bank. The Company has not purchased or redeemed any shares of its stock since the effective date of the Agreement.

(viii) the Company was required to submit to the Reserve Bank, by January 23, 2011, an acceptable written plan to maintain sufficient capital at the Company on a consolidated basis. Thereafter, the Company must notify the Reserve Bank within 45 days of the end of any quarter in which the Company’s capital ratios fall below the approved capital plan’s minimum ratios, and submit an acceptable written plan to increase the Company’s capital ratios above the capital plan’s minimums;

The Company has developed a Capital Plan that it believes is acceptable and maintains sufficient capital at the Company on a consolidated basis. The Company notified the Reserve Bank that the OCC issued a written determination of supervisory non-objection to the 2014-2016 Capital Plan in June 2014, and that the Bank's Board of Directors adopted the plan in June 2014. The annual update and revision to the Capital Plan for the three-year period January 1, 2015 to December 31, 2017 was completed in conjunction with the annual budget and strategic planning initiatives and provided to the Reserve Bank in January 2015.

(ix) the Company was required to immediately take all actions necessary to ensure that: (1) each regulatory report accurately reflects the Company's condition on the date for which it is filed and all material transactions between the Company and its subsidiaries; (2) each such report is prepared in accordance with its instructions; and (3) all records indicating how the report was prepared are maintained for supervisory review;

The Company believes that it has taken actions to ensure that all required regulatory reports are filed to accurately reflect its financial condition on the date filed, are prepared in accordance with instructions and that records detailing how the reports were filed are maintained and available for supervisory review.

(x) the Company was required to submit to the Reserve Bank, by January 23, 2011, acceptable written procedures to strengthen and maintain internal controls to ensure all required regulatory reports and notices filed with the Board of Governors are accurate and filed in accordance with the instructions for preparation;

The Company believes that it has designed effective written procedures and strengthened internal controls so that all required Board of Governors reports and notices filed are accurate, timely and in accordance with instructions. The written procedures were provided to the Reserve Bank on January 21, 2011.

(xi) the Company was required to submit to the Reserve Bank, by January 8, 2011, a cash flow projection for 2011, reflecting the Company's planned sources and uses of cash, and submit a cash flow projection for each subsequent calendar year at least one month prior to the beginning of such year;

The Company created a cash flow projection for 2011 and submitted it to the Reserve Bank on January 7, 2011 in accordance with requirements of the Agreement. Similar projections for 2012, 2013, 2014 and 2015 were provided to the Reserve Bank within the time requirements prescribed in the Agreement.

(xii) the Company must comply with: (1) the notice provisions of Section 32 of the FDI Act and Subpart H of Regulation Y in appointing any new director or senior executive officer or changing the duties of any senior executive officer; and (2) the restrictions on indemnification and severance payments of Section 18(k) of the FDI Act and Part 359 of the FDIC's regulations;

The Company has acknowledged the notice requirements on the appointment of any new director or senior executive officer. The Company has filed the appropriate notice for each new director or senior executive officer since the date of the Agreement.

The Company acknowledges the restriction on indemnification and severance payments under Section 18(k) of the FDI Act and Part 359 of the FDIC's regulations. The Company has not made any such indemnification or severance payments since the effective date of the Agreement without obtaining prior regulatory non-objection and regulatory concurrence from the FDIC as required by Part 359.

(xiii) the Board must submit written progress reports within 30 days of the end of each calendar quarter.

The Company's Board of Directors has filed each of the required written progress reports with the Reserve Bank since the Agreement was executed.

Banking regulations also limit the amount of dividends that may be paid without prior approval of the Bank's regulatory agency. At March 31, 2015, the Company and the Bank are restricted from paying any dividends, without regulatory approval based on provisions contained in the Written Agreement.

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

In July 2013, the Federal Reserve, the OCC and the FDIC approved the final Basel III capital framework for U.S. banking organizations (the “Regulatory Capital Rules”) implementing regulatory capital reforms and changes required by the Dodd-Frank Act.

The Regulatory Capital Rules are effective on January 1, 2014; however, the mandatory compliance date for the Company and the Bank as “standardized approach” banking organizations began on January 1, 2015 and is subject to transitional provisions extending to January 1, 2019. The Regulatory Capital Rules include new risk-based capital and leverage ratios and refine the definition of what constitutes “capital” for purposes of calculating those ratios. The new minimum capital level requirements applicable to the Company and the Bank under the Regulatory Capital Rules will be:

· a new common equity Tier I capital ratio of 4.50%;
· a Tier I capital ratio of 6.00% (increased from 4.00%);
· a total capital ratio of 8.00% (unchanged from current rules); and
· a Tier I leverage ratio of 4.00% for all institutions.

The Regulatory Capital Rules also establish a “capital conservation buffer” above the new regulatory minimum capital requirements, which must consist entirely of common equity Tier I capital and result in the following minimum ratios effective January 1, 2019:

· a common equity Tier I capital ratio of 7.00%;
· a Tier I capital ratio of 8.50%; and
· a total capital ratio of 10.50%.

The new capital conservation buffer requirement will be phased in beginning in January 2016 at 0.625% of risk-weighted assets and will increase by that amount each year until fully implemented in January 2019 at 2.50%. An institution will be subject to limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses if its capital level falls below the buffer amount. These limitations will establish a maximum percentage of eligible retained income that could be utilized for such actions.

The Regulatory Capital Rules also implement revisions and clarifications consistent with Basel III regarding the various components of Tier I capital, including common equity, unrealized gains and losses, as well as certain instruments that will no longer qualify as Tier I capital, some of which will be phased out over time.

The Regulatory Capital Rules also revise the prompt corrective action framework, which is designed to place restrictions on insured depository institutions, including the Bank, if their capital levels begin to show signs of weakness. These revisions took effect January 1, 2015. Under the prompt corrective action requirements, which are designed to complement the capital conservation buffer, insured depository institutions will be required to meet the following increased capital level requirements in order to qualify as “well capitalized:”

- a new common equity Tier I risk-based capital ratio of 6.50%;
- a Tier I risk-based capital ratio of 8.00% (increased from 6.00%);
- a total risk-based capital ratio of 10.00% (unchanged from current rules); and
- a Tier I leverage ratio of 5.00%.

The Regulatory Capital Rules set forth certain changes for the calculation of risk-weighted assets, which are required to be utilized beginning January 1, 2015. The provisions applicable to banking organizations under the “standardized approach” include changes with respect to risk weights for commercial real estate loans, past due exposures and conversion factors for commitments with an original maturity of one year or less.

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

Current quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined).

The Company's and the Bank's actual capital positions and ratios at March 31, 2015 and December 31, 2014 are presented in the following table:

Capital Analysis

(in thousands)	March 31, 2015	December 31, 2014
Company:		
Tier I common equity	$ 53,646	N/A
Tier I capital	63,646	$ 59,930
Tier II capital:		
Subordinated notes	17,500	25,000
Allowable portion of allowance for loan losses	8,697	8,591
Total tier II capital	26,197	33,591
Total risk-based capital	89,843	93,521
Total risk-weighted assets	$ 693,098	$ 683,956
Total average assets (for Tier I leverage ratio)	$ 968,240	$ 990,346
Bank:		
Tier I common equity	$ 101,137	N/A
Tier I capital	101,137	$ 96,816
Tier II capital:		
Allowable portion of allowance for loan losses	8,692	8,587
Total tier II capital	8,692	8,587
Total risk-based capital	109,829	105,403
Total risk-weighted assets	$ 692,707	$ 683,576
Total average assets (for Tier I leverage ratio)	$ 968,119	$ 990,407

The following tables present summary information regarding the Company’s and the Bank’s risk-based capital and related ratios at March 31, 2015 and December 31, 2014:

(dollars in thousands)	Actual Amount	Ratio	For Capital Adequacy Purposes Amount	Ratio	To Be Well Capitalized Under Prompt Corrective Action Provision Amount	Ratio
March 31, 2015						
Total capital (to risk-weighted assets)						
Company	$89,843	12.96%	$>/=55,448	>/=8.00%	$>/=69,310	>/=10.00%
Bank	$109,829	15.86%	$>/=55,417	>/=8.00%	$.>/=69,271	>/=10.00%
Tier I capital (to risk-weighted assets)						
Company	$63,646	9.18 %	$>/=41,586	>/=6.00%	$>/=55,448	>/=8.00%
Bank	$101,137	14.60%	$>/=41,562	>/=6.00%	$>/=55,417	>/=8.00%
Tier I common equity (to risk-weighted assets)						
Company	$53,646	7.74 %	$>/=31,189	>/=4.50%	$>/=45,051	>/=6.50%
Bank	$101,137	14.60%	$>/=31,172	>/=4.50%	$>=45,026	>/=6.50%
Tier I capital (to average assets)						
Company	$63,646	6.57 %	$>/=38,730	>/=4.00%	$>/=48,412	>/=5.00%
Bank	$101,137	10.45%	$>/=38,725	>/=4.00%	$>/=48,406	>/=5.00%

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