FNCB Bancorp, Inc.
Form 10-K
March 10, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2016

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

FNCB BANCORP, INC.

(Exact Name of Registrant as Specified in Its Charter)

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

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

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

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

Common Stock, $1.25 par value

(Title of Class)

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

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or section 15(d) of the Act. Yes No

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

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

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

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

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

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

The aggregate market value of the voting and non-voting common stock of the registrant, held by non-affiliates was $80,096,019 at June 30, 2016.

APPLICABLE ONLY TO CORPORATE REGISTRANTS

State the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date: 16,661,978 shares of common stock as of March 10, 2017.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information required by Items 10, 11, 12, 13 and 14 is incorporated by reference into Part III hereof from portions of the Proxy Statement for the registrant's 2017 Annual Meeting of Shareholders.

Contents

PART I

Item 1. Business

Overview

The Company

FNCB Bancorp, Inc., formerly First National Community Bancorp, Inc., incorporated in 1997, is a Pennsylvania business corporation and a registered bank holding company headquartered in Dunmore, Pennsylvania. FNCB Bancorp, Inc. became an active bank holding company on July 1, 1998 when it acquired 100% ownership of the former First National Community Bank. In this report, the terms "FNCB," "we," "us," and "our" refer to FNCB Bancorp, Inc. and its subsidiaries, unless the context requires otherwise. In certain circumstances, however, FNCB Bancorp, Inc. uses the term "FNCB" to refer to itself.

Effective June 30, 2016, following receipt of required regulatory approvals from the Pennsylvania Department of Banking and Securities, First National Community Bank completed a charter conversion from a national bank to a Pennsylvania state bank. Following the change in charter, First National Community Bank changed its legal name to FNCB Bank (the "Bank"). Subsequently, on October 4, 2016, the holding company filed an amendment to its articles of incorporation to change its name, effective October 17, 2016, from First National Community Bancorp, Inc. to FNCB Bancorp, Inc.

FNCB's primary activity consists of owning and operating the Bank, which provides substantially all of FNCB's earnings as a result of its banking services.

FNCB had net income of $6.3 million, $35.8 million and $13.4 million in 2016, 2015 and 2014, respectively. Total assets were $1.2 billion at December 31, 2016, $1.1 billion at December 31, 2015 and $1.0 billion at December 31, 2014.

The Bank

Established as a national banking association in 1910, as of December 31, 2016 the Bank operated 19 full-service branch offices within three contiguous counties, Lackawanna, Luzerne and Wayne, its primary market area located in the Northeast section of Pennsylvania.

On January 6, 2017, the Bank notified the Pennsylvania Department of Banking and Securities and FNCB's federal banking regulators of its intent to open a limited purpose office ("LPO") in Allentown, Lehigh County, Pennsylvania. The Pennsylvania Department of Banking and Securities issued a non-objection letter to the Bank on February 22, 2017 regarding the establishment of the Allentown-based LPO.

Products and Services

Retail Banking

The Bank provides a wide variety of traditional banking products and services to individuals and businesses, including online, mobile and telephone banking, debit cards, check imaging and electronic statements. Deposit products include various checking, savings and certificate of deposit products, as well as a line of preferred products for higher-balance customers. The Bank is a member of the Promontory Interfinancial Network and participates in their Certificate of Deposit Account Registry ("CDARs") and Insured Cash Sweep ("ICS") programs, which allow customers to secure Federal Deposit Insurance Corporation ("FDIC") insurance on balances in excess of the standard limitations.

The Bank also offers customers the convenience of 24-hour banking, seven days a week, through FNCB Online Banking ("FNCB Online") and FNCB Business Online Banking via a secure website, https://www.fncb.com. FNCB's online product suite includes Bill Payment, Internal and External Funds Transfer and POP Money (person to person transfers), and Purchase Rewards. Through FNCB Online, customers can directly access their accounts, open new accounts and apply for a mortgage or obtain a pre-qualification approval through the Bank's mortgage center. Customers can also access FNCB Online through the Bank's mobile application. Telephone banking ("Account Link"), a service that provides customers with the ability to access account information and perform related account transfers through the use of a touch tone telephone, is also available. In addition, customers can access money from their deposit accounts by using their debit card to make purchases or withdraw cash from any automated teller machines ("ATMs") including ATMs located in each of the Bank's branch offices as well as additional locations. FNCB's mobile deposit, available to personal banking customers with access to FNCB Online and an eligible deposit account, allows customers to deposit checks, electronically from start to finish, from anywhere at any time.

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

The Bank offers several overdraft protection products including, Bounce Protection, Instant Money and transfer from another FNCB checking or savings account, which provide customers with an added level of protection against unanticipated overdrafts due to cash flow emergencies and account reconciliation errors. The Bank offers its customers an identity theft protection plan through a strategic partnership with an independent vendor. Subscribers select which coverage package they desire by visiting the Bank's secure website and choosing "Identity Protection" from the Resources menu.

Lending Activities

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

Residential Mortgage Loans

FNCB offers a variety of fixed-rate one- to four-family residential loans including First Time Homebuyer mortgages, FHA and Home Possible® mortgages to meet the home financing needs of customers with low down payments. FNCB also offers a "WOW" mortgage, a first-lien, fixed-rate mortgage product with maturity terms ranging from 7.5 to 14.5 years. At December 31, 2016, one- to four-family residential mortgage loans totaled $144.3 million, or 19.7%, of the total loan portfolio. Except for the WOW mortgage, one- to four-family mortgage loans are originated generally for sale in the secondary market. However, FNCB may hold in portfolio one- to four-family residential mortgage loans as deemed necessary according to current asset/liability management strategies. During the year ended December 31, 2016, the Bank sold $9.5 million of one- to four-family mortgages. FNCB retains servicing rights on these mortgages.

Construction, Land Acquisition and Development Loans

FNCB offers interim construction financing secured by residential property for the purpose of constructing one- to four-family homes. FNCB also offers interim construction financing for the purpose of constructing residential developments and various commercial properties including shopping centers, office complexes and single purpose owner-occupied structures and for land acquisition. At December 31, 2016, construction, land acquisition and development loans amounted to $18.4 million and represented 2.5% of the total loan portfolio.

Commercial Real Estate Loans

Commercial real estate mortgage loans represent the largest portion of FNCB's total loan portfolio and loans in this portfolio generally have larger loan balances. These loans are secured by a broad range of real estate, including but not limited to, office complexes, shopping centers, hotels, warehouses, gas stations, convenience markets, residential care facilities, nursing care facilities, restaurants, multifamily housing, farms and land subdivisions. At December 31, 2016, FNCB's commercial real estate loans totaled $243.8 million, or 33.3%, of the total loan portfolio.

Commercial and Industrial Loans

FNCB generally offers commercial loans to sole proprietors and businesses located in its primary market area. The commercial loan portfolio includes, but is not limited to, lines of credit, dealer floor plan lines, equipment loans, vehicle loans and term loans. These loans are primarily secured by vehicles, machinery and equipment, inventory, accounts receivable, marketable securities and deposit accounts. At December 31, 2016, FNCB's commercial and industrial loans totaled $153.8 million, or 21.0%, of the total loan portfolio.

Consumer Loans

Consumer loans include both secured and unsecured installment loans, lines of credit and overdraft protection loans. The Bank is also in the business of underwriting indirect auto loans which are originated through various auto dealers in its market area and dealer floor plan loans. FNCB also offers home equity loans and lines of credit with a maximum combined loan-to-value ratio of 90%, based on the appraised value of the property. Home equity loans have fixed rates of interest and are for terms up to 15 years. Home equity lines of credit have adjustable interest rates and are based on the prime interest rate. At December 31, 2016, FNCB's consumer loans totaled $127.8 million, or 17.5%, of the total loan portfolio.

State and Political Subdivision Loans

FNCB originates state and political subdivision loans, including general obligation and tax anticipation notes, primarily to municipalities in the Bank's market area. At December 31, 2016, FNCB's state and political subdivision loans totaled $43.7 million, or 6.0%, of the total loan portfolio.

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

Wealth Management

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

Deposit Activities

In general, deposits, borrowings and loan repayments are the major sources of funding for lending and other investment purposes. FNCB relies primarily on marketing, product innovation, technology and service to attract, grow and retain its deposits. Deposit account terms vary according to the minimum balance required, the time periods the funds must remain on deposit and the interest rate, among other factors. In determining the terms of deposit accounts, management considers the interest rates offered by its competitors, the interest rates available on borrowings, its liquidity needs and customer preferences. Management regularly reviews FNCB's deposit mix and deposit pricing as part of its asset/liability management, taking into consideration rates offered by competitors in its market area.

Competition

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

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

Supervision and Regulation

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

FNCB

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

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

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

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

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

FNCB also is subject to the jurisdiction of the Securities and Exchange Commission (“SEC”) and is subject to the disclosure and regulatory requirements under the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended. The common stock of FNCB trades on the OTCQX marketplace under the symbol “FNCB” and, therefore, FNCB also is subject to the rules and requirements of FINRA for companies with securities trading on the OTCQX.

The Bank

Effective June 30, 2016, upon its conversion to a state charter, the Bank is regulated by the Pennsylvania Department of Banking and Securities. The Bank's deposit accounts are insured up to the maximum legal limit by the Deposit Insurance Fund of the FDIC and accordingly, the Bank is also regulated by the FDIC. The regulations of these agencies and the FDIC govern most aspects of the Bank's business, including required reserves against deposits, loans, investments, mergers and acquisitions, borrowings, dividends and location and number of branch offices. The laws and regulations governing the Bank generally have been promulgated to protect depositors and the Deposit Insurance Fund, and not for the purpose of protecting shareholders.

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

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

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

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

The federal banking regulators issued a final rulemaking in July 2013 (the "Basel III Rule") to implement the Basel III regulatory capital reforms and changes required by the Dodd-Frank Act. The phase-in period for community banking organizations began January 1, 2015, while larger institutions (generally those with assets of $250 billion or more) began compliance on January 1, 2014. The final rules call for the following capital requirements:

- A minimum ratio of common equity tier I ("CET I") capital to risk-weighted assets of 4.5%.
- A minimum ratio of tier I capital to risk-weighted assets of 6%.
- A minimum ratio of total capital to risk-weighted assets of 8%.
- A minimum leverage ratio of 4%.

Basel III also establishes a "countercyclical capital buffer," that is designed to absorb losses during periods of economic stress. Generally, the capital conservation buffer of 2.50% of risk-weighted assets, when fully phased in, will be imposed when federal banking regulators determine that excess aggregate credit growth becomes associated with a buildup of systemic risk. For all banking institutions, the phase-in period for the capital conservation buffer requirement began on January 1, 2016 at 0.625% and will increase by that amount each year until it reaches 2.50% on January 1, 2019.

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

The Basel III Rule also includes, as part of the definition of CET I capital, a requirement that banking institutions include the amount of Accumulated Other Comprehensive Income ("AOCI"), which primarily consists of unrealized gains and losses, net of tax, on available-for-sale securities, that are not other than temporarily impaired ("OTTI") in calculating regulatory capital, unless the institution makes a one-time opt-out election from this provision in connection with the filing of its first regulatory reports after applicability of the Basel III Rule to that institution. The Basel III Rule also imposes a 4.00% minimum Tier I leverage ratio.

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

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

As discussed below, the Basel III Rule also integrates the new capital requirements into the prompt corrective action provisions under Section 38 of the Federal Deposit Insurance Act (“FDIA”).

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

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

The following are the capital requirements under the Basel III Rules integrated into the prompt corrective action category definitions. As of December 31, 2016, the following capital requirements were applicable to the Bank for purposes of Section 38 of the FDIA.

Capital Category	**Total Risk-Based Capital Ratio**	**Tier I Risk-Based Capital Ratio**	**CET I Capital Ratio**	**Leverage Ratio**	**Tangible Equity to Assets**
Well capitalized	>/=10.0%	>/=8.0%	>/=6.5%	>/=5.0%	N/A
Adequately capitalized with converation buffer	>/=8.625%	>/=6.625%	>/=5.125%	>/=4.0%	N/A
Adequately capitalized	>/=8.0%	>/=6.0%	>/=4.5%	>/=4.0%	N/A
Undercapitalized	<8.0%	<6.0%	<4.5%	<4.0%	N/A
Significantly undercapitalized	<6.0%	<4.0%	<3.0%	<3.0%	N/A
Critically undercapitalized	N/A	N/A	N/A	N/A	Less than 2.0%

At December 31, 2016, FNCB met its capital requirements with a common equity Tier I capital to risk-weighted assets of 9.97%, a Tier I capital to risk-weighted assets ratio of 10.23%, a Total capital to risk-weighted assets ratio of 12.06%, and a Leverage ratio of 7.53%.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

President Donald J. Trump has indicated that one of the goals of his administration is to reduce federal government regulation, including, among other things, reconsidering certain regulations promulgated under the Dodd-Frank Act. On February 3, 2017, President Trump issued an executive order that directs the Secretary of the Treasury Department to consult with the heads of the member agencies of the Financial Stability Oversight Council and report to President Trump on the extent to which the laws and regulations governing the U.S. financial system are in accord with certain enumerated “core principles” (the “Executive Order”). The “core principles” set forth in the Executive Order relate to U.S. financial system regulation, and include fostering economic growth and vibrant financial markets through more rigorous regulatory impact analysis, and making “regulation more efficient, effective and appropriately tailored.” Given the recent nature of this Trump Administration initiative, at this time, FNCB cannot determine what existing provisions of and regulations under the Dodd-Frank Act, if any, will be repealed or modified, or what impact, if any, the effect of the Trump Administration’s initiative may have on FNCB, its business or future results of operations.

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

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

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

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

The CFPB's rulemaking, examination and enforcement authority has and will continue to significantly affect financial institutions offering consumer financial products and services, including FNCB and the Bank. These regulatory activities may limit the types of financial services and products the Bank may offer, which in turn may reduce FNCB's revenues.

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

The Dodd-Frank Act permanently increased the maximum deposit insurance amount for banks, savings institutions and credit unions to $250,000 per depositor. The Dodd-Frank Act also broadened the base for FDIC insurance assessments. Assessments are now based on a financial institution's average consolidated total assets less tangible equity capital. The Dodd-Frank Act requires the FDIC to increase the reserve ratio of the Deposit Insurance Fund from 1.15% to 1.35% of insured deposits by 2020 and eliminates the requirement that the FDIC pay dividends to insured depository institutions when the reserve ratio exceeds certain thresholds. The Dodd-Frank Act eliminated the statutory prohibition against the payment of interest on business checking accounts.

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

At December 31, 2016, the Bank was considered risk category I, the lowest risk category, for deposit insurance assessments and paid an annual assessment rate ranging from 0.0005 basis points to 0.0006 basis points on the assessment base of average consolidated total assets less the average tangible equity during the assessment period.

Dividend Restrictions

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

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

Employees

As of December 31, 2016, FNCB, including the Bank employed 253 persons, including 34 part-time employees.

Available Information

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

Item 1A. Risk Factors.

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

Risks Related to FNCB and its Business

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

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

Downward trends in the economic environment could pose significant challenges for FNCB and could adversely affect its financial condition and results of operations.

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

- economic conditions that negatively affect housing prices and the job market could result in deterioration in credit quality of the loan portfolios, which, in turn, could have , a negative impact on our business;
- market developments may affect consumer confidence levels and result in reduced loan demand and cause adverse changes in payment patterns, leading to a reduced asset base, as well as increases in delinquencies and default rates on loans and other credit facilities;
- the methodologies that are used to establish the ALLL rely on complex judgments, including forecasts of economic conditions, that are inherently uncertain and may be inadequate;
- the continuation of low market interest rates, may further pressure FNCB's interest margins as interest-earning assets, such as loans and investments, are reinvested or reprice at lower rates; and
- volatility in the market, and lower level of confidence in the banking system, could require the Bank to pay higher interest rates to obtain deposits to meet the needs of its depositors and borrowers, resulting in reduced margin and net interest income. If conditions worsen, it is possible that banks such as the Bank may be unable to meet the needs of their depositors and borrowers, which could, in the worst case, result in the Bank being placed into receivership.

If these conditions or similar ones continue to exist or worsen, FNCB could experience adverse effects on its operating results and/or financial condition.

FNCB is subject to lending risk.

As of December 31, 2016, approximately 35.8% of FNCB's loan portfolio consisted of commercial real estate loans and construction, land acquisition and development loans. These types of loans are generally viewed as having a higher risk of default than residential real estate loans or consumer loans. These types of loans are also typically larger than residential real estate loans and consumer loans. Because FNCB's loan portfolio contains a significant number of commercial real estate loans with relatively large balances, the deterioration of one or a few of these loans could cause a significant increase in non-performing loans. All non-performing loans totaled $2.2 million, or 0.3% of total gross loans, as of December 31, 2016, and $3.8 million, or 0.5% of total gross loans, as of December 31, 2015. Although non-performing asset levels decreased from the prior year, an increase in non-performing loans in the future could result in an increase in the provision for loan and lease losses and an increase in loan charge-offs, both of which could have a material adverse effect on FNCB's financial condition and results of operations. The lending activities in which the Bank engages carry the risk that the borrowers will be unable to perform on their obligations. As such, general economic conditions, nationally and in FNCB's primary market area, will have a significant impact on its results of operations. To the extent that economic conditions deteriorate, business and individual borrowers may be less able to meet their obligations to the Bank in full, in a timely manner, resulting in decreased earnings or losses to the Bank. To the extent that loans are secured by real estate, adverse conditions in the real estate market may reduce the ability of the borrowers to generate the necessary cash flow for repayment of the loan, and reduce the ability to collect the full amount of the loan upon a default. To the extent that the Bank makes fixed-rate loans, general increases in interest rates will tend to reduce its spread as the interest rates FNCB must pay for deposits would increase while interest income is flat. Economic conditions and interest rates may also adversely affect the value of property pledged as security for loans.

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

A substantial portion of FNCB's loans are secured by real estate in the Northeastern Pennsylvania market, and substantially all of its loans are to borrowers in that area. FNCB also has a significant amount of commercial real estate, commercial and industrial, construction, land acquisition and development loans and land-related loans for residential and commercial developments. At December 31, 2016, $430.1 million, or 58.8%, of gross loans were secured by real estate, primarily commercial real estate. Management has taken steps to mitigate commercial real estate concentration risk by diversification among the types and characteristics of real estate collateral properties, sound underwriting practices, and ongoing portfolio monitoring and market analysis. Of total gross loans, $18.4 million, or 2.5%, were construction, land acquisition and development loans. Construction, land acquisition and development loans have the highest risk of uncollectability. An additional $153.8 million, or 21.0%, of portfolio loans were commercial and industrial loans not secured by real estate. Historically, commercial and industrial loans generally have had a higher risk of default than other categories of loans, such as single family residential mortgage loans. The repayment of these loans often depends on the successful operation of a business and are more likely to be adversely affected by adverse economic conditions. While management believes that the loan portfolio is well diversified in terms of borrowers and industries, these concentrations expose FNCB to the risk that adverse developments in the real estate market, or in the general economic conditions in its general market area, could increase the levels of non-performing loans and charge-offs, and reduce loan demand. In that event, FNCB would likely experience lower earnings or losses. Additionally, if, for any reason, economic conditions in its market area deteriorate, or there is significant volatility or weakness in the economy or any significant sector of the area's economy, FNCB's ability to develop business relationships may be diminished, the quality and collectability of its loans may be adversely affected, the value of collateral may decline and loan demand may be reduced.

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

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

Outstanding loans and line of credit balances to directors, officers and their related parties totaled $42.0 million as of December 31, 2016. At December 31, 2016, except for one loan relationship aggregating $381 thousand to a business partially owned by a director that was classified as “Special Mention,” there were no loans to directors, officers and their related parties that were categorized as criticized loans within the Bank’s risk rating system, meaning they are not considered to present a higher risk of collection than other loans. FNCB has received all contractual principal and interest payments in a timely manner and the individual loans in the relationship were current as of December 31, 2016. Management has classified the loan relationship as special mention strictly because FNCB has not received current financial information from a non-related party to the loan agreements. For more information regarding loans to officers and directors and/or their related parties, please refer to Note 11, “Related Party Transactions” to the consolidated financial statements included in Item 8 and Item 13, “Certain Relationships and Related Transactions, and Director Independence” to this Annual Report on Form 10-K.

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

The lending activities in which the Bank engages carry the risk that the borrowers will be unable to perform on their obligations, and that the collateral securing the payment of their obligations may be insufficient to assure repayment. FNCB may experience significant credit losses, which could have a material adverse effect on its operating results. Management makes various assumptions and judgments about the collectability of FNCB’s loan portfolio, including the creditworthiness of its borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of its loans, which it uses as a basis to estimate and establish its reserves for losses. In determining the amount of the ALLL, management reviews loans, loss and delinquency experience, and evaluates current economic conditions. If these assumptions prove to be incorrect, the ALLL may not cover inherent losses in FNCB’s loan portfolio at the date of its financial statements. Material additions to FNCB’s allowance or extensive charge-offs would materially decrease its net income. At December 31, 2016, the ALLL totaled $8.4 million, representing 1.15% of total loans.

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

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

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

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

FNCB held approximately $3.3 million in capital stock of the Federal Home Loan Bank of Pittsburgh ("FHLB") as of December 31, 2016. FNCB must own such capital stock to qualify for membership in the Federal Home Loan Bank system which enables it to borrow funds under the FHLB advance program. If the FHLB were to cease operations, FNCB's business, financial condition, liquidity, capital and results of operations may be materially and adversely affected.

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

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

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

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

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

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

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

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

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

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

Effective and competitive delivery of FNCB's products and services increasingly depends on information technology resources and processes, both those provided internally as well as those provided through third party vendors. In addition to better serving customers, the effective use of technology can improve efficiency and help reduce costs. FNCB's future success will depend, in part, upon its ability to address the needs of its customers by using technology to provide products and services to enhance customer convenience, as well as to create efficiencies in its operations. There is increasing pressure to provide products and services at lower prices. This can reduce net interest income and noninterest income from fee-based products and services. In addition, the widespread adoption of new technologies could require FNCB to make substantial capital expenditures to modify or adapt existing products and services or develop new products and services. FNCB may not be successful in introducing new products and services in response to industry trends or developments in technology, or those new products may not achieve market acceptance. Many of FNCB's competitors have greater resources to invest in technological improvements. Additionally, as technology in the financial services industry changes and evolves, keeping pace becomes increasingly complex and expensive. There can be no assurance that FNCB will be able to effectively implement new technology-driven products and services, which could reduce its ability to compete effectively. As a result, FNCB could lose business, be forced to price products and services on less advantageous terms to retain or attract customers, or be subject to cost increases.

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

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

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

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

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

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

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

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

FNCB maintains disclosure controls and procedures designed to ensure the timely filing of reports as specified in the rules and forms of the Securities and Exchange Commission. FNCB also maintains a system of internal control over financial reporting. These controls may not achieve their intended objectives. Control processes that involve human diligence and compliance, such as its disclosure controls and procedures and internal controls over financial reporting, are subject to lapses in judgment and breakdowns resulting from human failures. Controls can also be circumvented by collusion or improper management override. Because of such limitations, there are risks that material misstatements due to error or fraud may not be prevented or detected and that information may not be reported on a timely basis. If FNCB's controls are not effective, it could have a material adverse effect on its financial condition, results of operations, and market for its common stock, and could subject it to additional regulatory scrutiny.

Risks Related to FNCB's Common Stock

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

FNCB's common stock per share price may fluctuate significantly as a result of a variety of factors, many of which are beyond its control. These factors include, in addition to those described above:

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

During 2016, the per share closing bid price of FNCB's common stock on the OTCQX Marketplace ("OTCQX") ranged from a low of $4.75 on August 29, 2016, to a high of $6.90 on February 1, 2016.

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

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

FNCB's common shares are currently quoted on the OTCQX. During the year ended December 31, 2016, an average of 3,484 shares traded on a daily basis. There can be no assurance that an active and liquid market for FNCB's common shares will develop, or if one develops that it can be maintained. The absence of an active trading market may make it difficult for FNCB shareholder to sell FNCB's common shares at the prevailing price, particularly in large quantities. For a further discussion, see Item 5, "Market for Registrant's Common Equity, Related Shareholder Matters, and Issuer Purchases of Equity Securities" to this Annual Report on Form 10-K.

FNCB's ability to pay dividends or repurchase shares is subject to limitations.

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

Risks Related to Government Regulation and Accounting Pronouncements

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

The banking industry is subject to extensive regulation and supervision that govern almost all aspects of its operations. The extensive regulatory framework is primarily intended to protect the federal deposit insurance fund and depositors, not shareholders. Compliance with applicable laws and regulations can be difficult and costly and, in some instances, may put banks at a competitive disadvantage compared to less regulated competitors such as finance companies, mortgage banking companies, leasing companies and internet-based Fintech companies. FNCB's regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including with respect to the imposition of restrictions on the operation of a bank or a bank holding company, the imposition of significant fines, the ability to delay or deny merger or other regulatory applications, the classification of assets by a bank, and the adequacy of a bank's allowance for loan losses, among other matters. If they deem FNCB to be operating in a manner inconsistent with safe and sound banking practices, these regulatory authorities can require the entry into informal and formal supervisory agreements, including board resolutions, memoranda of understanding, settlement agreements and consent or cease and desist orders, pursuant to which FNCB would be required to implement identified corrective actions to address cited concerns and/or to refrain from taking certain actions in the form of injunctive relief. In recent years, the banking industry has faced increased regulation and scrutiny; for instance, areas such as BSA compliance (including BSA and related anti-money laundering regulations) and real estate-secured consumer lending (such as Truth-in-Lending regulations, changes in Real Estate Settlement Procedures Act regulations, implementation of licensing and registration requirements for mortgage originators and more recently, heightened regulatory attention to mortgage and foreclosure-related activities and exposures) are being confronted with escalating regulatory expectations and scrutiny. Non-compliance with laws and regulations such as these, even in cases of inadvertent non-compliance, could result in litigation, significant fines and/or sanctions. Any failure to comply with, or any change in, any applicable regulation and supervisory requirement, or change in regulation or enforcement by such authorities, whether in the form of policies, regulations, legislation, rules, orders, enforcement actions, or decisions, could have a material impact on FNCB, the Bank and other affiliates, and its operations. Federal economic and monetary policy may also affect FNCB’s ability to attract deposits and other funding sources, make loans and investments, and achieve satisfactory interest spreads. Any failure to comply with such regulation or supervision could result in sanctions by regulatory agencies, civil money penalties and/or reputation damage, which could have a material adverse effect on FNCB’s business, financial condition and results of operations. In addition, compliance with any such action could distract management’s attention from FNCB’s operations, cause it to incur significant expenses, restrict it from engaging in potentially profitable activities and limit its ability to raise capital.

The impact of recent legislation, proposed legislation, and government programs designed to stabilize the financial markets cannot be predicted at this time, and such legislation is subject to change. In addition, any instability in financial markets and weakening in current financial market conditions could materially and adversely affect FNCB’s business, financial condition, results of operations and access to capital.

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

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

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

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

Changes in accounting standards could impact reported earnings.

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

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

FNCB currently conducts business from its headquarters, which also houses the Bank's main office, located at 102 East Drinker Street, Dunmore, Pennsylvania, 18512. At December 31, 2016, FNCB also operated 18 additional branches located throughout Lackawanna, Luzerne and Wayne counties, a loan production office located in Wilkes-Barre, Luzerne County, Pennsylvania and two administrative offices located in Dunmore, Lackawanna County, Pennsylvania. Fourteen of the offices are leased and the balance are owned by the Bank. Except for potential remodeling of certain facilities to provide for the efficient use of work space and/or to maintain an appropriate appearance, each property is considered reasonably suitable and adequate for current and immediate future purposes.

As part of its responsibilities, management regularly evaluates FNCB's delivery system and facilities including analyzing each office's operating efficiency, location, foot traffic, structure and design. The results of these evaluations may lead to improvements in FNCB's delivery system network and facilities including the remodeling, consolidation and/or relocation of existing facilities and branches and the potential for opening offices and/or branches in new market areas.

On December 21, 2016, the Bank purchased a building located immediately adjacent to its main office at 106-108 East Drinker Street, Dunmore, Pennsylvania, 18512. On February 15, 2017, the Bank notified the Pennsylvania Department of Banking and Securities and its federal banking regulators of its intent to open a lending center at this location for the purpose of housing its commercial and retail lending units. This lending center is scheduled to open at the end of the first quarter of 2017.

On January 6, 2017, the Bank notified the Pennsylvania Department of Banking and Securities and FNCB’s federal banking regulators of its intent to open a Limited Purpose Office (“LPO”) in Allentown, Lehigh County, Pennsylvania to provide services related to loan production. This LPO is located in an office leased by the Bank at 3500 Winchester Road, Suites 101 and 102, Allentown, Pennsylvania, 18104. The Pennsylvania Department of Banking and Securities issued a non-objection letter to the Bank on February 22, 2017 regarding the establishment of the Allentown-based LPO.

Item 3. Legal Proceedings.

On May 24, 2012, a putative shareholder filed a complaint in the Court of Common Pleas for Lackawanna County (“Shareholder Derivative Suit”) against certain present and former directors and officers of FNCB (the “Individual Defendants”) alleging, inter alia, breach of fiduciary duty, abuse of control, corporate waste, and unjust enrichment. FNCB was named as a nominal defendant. The parties to the Shareholder Derivative Suit commenced settlement discussions and on December 18, 2013, the Court entered an Order Granting Preliminary Approval of Proposed Settlement subject to notice to shareholders. On February 4, 2014, the Court issued a Final Order and Judgment for the matter granting approval of a Stipulation of Settlement (the “Settlement”) and dismissing all claims against FNCB and the Individual Defendants. As part of the Settlement, there was no admission of liability by the Individual Defendants. Pursuant to the Settlement, the Individual Defendants, without admitting any fault, wrongdoing or liability, agreed to settle the derivative litigation for $5.0 million. The $5.0 million Settlement payment was made to FNCB on March 28, 2014. The Individual Defendants reserved their rights to indemnification under FNCB’s Articles of Incorporation and Bylaws, resolutions adopted by the Board, the Pennsylvania Business Corporation Law and any and all rights they have against FNCB’s and the Bank’s insurance carriers. In addition, in conjunction with the Settlement, FNCB accrued $2.5 million related to fees and costs of the plaintiff’s attorneys, which was included in non-interest expense in the consolidated statements of income for the year ended December 31, 2013. On April 1, 2014, FNCB paid the $2.5 million related to fees and costs of the plaintiff’s attorneys and partial indemnification of the Individual Defendants in the amount of $2.5 million, and as such, as of September 30, 2016 $2.5 million plus accrued interest remains accrued in other liabilities related to the potential indemnification of the Individual Defendants.

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

On February 16, 2017, FNCB and the Bank entered into a Class Action Settlement Agreement and Release (the "Settlement Agreement") in the matters filed in the Court of Common Pleas of Lackawanna County to *Steven Antonik, Individually, and as Administrator of the Estate of Linda Kluska, William R. Howells and Louise A. Howells, Summer Benjamin, and Joshua Silfee, on behalf of themselves and all others similarly situated vs. First National Community Bancorp, Inc. and First National Community Bank*, Civil Action No. 2013-CV-4438 and *Charles Saxe, III, Individually and on behalf of all others similarly situated vs. First National Community Bank* No. 2013-CV-5071 (collectively, the "Actions"). By entering into this Settlement Agreement, the parties to the Actions have resolved the claims made in the complaints to their mutual satisfaction. FNCB has not admitted to the validity of any claims or allegations and deny any liability in the claims made and the Plaintiffs have not admitted that any claims or allegations lack merit or foundation. Under the terms of the Settlement Agreement, the parties have agreed to the following: 1) FNCB is to pay the Plaintiffs' class members the aggregate sum of Seven Hundred Fifty Thousand and 00/100 ($750,000.00)(an amount which FNCB recorded as a liability and corresponding expense in its 2015 operating results); 2) Plaintiffs shall release all claims against FNCB related to the Actions; 3) FNCB shall move to vacate or satisfy any judgments against any class members arising from the vehicle loans that are the subject of the Actions; 4) FNCB shall waive the deficiency balance of each class member and remove the trade lines on each class members' credit report associated with the subject vehicle loans that are at issue in the Actions for Experian, Equifax and Transunion. The Settlement Agreement provides for an Incentive Award for the representative Plaintiffs and an award to Plaintiffs' counsel of attorney's fees and reimbursement of expenses in connection with their roles in these Actions, subject to Court Approval. The Settlement Agreement remains subject to approval by the Court after notice to the class members and a final settlement hearing. The hearing on the terms of the proposed Settlement Agreement will be to determine whether 1) the terms and conditions of the settlement provided for in the Settlement Agreement are fair, reasonable and adequate and in the best interests of the class members; 2) the judgment dismissing the claims of the class members, as provided for in the Settlement Agreement, shall be entered, and 3) the request of the representative Plaintiffs for the Incentive Award and the Plaintiffs' counsel for an award for attorney's fees and reimbursement of expenses shall be granted. As previously mentioned above, and in connection with, the primary terms of the tentative settlement agreement entered by Order of Court on December 17, 2015, FNCB recorded a liability and corresponding expense in the amount of Seven Hundred Fifty Thousand and 00/100 ($750,000.00), which was included in FNCB's 2015 operating results.

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

Item 4. Mine Safety Disclosures.

Not Applicable.

PART II

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

Market Prices of Stock and Dividends Paid

FNCB's common shares are quoted on the OTCQX under the symbol "FNCB." Quarterly market highs and lows and dividends paid for each of the past two years are presented below. These prices represent actual transactions.

	Market Price		**Dividends Paid**
	High	**Low**	**Per Share**
Quarter	**2016**		**2016**
First	$6.90	$5.11	$ 0.02
Second	6.12	5.50	0.02
Third	6.00	4.75	0.02
Fourth	6.30	5.00	0.03
Quarter	**2015**		**2015**
First	$6.10	$5.12	$0.00
Second	6.55	5.15	0.00
Third	6.05	5.02	0.00

Fourth	5.50	5.06	0.00

Holders

As of February 28, 2017, there were approximately 1,778 holders of record of FNCB's common shares. Because many of FNCB's shares are held by brokers and other institutions on behalf of shareholders, FNCB is unable to estimate the total number of shareholders represented by these record holders.

Dividends

FNCB had been under a Written Agreement with the Federal Reserve Bank of Philadelphia from November 24, 2010 until it was fully and completely released from the enforcement action on September 2, 2015. The Bank had been under a Consent Order with the Office of the Comptroller of the Currency from September 1, 2010 until it was fully and completely released from the enforcement action on March 25, 2015. While under the Written Agreement, FNCB was precluded from paying dividends, and accordingly, did not pay dividends to shareholders during the tenure of the Written Agreement. FNCB resumed quarterly dividend payments effective with a quarterly dividend paid on March 15, 2016. It is the present intent of the Board of Directors to continue paying quarterly dividends going forward. However, FNCB's ability to declare and pay future dividends is dependent upon earnings, financial position, appropriate restrictions under applicable laws, legal and regulatory restrictions and other factors relevant at the time FNCB's Board of Directors considers any declaration of any dividends. For a further discussion of FNCB's and the Bank's dividend restrictions, refer to Note 14, "Regulatory Matters/Subsequent Events" in the notes to consolidated financial statements to this Annual Report on Form 10-K.

In addition to the resumption of dividend payments, on April 27, 2016, FNCB's Board of Directors approved the reinstatement of the Dividend Reinvestments and Stock Purchase Plan effective June 1, 2016.

Equity Compensation Plans

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

Performance Graph

The following graph compares the cumulative total shareholder return (i.e. price change, reinvestment of cash dividends and stock dividends received) on FNCB's common shares against the cumulative total return of the NASDAQ Stock Market (U.S. Companies) Index, the SNL Bank Index for banks with $500 million to $1 billion in assets and the SNL U.S. Bank Pink for banks traded on the OTC with total assets greater than $500 million. The stock performance graph assumes that $100 was invested on December 31, 2011. The graph further assumes the reinvestment of dividends into additional shares of the same class of equity securities at the frequency with which dividends are paid on such securities during the relevant fiscal year. The yearly points marked on the horizontal axis correspond to December 31 of that year. FNCB calculates each of the referenced indices in the same manner. All are market-capitalization-weighted indices, so companies judged by the market to be more important (i.e. more valuable) count for more in all indices.

Purchase of Equity Securities by the Issuer and Affiliated Purchasers

None.

Recent Sales of Unregistered Securities

None.

Item 6. Selected Financial Data

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

	For the Years Ended December 31,				
(dollars in thousands, except per share data)	**2016**	**2015**	**2014**	**2013**	**2012**
Balance Sheet Data:					
Total assets	$1,195,375	$1,090,618	$970,029	$1,003,808	$968,274
Securities, available-for-sale	272,676	253,773	218,989	203,867	185,361
Securities, held-to-maturity	-	-	-	2,308	2,198
Net loans	725,860	724,926	658,747	629,880	579,396
Total deposits	1,015,139	821,546	795,336	884,698	854,613
Borrowed funds	78,847	160,112	96,504	62,433	53,903
Shareholders' equity	90,147	86,178	51,398	33,578	36,925
Income Statement Data:					
Interest income	$34,748	$32,201	$32,673	$32,953	$37,027
Interest expense	4,197	4,801	6,147	7,176	9,218
Net interest income before provision (credit) for loan and lease losses	30,551	27,400	26,526	25,777	27,809
Provision (credit) for loan and lease losses	1,153	(1,345)	(5,869)	(6,270)	4,065
Non-interest income	6,203	7,800	14,920	9,283	4,283
Non-interest expense	27,545	28,464	33,569	34,948	41,738
Income (loss) before income taxes	8,056	8,081	13,746	6,382	(13,711)
Income tax expense (benefit)	1,747	(27,759)	326	-	-
Net income (loss)	6,309	35,840	13,420	6,382	(13,711)
Earnings (loss) per share, basic and diluted	0.38	2.17	0.81	0.39	(0.83)
Capital and Related Ratios:					
Cash dividends declared per share	$0.09	$-	$-	$-	$-
Book value per share	5.42	5.22	3.12	2.04	2.24
Tier I leverage ratio	7.53%	7.27%	6.05%	4.71%	4.07%
Total risk-based capital to risk-adjusted assets	12.06%	11.79%	13.67%	11.58%	10.20%
Average equity to average total assets (1)	8.42%	5.64%	4.66%	3.60%	3.97%
Tangible equity to tangible assets	7.54%	7.89%	5.27%	3.30%	3.75%
Selected Performance Ratios:					
Return on average assets (1)	0.57%	3.57%	1.38%	0.67%	(1.35%)

Return on average equity (1)	6.82	%	63.24	%	29.50	%	18.65	%	(34.09%	)
Net interest margin (2)	3.13	%	2.99	%	3.08	%	3.21	%	3.26	%
Noninterest income/operating income (2)	14.88	%	18.73	%	30.30	%	20.79	%	9.71	%
Asset Quality Ratios:										
Allowance for loan and lease losses/total loans	1.15	%	1.20	%	1.72	%	2.18	%	3.10	%
Nonperforming loans/total loans	0.31	%	0.52	%	0.82	%	0.99	%	1.62	%
Allowance for loan and lease losses/nonperforming loans	376.86	%	232.05	%	208.62	%	219.87	%	190.92	%
Net charge-offs/average loans	0.21	%	0.20	%	(0.51%	)	(0.28%	)	0.97	%
Loan loss provision/net charge-offs	75.66	%	***		***		***		63.88	%

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

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

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

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

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

FNCB is in the business of providing customary retail and commercial banking services to individuals, businesses and local governments and municipalities within its primary market area located in Northeastern Pennsylvania.

FORWARD-LOOKING STATEMENTS

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

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

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

CRITICAL ACCOUNTING POLICIES

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

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

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

Allowance for Loan and Lease Losses

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

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

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

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

Securities Valuation and Evaluation for Impairment

Management utilizes various inputs to determine the fair value of its investment portfolio. To the extent they exist, unadjusted quoted market prices in active markets (Level 1) or quoted prices for similar assets or models using inputs that are observable, either directly or indirectly (Level 2) are utilized to determine the fair value of each investment in the portfolio. In the absence of observable inputs or if markets are illiquid, valuation techniques are used to determine fair value of any investments that require inputs that are both unobservable and significant to the fair value measurement (Level 3). For Level 3 inputs, valuation techniques are based on various assumptions, including, but not limited to, cash flows, discount rates, adjustments for nonperformance and liquidity, and liquidation values. A significant degree of judgment is involved in valuing investments using Level 3 inputs. The use of different assumptions could have a positive or negative effect on FNCB's financial condition or results of operations. See Note 4,"Securities" and Note 15, "Fair Value Measurements" of the notes to consolidated financial statements included in Item 8, "Financial Statements and Supplementary Data" to this Annual Report on Form 10-K for additional information about FNCB's securities valuation techniques.

On a quarterly basis, management evaluates individual investment securities in an unrealized loss position for other than temporary impairment ("OTTI"). The analysis of OTTI requires the use of various assumptions, including but not limited to, the length of time an investment's fair value is less than book value, the severity of the investment's decline, any credit deterioration of the issuer, whether management intends to sell the security, and whether it is more-likely-than-not that FNCB will be required to sell the security prior to recovery of its amortized cost basis. Debt investment securities deemed to have OTTI are written down by the impairment related to the estimated credit loss, and the non-credit related impairment loss is recognized in other comprehensive income. FNCB did not recognize any OTTI charges on investment securities for years ended December 31, 2016, 2015 and 2014 within the consolidated statements of income.

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

Other Real Estate Owned

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

Income Taxes

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

FNCB records an income tax provision or benefit based on the amount of tax, including alternative minimum tax, currently payable or receivable and the change in deferred tax assets and liabilities. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial and tax reporting purposes. Management conducts quarterly assessments of all available positive and negative evidence to determine the amount of deferred tax assets that will more likely than not be realized. FNCB establishes a valuation allowance for deferred tax assets and records a charge to income if management determines, based on available evidence at the time the determination is made, that it is more likely than not that some portion or all of the deferred tax assets will not be realized. In evaluating the need for a valuation allowance, management considers past operating results, estimates of future taxable income based on approved business plans, future capital requirements and ongoing tax planning strategies. This evaluation process involves significant management judgment about assumptions that are subject to change from period to period depending on the related circumstances. The recognition of deferred tax assets requires management to make significant assumptions and judgments about future earnings, the periods in which items will impact taxable income, future corporate tax rates, and the application of inherently complex tax laws. The use of different estimates can result in changes in the amounts of deferred tax items recognized, which may result in equity and earnings volatility because such changes are reported in current period earnings. On December 31, 2010, management established a valuation allowance equal to 100 percent of FNCB’s net deferred tax asset, excluding deferred tax assets and liabilities related to unrealized holding gains and losses on available-for-sale securities, and maintained such an allowance through December 31, 2014. As part of its evaluation conducted as of December 31, 2015, management reviewed all the positive and negative evidence available at that time and concluded that significant positive evidence outweighed any negative evidence and the valuation allowance previously established for FNCB's deferred tax assets should be reversed, except for the amount established for charitable contribution carryovers. Management's subsequent evaluation as of December 31, 2016 concluded that the previously established valuation allowance for charitable contributions should be reversed, and as such, FNCB did not have any valuation allowances for deferred tax assets as of December 31, 2016.

FNCB uses the current statutory tax rate of 34.0% to value its deferred tax assets and liabilities. The Trump Administration and the U.S. Congress are in the process of evaluating possible tax changes which may include a reduction in the U.S. corporate income tax rates. If corporate tax rates were reduced, management expects FNCB would be required to record an initial charge against earnings to lower the carrying amount of its net deferred tax asset, and then, going forward, would record lower tax provisions on an ongoing basis. There is no specific proposal currently pending. Management cannot assess the effect a change in the corporate tax rate would have on FNCB's operating results or financial position at the present time.

In connection with determining the income tax provision or benefit, management considers maintaining liabilities for uncertain tax positions and tax strategies that it believes contain an element of uncertainty. Periodically, management evaluates each of FNCB's tax positions and strategies to determine whether a liability for uncertain tax benefits is required. As of December 31, 2016 and 2015, management determined that FNCB did not have any uncertain tax positions or tax strategies and that no liability was required to be recorded.

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

New Authoritative Accounting Guidance and Accounting Guidance to be Adopted in Future Periods

For information regarding new authoritative accounting guidance adopted by FNCB during the year ended December 31, 2016 and accounting guidance that FNCB will adopt in future periods, see Note 2, “Summary of Significant Accounting Policies” of the notes to consolidated financial statements included in Item 8, “Financial Statements and Supplementary Data” to this Annual Report on Form 10-K.

EXECUTIVE OVERVIEW

The following overview should be read in conjunction with this MD&A in its entirety.

On June 30, 2016, First National Community Bancorp, Inc., the parent company of First National Community Bank, announced that following receipt of required regulatory approvals from the Pennsylvania Department of Banking and Securities, First National Community Bank had completed a charter conversion from a national bank to a Pennsylvania state bank and, as a result of the conversion, First National Community Bank changed its legal name to FNCB Bank. Both the charter conversion and legal name change were effective June 30, 2016. On October 4, 2016, First National Community Bancorp, Inc., the parent company of FNCB Bank, filed an amendment to its articles of incorporation to change its name, effective October 17, 2016, to “FNCB Bancorp, Inc.” The Board of Directors of FNCB has also amended the bylaws of FNCB, effective October 17, 2016, to reflect the new name.

On May 18, 2016, FNCB announced that effective June 30, 2016, Steven R. Tokach would retire from his position as President and Chief Executive Officer and a member of the Boards of Directors of both FNCB and the Bank. On the same day, both Boards of Directors appointed Gerard A. Champi as his successor effective July 1, 2016. Mr. Champi was appointed as a Class A director of FNCB, with a term expiring at the 2017 annual meeting of shareholders, filling the vacancy created by Mr. Tokach’s retirement. Mr. Champi has been with the Bank since 1991 and has served in various leadership positions, including, most recently, Chief Operating Officer since March 2011 and Interim President and Chief Executive Officer of FNCB and the Bank from March 2010 until February 2011.

Results of Operations

FNCB reported earnings in 2016 of $6.3 million, or $0.38 per diluted common share, a decrease of $29.5 million, or 82.4%, compared to $35.8 million, or $2.17 per diluted common share, in 2015. The decrease in net income was largely attributable to the reversal of the deferred tax asset (“DTA”) valuation allowance of $30.0 million in 2015, resulting in an income tax benefit of $27.8 million for the year ended December 31, 2015. The decrease in 2016 net income compared to 2015 attributable to the reversal was offset in part by strong improvement in net interest income and continued reductions in non-interest expense levels. Net interest income improved $3.1 million, or 11.5%, to $30.5 million in 2016 from $27.4 million in 2015. The improvement resulted primarily from solid growth in interest earning assets, higher yields on taxable loans and investments and reduced borrowing costs. Non-interest expense decreased $0.9 million, or 3.2%, to $27.6 million in 2016 from $28.5 million in 2015. FNCB experienced significant reductions in occupancy expense, regulatory assessments and insurance costs. In addition, FNCB recorded $0.8 million in non-recurring expense related to a legal settlement in 2015. Partially offsetting these cost reductions were increases in salaries and employee benefit costs and bank shares tax. These positive factors were offset by a $1.6 million reduction in non-interest income and a provision for loan and lease losses of $1.2 million in 2016 compared to a credit of $1.3 million in 2015.

Return on average assets and return on average shareholders’ equity equaled 0.57% and 6.82%, respectively, in 2016, compared to 3.57% and 63.24%, respectively, in 2015. For the three months ended December 31, 2016, return on average assets and return on average shareholders’ equity were 0.55% and 6.43%, respectively, compared to 10.99% and 192.68%, respectively, for the same three months of 2015. FNCB paid dividends to holders of common stock of $0.09 per share for the year ended December 31, 2016. FNCB did not pay any dividends during the year ended December 31, 2015.

Balance Sheet Profile

Total assets increased $104.8 million, or 9.6%, to $1.2 billion at December 31, 2016 from $1.1 billion at December 31, 2015. The growth in the balance sheet reflected an increase in total deposits of $193.6 million, or 23.6%, to $1.0 billion at December 31, 2016 from $0.8 billion at the end of 2015, which was used to pay down FHLB advances of $77.3 million, and fund net increases in loans, net of deferred costs and unearned income of $0.6 million, available-for-sale securities of $18.9 million, and cash and cash equivalents of $91.4 million. Specifically, non-interest-bearing demand deposits increased $19.2 million, or 12.4%, and interest-bearing deposits increased $174.4 million, or 26.2%. The increase in non-interest bearing demand deposits primarily reflected growth in business checking accounts, while the increase in interest-bearing deposits was due to growth in municipal deposit accounts. Additionally, on March 1, 2016, FNCB repaid in its entirety $10.8 million in accrued interest that it had been previously deferring on the subordinated debentures for the period September 1, 2010 through May 31, 2015, as well as accelerated the $4.0 million principal payment on the subordinated debentures due September 1, 2017, to December 1, 2016.

Total shareholders' equity improved $4.0 million, or 4.6%, to $90.1 million at December 31, 2016 from $86.2 million at the end of 2015, which resulted primarily from net income for 2016 of $6.3 million, partially offset by a $1.5 million increase in accumulated other comprehensive loss resulting from depreciation in the market value, net of tax, of FNCB's available-for-sale securities, due to changes in market interest rates. Also affecting shareholders' equity were dividends declared and paid of $1.5 million, common shares issued through the dividend reinvestment and optional cash purchase plans of $0.4 million and stock-based compensation of $0.3 million.

At December 31, 2016, FNCB's total risk-based capital ratio and the Tier 1 leverage ratio were 12.06% and 7.53%, respectively. The respective ratios for the Bank at December 31, 2016 were 12.81% and 8.63%. The ratios for both FNCB and the Bank exceeded the 10.00% and 5.00% required to be well capitalized under the prompt corrective action provisions of the Basel III capital framework for U.S. banking organizations.

Management's Focus in 2016

Following the recognition of FNCB's deferred tax assets in 2015, management focused its attention in 2016 on utilizing FNCB's improved capital position to reduce leverage at the holding company level and enhance value for its shareholders through the resumption of quarterly dividend payments and reinstituting the dividend reinvestment and optional cash purchase plans ("DRP"). In addition, management strategies and initiatives in 2016 were aimed at increasing core deposits through collaboration between FNCB's retail and commercial banking units and the addition of a governmental banking department and improving financial performance and efficiency.

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With respect to reducing leverage at the holding company level, on March 1, 2016, FNCB repaid $10.8 million in accrued interest that had previously been deferred on the subordinated debentures ("Notes") for the period September 1, 2010 through May 31, 2015. FNCB had resumed paying interest on the Notes effective with the June 1, 2015 payment and has continued making the quarterly interest payments. In addition, FNCB accelerated a $4.0 million principal payment on the Notes which was originally scheduled for September 1, 2017 to December 1, 2016. As a result, principal and accrued interest on the Notes together decreased $14.9 million, or 59.7%, to $10.0 million at December 31, 2016 from $24.9 million at December 31, 2015.

On March 15, 2016, FNCB resumed paying quarterly dividends with the payment of a $0.02 per share dividend, the first dividend payment since the fourth quarter of 2009. FNCB declared and paid dividends of $0.02 per share for each of the second and third quarters of 2016 and increased the dividend to $0.03 per share for the fourth quarter of 2016. The Bank and FNCB had previously suspended paying dividends in 2010 through 2015 in an effort to conserve capital while operating under a Consent Order and Written Agreement, which they were released from in 2015. In addition to paying quarterly dividends, FNCB reinstituted the DRP effective with the second quarter dividend payment on June 15, 2016. Common shares issued through the plan in 2016 following reinstatement were 78,752 shares. Furthermore, on January 25, 2017, the Board of Directors declared a dividend of $0.03 per share for the first quarter of 2017, an increase of 50.0% compared to the first quarter of 2016. The dividend is payable on March 15, 2017 to shareholders of record on March 1, 2017.

During the second quarter of 2016, FNCB formed a governmental banking department in order to develop banking relationships within the municipal sector. Also, during the second quarter of 2016, FNCB launched the “WOW ME” suite of personal deposit products, which include a high-yield checking account and savings account. Customers are able to earn an annual percentage yield (“APY”) of 2.00% on balances up to $10 thousand for the checking account, an APY of 1.00% on balances up to $25 thousand held in a related savings account and an APY of 0.50% on balances greater than these thresholds. In order to earn these APYs customers must meet certain qualifications, including a monthly direct deposit, a minimum of 12 debit card or ACH transactions per month, and an election to have monthly statements delivered electronically. The formation of the governmental banking department, along with collaboration between the commercial and retail banking units and new WOW ME products, contributed to the 23.6% growth in total deposits.

Management monitors several key metrics in evaluating FNCB’s financial performance. Specifically, a main objective of FNCB’s management team is improving the Bank’s efficiency ratio in order to drive its overall financial performance. The efficiency ratio is a key industry metric and indicator of a bank’s profitability. The efficiency ratio is computed by dividing non-interest expense by the sum of tax-equivalent net interest income and non-interest income. Management also monitors this metric in comparison to the Bank’s peer group. The Bank has experienced significant improvement in its efficiency, as its non-interest expense levels have normalized over recent years. This is evidenced by solid improvement in the efficiency ratio. The Bank’s efficiency ratio, which was 72.76% in 2016, improved 8.7% from 79.67% in 2015, and 14.1% from 84.71% in 2014. Despite the improvement, the Bank lags behind its peer group with respect to efficiency. According to the Uniform Bank Performance Report, banks within peer group 2 (with total assets between $1.0 and $3.0 billion) had an average efficiency ratio of 63.70% in 2016.

Looking Ahead to 2017

For 2017, management plans to continue to focus on improving efficiency to drive long-term financial performance. With non-interest expense near normal levels, management is also focused on increasing net interest income through commercial and retail loan growth initiatives and developing additional sources of non-interest income.

As part of its responsibilities, management regularly evaluates FNCB's delivery system and facilities including analyzing each office's operating efficiency, location, foot traffic, structure and design. The results of these evaluations may lead to improvements in FNCB's delivery system network and facilities including the remodeling, consolidation and/or relocation of existing facilities and branches and the potential for opening offices and/or branches in new market areas.

On December 21, 2016, the Bank purchased a building located immediately adjacent to its main office in Dunmore, Lackawanna County, Pennsylvania to open a lending center that will house part of its commercial and retail lending units. This lending center is expected to open by the end of the first quarter of 2017. In addition, on January 20, 2017, FNCB opened a loan production office in Allentown, Lehigh County, Pennsylvania and began offering its retail and commercial lending products in this new market area.

Summary of Performance

Net Interest Income

2016 compared to 2015

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

Tax-equivalent net interest income in 2016 improved $3.2 million to $31.3 million compared to $28.1 million in 2015. The 11.2% increase in tax-equivalent net interest income primarily reflected a $2.5 million increase in tax-equivalent interest income, coupled with a $0.6 million reduction in interest expense. Tax-equivalent interest income was positively impacted by an increase in average earning assets, coupled with a slight increase in the yield earned on loans and investment securities. The decrease in interest expense largely reflected a full year of the modification of the interest rate of the Notes from 9.0% to 4.5% during 2015, which had a positive effect on funding costs. In addition, FNCB’s cost of funds was also favorably impacted by a reduction in the rate paid on other time deposits, as higher-costing certificates of deposit matured and were reinvested at lower rates.

FNCB’s tax-equivalent interest margin improved 14 basis points to 3.13% in 2016 from 2.99% in 2015. Tax-equivalent net interest margin, a key measurement used in the banking industry to measure income from earning assets relative to the cost to fund those assets, is calculated by dividing tax-equivalent net interest income by average interest-earning assets. Rate spread, the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities shown on a fully tax-equivalent basis, was 3.05% for the year ended December 31, 2016, an increase of 16 basis points compared to 2.89% for the year ended December 31, 2015.

Tax-equivalent interest income increased $2.5 million, or 7.7%, to $35.5 million in 2016 from $32.9 million in 2015. The growth in tax-equivalent interest income reflected strong growth in interest-earning assets, as average loans increased $35.0 million, or 5.0%, resulting in an increase to tax-equivalent interest income of $1.4 million, and average investments increased $34.4 million or 15.1%, resulting in an increase to tax-equivalent interest income of $0.8 million. Accompanying the growth in average earning assets was a 5-basis point improvement in the tax-equivalent yield on average earning assets to 3.55% in 2016 from 3.50% in 2015. Specifically, the tax-equivalent yield earned on the loan portfolio increased 2 basis points, while the tax-equivalent yield earned on the investment portfolio increased 5 basis points, each of which contributed $0.2 million to the improvement in tax-equivalent interest income. The tax-equivalent yield earned on interest-bearing deposits in other banks improved 22 basis points, reflecting the 25-basis point increase in the federal funds target rate in December, 2015. However, the increase was more than offset by a decrease in the average balance of interest-bearing deposits in other banks of $11.0 million, or 60.8%.

Interest expense decreased $0.6 million, or 12.6%, to $4.2 million in 2016 from $4.8 million in 2015. The decrease in interest expense was driven almost entirely by an 11 basis point decrease in the cost of funds to 0.50% in 2016 compared to 0.61% in 2015, which resulted in a $0.6 million corresponding decrease in interest expense due to changes in rates. Specifically, the modification of the interest rate on the subordinated debentures from 9.0% to 4.5% effective July 1, 2015 had the greatest impact on interest expense, as it was the leading factor driving a 59 basis point decrease in the cost of borrowed funds to 1.42% in 2016 from 2.01% in 2015. The decrease in borrowing costs resulted in a $0.6 million reduction in interest expense. Partially offsetting the decrease in borrowing costs was a slight increase in FNCB’s cost of interest-bearing demand deposits, savings deposits and time deposits over $100,000 of 3 basis points, 3 basis points, and 2 basis points, respectively, all of which more than offset a 12 basis point decrease in the cost of other time deposits. Changes in the average deposit rates resulted in a $34 thousand increase in interest expense.

Average interest-bearing liabilities increased $61.8 million, or 7.9%, to $844.3 million in 2016 from $782.5 million in 2015. Despite the increase, changes in the volumes of interest-bearing liabilities resulted in a $34 thousand decrease in interest expense, as a reduction in average borrowed funds more than offset an increase in average interest-bearing deposits. Specifically, a $4.7 million, or 4.4%, decrease in average borrowed funds, resulted in a reduction to interest expense of $99 thousand. The decline in interest expense paid on borrowed funds was partially offset by a $65 thousand increase in interest expenses resulting from a $66.5 million increase in average interest-bearing deposits. An increase in municipal deposits was the primary factor contributing to an increase of $76.7 million, or 21.4%, in average interest-bearing demand deposits, which led to an increase in interest expense of $158 thousand. In addition, other time deposits increased $2.7 million, or 2.2%, which caused a corresponding increase in interest expense of $27 thousand. Partially offsetting these increases was a decrease in the average balance of time deposits over $100,000 of $18.5 million, or 18.9%, which resulted in a $124 thousand reduction in interest expense.

2015 compared to 2014

Comparing the years ended December 31, 2015 and 2014, tax-equivalent net interest income was stable, decreasing only $40 thousand, or 0.1%. FNCB's tax-equivalent net interest margin contracted 9 basis points to 2.99% in 2015 from 3.08% in 2014, while the rate spread decreased 6 basis points to 2.89% in 2015 compared to 2.95% in 2014. FNCB's net interest margin and rate spread were impacted by several strategic tax planning and Asset/Liability Management Committee ("ALCO") initiatives in 2015, as well as an ongoing challenging rate environment and competitive pressures that continued to impact loan pricing.

In 2015, management continued tax planning strategies designed to generate taxable income and reduce the amount of credit and concentration risk within the investment portfolio. Accordingly, management continued repositioning the investment portfolio by selling the majority of its tax-exempt obligations of state and political subdivisions and replacing them with taxable obligations of U.S. government and government-sponsored agencies including collateralized mortgage obligations ("CMOs"), residential mortgage-backed securities and single-maturity bonds. The effect of this repositioning was the primary factor leading to a $1.4 million, or 20.2%, decrease in tax-equivalent interest income generated from the investment portfolio.

Yields on the lending portfolio were forced down, reflecting competitive pressures for commercial loans within our market area, promotions involving lower-yielding short-term residential mortgage products and indirect auto loans, along with a prolonged depressed rate environment, but were more than offset by increased demand for FNCB's loan products.

Tax-equivalent interest income decreased $1.4 million, or 4.0%, to $32.9 million in 2015 from $34.3 million in 2014. Tax-equivalent interest income was significantly impacted by the repositioning of the investment portfolio from tax-exempt obligations of state and political subdivisions to taxable investments. As a result, the average balance of tax-exempt investments decreased $37.9 million, or 94.0%, which caused a $2.6 million corresponding decrease to tax-equivalent interest income. The average balance of taxable investments increased $45.1 million, or 25.0%, but was only able to mitigate the decrease by $1.1 million. The tax-equivalent yield on the investment portfolio decreased 71 basis points from 3.15% in 2014 to 2.44% in 2015. However, a 12 basis point increase in the yield on taxable investment securities more than offset the effects of a 25 basis point decrease in the yield on tax-exempt investment securities. Overall, changes in the volumes and rates on the investment portfolio resulted in a $1.4 million decrease in tax-equivalent interest income in 2015. Strong loan demand during 2015 resulted in a $30.3 million, or 4.5% increase in average total loans, resulting in additional tax-equivalent interest income of $1.2 million. However, the additional interest income was entirely offset by a 17 basis point decline in the tax-equivalent yield on the loan portfolio due to the factors described above, which caused a corresponding decrease in tax-equivalent interest income of $1.2 million.

However, the effects of the securities portfolio repositioning and declining loan yields were almost entirely mitigated by a $1.3 million, or 21.9%, reduction in interest expense, driven primarily by a 19 basis point decrease in the cost of funds, which resulted in a $1.4 million corresponding decrease in interest expense due to changes in rates. Specifically, the modification of the interest rate on the subordinated debentures from 9.0% to 4.5% had the greatest impact on interest expense, as it was the leading factor driving a 116 basis point decrease in the cost of borrowed funds, resulting in a $1.2 million reduction in interest expense. In addition, the cost of deposits decreased 8 basis points, which resulted from decreases in the cost of time deposits over $100,000 and other time, partially offset by an increase in the average rate paid for interest-bearing demand deposits. Changes in the average deposit rates resulted in a $0.2 million decrease in interest expense.

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

Non-accrual loans

The interest income that would have been earned on non-accrual and restructured loans outstanding at December 31, 2016, 2015 and 2014 in accordance with their original terms approximated $221 thousand, $406 thousand and $406 thousand, respectively. Interest income on impaired loans of $202 thousand, $258 thousand, and $235 thousand was recognized based on payments received in 2016, 2015 and 2014, respectively.

The following table presents the components of net interest income for each of the three years ended December 31, 2016, 2015 and 2014:

Summary of Net Interest Income

	Year ended December 31, 2016			**Year ended December 31, 2015**			**Year ended December 31, 2014**		
(dollars in thousands)	**Average Balance**	**Interest**	**Yield/ Cost**	**Average Balance**	**Interest**	**Yield/ Cost**	**Average Balance**	**Interest**	**Yield/ Cost**
ASSETS									
Earning assets (2)(3)									
Loans-taxable (4)	$685,289	$26,853	3.92 %	$654,470	$25,360	3.87 %	$625,969	$25,316	4.04 %
Loans-tax free (4)	46,305	2,076	4.48 %	42,135	1,988	4.72 %	40,370	1,989	4.93 %
Total loans (1)(2)	731,594	28,929	3.95 %	696,605	27,348	3.93 %	666,339	27,305	4.10 %
Securities-taxable	260,624	6,446	2.47 %	224,955	5,374	2.39 %	179,903	4,090	2.27 %
Securities-tax free	1,192	70	5.87 %	2,419	165	6.82 %	40,277	2,853	7.08 %
Total securities (1)(5)	261,816	6,516	2.49 %	227,374	5,539	2.44 %	220,180	6,943	3.15 %
Interest-bearing deposits in other banks	7,089	33	0.47 %	18,076	46	0.25 %	28,729	71	0.25 %
Total earning assets	1,000,499	35,478	3.55 %	942,055	32,933	3.50 %	915,248	34,319	3.75 %
Non-earning assets	107,061			73,587			73,713		
Allowance for loan and lease losses	(8,684)			(10,729)			(13,094)		
Total assets	$1,098,876			$1,004,913			$975,867		
LIABILITIES AND SHAREHOLDERS' EQUITY									
Interest-bearing liabilities									
Interest-bearing demand deposits	$435,092	973	0.22 %	$358,442	672	0.19 %	$320,780	453	0.14 %
Savings deposits	97,188	94	0.10 %	91,603	60	0.07 %	88,678	57	0.06 %
Time deposits over $100,000	79,193	573	0.72 %	97,687	679	0.70 %	135,871	1,048	0.77 %
Other time deposits	129,590	1,090	0.84 %	126,851	1,220	0.96 %	132,489	1,622	1.22 %
Total interest-bearing deposits	741,063	2,730	0.37 %	674,583	2,631	0.39 %	677,818	3,180	0.47 %
Borrowed funds and other interest-bearing	103,239	1,467	1.42 %	107,965	2,170	2.01 %	93,694	2,967	3.17 %

liabilities									
Total interest-bearing liabilities	844,302	4,197	0.50 %	782,548	4,801	0.61 %	771,512	6,147	0.80 %
Demand deposits	148,746			139,945			134,132		
Other liabilities	13,263			25,744			24,724		
Shareholders' equity	92,565			56,676			45,499		
Total liabilities and shareholders' equity	$1,098,876			$1,004,913			$975,867		
Net interest income/interest rate apread (6)		31,281	3.05 %		28,132	2.89 %		28,172	2.95 %
Tax equivalent adjustment		(730)			(732)			(1,646)	
Net interest income as reported		$30,551			$27,400			$26,526	
Net interest margin (7)			3.13 %			2.99 %			3.08 %

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

Rate Volume Analysis

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

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

	For the Year Ended December 31, 2016 vs. 2015 Increase (Decrease) Due to Change in			For the Year Ended December 31, 2015 vs. 2014 Increase (Decrease) Due to Change in		
(in thousands)	**Volume**	**Rate**	**Total**	**Volume**	**Rate**	**Total**
Interest Income:						
Loans - taxable	$1,205	$288	$1,493	$1,128	$(1,084)	$44
Loans - tax free	190	(102)	88	85	(86)	(1)
Total loans	1,395	186	1,581	1,213	(1,170)	43
Securities - taxable	877	195	1,072	1,067	217	1,284
Securities - tax free	(74)	(21)	(95)	(2,586)	(102)	(2,688)
Total securities	803	174	977	(1,519)	115	(1,404)
Interest-bearing deposits in other banks	(38)	25	(13)	(27)	2	(25)
Total interest income	2,160	385	2,545	(333)	(1,053)	(1,386)
Interest Expense:						
Interest-bearing demand deposits	158	143	301	58	161	219
Savings deposits	4	30	34	2	1	3
Time deposits over $100,000	(124)	18	(106)	(316)	(53)	(369)
Other time deposits	27	(157)	(130)	(67)	(335)	(402)
Total interest-bearing deposits	65	34	99	(323)	(226)	(549)
Borrowed funds and other interest-bearing liabilities	(99)	(604)	(703)	403	(1,200)	(797)
Total interest expense	(34)	(570)	(604)	80	(1,426)	(1,346)
Net Interest Income	$2,194	$955	$3,149	$(413)	$373	$(40)

Provision for Loan and Lease Losses

Management closely monitors the loan portfolio and the adequacy of the ALLL by considering the underlying financial performance of the borrower, collateral values and associated credit risks. Future material adjustments may be necessary to the provision for loan and lease losses and the ALLL if economic conditions or loan performance differ substantially from the assumptions management considered in its evaluation of the ALLL. The provision for loan and lease losses is an expense charged against net interest income to provide for probable losses attributable to uncollectible loans and is based on management’s analysis of the adequacy of the ALLL. A credit to loan and lease losses reflects the reversal of amounts previously charged to the ALLL.

2016 compared to 2015

For the year ended December 31, 2016, FNCB recorded a provision for loan and lease losses of $1.2 million compared to a credit for loan and lease losses of $1.3 million for the year ended December 31, 2015. The provision for loan and lease losses in 2016 was due largely to net charge-offs of $1.5 million during 2016. Net charge-offs within the commercial real estate, commercial and industrial and consumer segments were the most elevated, totaling $0.4 million, $0.6 million, and $0.4 million, respectively.

2015 compared to 2014

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

The credit for loan and losses during 2014 was primarily attributable to the receipt of a substantial legal settlement in the amount of $5.8 million resulting from judgments filed by FNCB pursuant to a large credit relationship. Of the total amount received, $3.6 million represented full recovery of previously charged-off loans, which was the primary factor leading to the credit for loan and lease losses.

Non-Interest Income:

The following table presents the components of non-interest income for the years ended December 31, 2016, 2015 and 2014:

Components of Non-Interest Income

	Year Ended December 31,		
(in thousands)	**2016**	**2015**	**2014**
Deposit service charges	$2,892	$2,960	$2,975
Net gain on the sale of securities	960	2,296	6,640
Net gain on the sale of mortgage loans held for sale	340	292	292
Net gain on the sale of SBA guaranteed loans	51	-	-
Net loss on the sale of education loans	-	-	(13)
Net gain on the sale of other real estate owned	49	162	209
Gain on branch divestitures	-	-	607
Loan-related fees	439	442	440
Income from bank-owned life insurance	552	564	650
Legal settlements	-	184	2,127
Other	920	900	993
Total non-interest income	$6,203	$7,800	$14,920

2016 compared to 2015

For the year ended December 31, 2016, non-interest income decreased $1.6 million, or 20.5%, to $6.2 million compared to $7.8 million for the same period of 2015. Non-interest income levels in 2016 were largely impacted by a reduction in net gains on the sale of securities of $1.3 million, or 58.2%, from $2.3 million during 2015 to $1.0 million during 2016. In addition, FNCB received non-recurring income from legal settlements of $0.2 million in 2015.

Also affecting non-interest income were reductions in net gains on the sale of OREO and deposit services charges, which were partially mitigated by increases in gains from loan sales. The sale of OREO properties generated net gains of $49 thousand in 2016, a decrease of $113 thousand, or 69.8%, from $162 thousand in 2015. Deposit service charges also declined slightly by $68 thousand, or 2.3%. Partially offsetting these decreases was an increase in net gains on the sale of mortgage loans held for sale of $48 thousand, or 16.4%, from $292 thousand in 2015 to $340 thousand in 2016. Also during 2016, FNCB realized a net gain of $51 thousand on the sale of the guaranteed principal balance of three loans that were guaranteed by the Small Business Administration (“SBA”). Loan-related fees, income from bank-owned life insurance policies, and other income remained steady comparing 2016 and 2015.

2015 compared to 2014

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

The sale of OREO properties generated net gains of $162 thousand in 2015, a decrease of $47 thousand, or 22.5%, from $209 thousand in 2014. Deposit service charges, loan-related fees and net gains on the sale of mortgage loans held for sale all were relatively flat comparing 2015 and 2014. Income from bank-owned life insurance policies and other income decreased $86 thousand and $93 thousand, respectively, in 2015 as compared to 2014.

Non-Interest Expense

The following table presents the major components of non-interest expense for the years ended December 31, 2016, 2015 and 2014:

Components of Non-Interest Expense

	Year Ended December 31,		
(in thousands)	**2016**	**2015**	**2014**
Salaries and employee benefits	$14,320	$13,810	$13,111
Occupancy expense	1,777	2,284	2,088
Equipment expense	1,732	1,657	1,471
Advertising expense	554	483	470
Data processing expense	1,997	1,976	2,088
Regulatory assessments	729	950	1,801
Bank shares tax	836	705	522
Expense of other real estate	409	400	2,569
Legal expense	362	437	1,799
Professional fees	961	1,014	1,567
Insurance expense	516	659	951
Legal settlements	-	777	-
Other losses	277	281	2,279
Other operating expenses	3,075	3,031	2,853
Total non-interest expense	$27,545	$28,464	$33,569

2016 compared to 2015

Non-interest expense levels continued to improve during 2016. Non-interest expense totaled $27.5 million in 2016, a decrease of $0.9 million, or 3.2%, from $28.5 million in 2015. The decrease resulted primarily from reductions in legal settlements, occupancy expense, regulatory assessments, insurance expenses, legal expenses, and professional fees. Partially offsetting these decreases were increases in salaries and employee benefits, bank shares tax, equipment expense and advertising expenses.

Long-term facilities planning and the relocation of one of the Bank's corporate offices contributed to occupancy expense reductions of $0.5 million, or 22.2%, to $1.8 million in 2016 as compared to $2.3 million in 2015. Specifically, FNCB experienced decreases in rent expense, maintenance expenses, snow removal costs, and utilities expenses.

Included in regulatory assessments expense are FDIC insurance assessments and semi-annual assessments imposed by the Bank's primary regulator. FNCB experienced a $0.2 million, or 23.3%, reduction in regulatory assessment expense comparing 2016 and 2015. The decrease largely reflected the Bank's conversion from a national charter to a state charter and continued improvement in the Bank's risk profile. The change in charter resulted in a reduction in semi-annual regulatory assessments of $150 thousand, or 53.4%, to $131 thousand in 2016 from $281 thousand in 2015. In addition, during the second quarter of 2015, FNCB was notified by the FDIC that the Bank's risk category for FDIC assessments had improved to a risk category I, the lowest risk category from risk category II based upon the results of its most recent regulatory examination. The change in risk categories became effective on February 1, 2015, and as a result the Bank's initial base assessment rate for deposit insurance decreased from 0.14 basis points to a range of 0.05 – 0.09 basis points. FNCB was able to realize a full-year of lower assessment rates in 2016, which resulted in a $71 thousand, or 10.6%, reduction in FDIC assessments comparing 2016 and 2015. Moreover, FNCB's improved risk profile contributed to a $0.1 million, or 21.7%, reduction in insurance expenses.

Legal and professional fee expenses continued to decline throughout 2016 as outstanding litigation was resolved and reliance on outside consulting firms declined. Legal expenses declined $75 thousand, or 17.2%, as compared to 2015, while professional fees decreased $53 thousand, or 5.2%.

FNCB experienced an increase in salaries and employee benefit costs of $0.5 million, or 3.7%, to $14.3 million in 2016 as compared to $13.8 million in 2015. Despite a reduction in the number of full-time equivalent employees to 236 at December 31, 2016 from 250 at December 31, 2015, total salary expense increased $245 thousand, or 2.1%, due to annual merit increases and severance-related costs. Payroll taxes and employee benefits increased $265 thousand, or 11.1%, which largely reflected higher health insurance premiums and an increase in the state unemployment compensation rate.

On October 1, 2015, the Bank executed a Supplemental Executive Retirement Plan (“SERP”) for a select group of management or highly compensated employees within the meaning of Sections 201(2), 301(a)(3) and 401(a)(1) of The Employee Retirement Income Security Act of 1974. The general provisions of the SERP provide for annual year-end contributions, performance contingent contributions and discretionary contributions. The SERP contributions are unfunded for federal tax purposes and constitute an unsecured promise by the Bank to pay benefits in the future. Participants in the SERP shall have the status of general unsecured creditors of the Bank. Annual accrued unfunded contributions included in salaries and employee benefits expense totaled $147 thousand in 2016 and $130 thousand in 2015.

2015 compared to 2014

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

Expenses of other real estate owned amounted to $400 thousand in 2015, a decrease of $2.2 million from $2.6 million in 2014. Valuation adjustments to the values of OREO properties decreased $2.0 million comparing 2016 and 2015, which was the primary factor leading to the decrease in OREO-related expenses.

As mentioned above, the Bank’s risk category for FDIC insurance assessments improved to risk category I, the lowest category, effective February 1, 2015. The change in assessment rate contributed to a decrease in regulatory assessments of $851 thousand, or 47.3%, to $1.0 million in 2015 from $1.8 million in 2014.

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

Due to its improved risk profile, in mid-2016, FNCB was able to renew its professional liability, fidelity bond and errors and omissions insurance policies at lower rates. As a result, insurance expense decreased $292 thousand, or 30.7%, to $0.7 million in 2015 from $1.0 million in 2014.

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

Salaries and employee benefits expense increased $699 thousand, or 5.3%, to $13.8 million in 2015 from $13.1 million in 2014. Total salary expense increased $540 thousand, or 5.0%, due to increases in stock-based compensation and employee incentive compensation. Payroll taxes and employee benefits increased $158 thousand, or 7.1%, which was due primarily due to increases in state unemployment taxes and costs associated with the establishment of SERP of $130 thousand in 2015. There were no SERP-related expenses in 2014. At December 31, 2015, the number of full-time equivalent employees was 250 as compared to 237 at December 31, 2014.

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

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

Provision for Income Taxes

FNCB recorded income tax expense of $1.7 million in 2016, as compared to an income tax benefit of $27.8 million in 2015. The income tax benefit recorded in 2015 resulted primarily from the reversal of the valuation allowance for FNCB's deferred tax assets. FNCB recorded income tax expense of $0.3 million in 2014, which was related entirely to alternative minimum tax.

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

In evaluating available evidence, management considers, among other factors, historical financial performance, expectation of future earnings, the ability to carry back losses to recoup taxes previously paid, length of statutory carry forward periods, experience with operating loss and tax credit carry forwards not expiring unused, tax planning strategies and timing of reversals of temporary differences. In assessing the need for a valuation allowance, management carefully weighs both positive and negative evidence currently available. Based on the analysis of all available positive and negative evidence, management determined that negative evidence existed at December 31, 2014 that outweighed any positive evidence that existed at that time. Accordingly, management had established a valuation allowance equal to 100.0% of net deferred tax assets, excluding deferred tax assets or liabilities related to unrealized holding gains and losses on available-for-sale securities.

Management performed an evaluation of FNCB's deferred tax assets at December 31, 2015 and determined that based on its consistent methodology the negative evidence that was present at December 31, 2014 no longer existed. FNCB's core earnings had normalized and it was now in a cumulative three-year income position, which management deemed to be positive evidence. In addition, management believed that FNCB's projected future earnings were sufficient to be able to utilize its available net operating loss (NOL) carryforwards prior to their expiration.

This analysis supported the reversal of the valuation allowance established for deferred tax assets at December 31, 2015 except for the valuation allowance established for charitable contribution carryforwards. At December 31, 2015, FNCB had $1.0 million in contribution carryforwards available. Unlike the expiration period for net operating loss carryforwards (generally 20 years) and AMT Credit carryovers (indefinite), the expiration of an excess charitable contribution carryover occurs after the 5th succeeding tax year for which a charitable contribution is made. Management did not believe that enough positive evidence existed to support the utilization of charitable contribution carryforwards in entirety before expiration at December 31, 2015. Accordingly, management believed a valuation allowance in the amount of $355 thousand was appropriate strictly in the case of the excess charitable contribution carryover deferred tax asset at December 31, 2015.

At December 31, 2016, management performed an evaluation of FNCB's deferred tax assets taking into consideration both positive and negative evidence that existed as of that date. In addition, management assessed the continued need for a valuation allowance related to its contribution carryovers. Management anticipates that, based on its current tax provision, FNCB will have generated enough taxable income in 2016 to utilize $353 thousand of the $1.0 million in available charitable contribution carryforwards. At December 31, 2016, management believes that FNCB will be able to generate future taxable income sufficient to utilize its deferred tax assets including the remaining contribution carryforwards in full prior to their expiration in 2020. In addition, management believes that future taxable income will be sufficient to utilize deferred tax assets. FNCB's core earnings in 2016 were strong and its projected future core earnings will continue to support the recognition of the deferred tax assets based on future growth projections. Accordingly, management concluded that no valuation allowance was required at December 31, 2016.

FNCB uses the current statutory tax rate of 34.0% to value its deferred tax assets and liabilities. The Trump Administration and the U.S. Congress are in the process of evaluating possible tax changes which may include a reduction in the U.S. corporate income tax rates. There is no specific proposal currently pending. If corporate tax rates were reduced, management expects FNCB would be required to record an initial charge against earnings to lower the carrying amount of its net deferred tax asset, and then, going forward, would record lower tax provisions on an ongoing basis. There is no specific proposal currently pending. Management cannot assess the effect a change in the corporate tax rate would have on FNCB's operating results or financial position at the present time.

FINANCIAL CONDITION

Total assets were $1.2 billion at December 31, 2016, an increase of $104.8 million, or 9.6%, from $1.1 billion, at December 31, 2015. The balance sheet growth reflected an increase in total deposits of $193.6 million, or 23.6%, to $1.0 billion at December 31, 2016 from $0.8 billion at the end of 2015. The deposit growth was primarily used to pay down FHLB advances of $77.3 million, and fund an increase in available-for-sale securities of $18.9 million. In addition, as previously mentioned, FNCB repaid all previously deferred accrued interest on the Notes in the amount of $10.8 million, as well as accelerated a $4.0 million principal payment due on the Notes September 1, 2017 to December 1, 2016.

FNCB's capital position improved during 2016, demonstrated by an increase in total shareholders' equity of $4.0 million, or 4.6%. Net income of $6.3 million, partially offset by dividends declared in 2016 of $1.5 million and a $1.5 million increase in the accumulated other comprehensive loss due to depreciation in the fair value of FNCB's available-for-sale securities portfolio, accounted for the majority of the capital improvement. Dividends declared and paid by FNCB on its common shares totaled $0.09 per share during 2016, which represented 23.6% of net income. On January 25, 2017, the Board of Directors of FNCB declared a $0.03 per share dividend for the first quarter of 2017, payable on March 15, 2017 to shareholders of record on March 1, 2017.

Securities

FNCB's investment securities portfolio provides a source of liquidity needed to meet expected loan demand and interest income to increase profitability. Additionally, the investment securities portfolio is used to meet pledging requirements to secure public deposits and for other purposes. Management classifies investment securities as either held-to-maturity or available-for-sale at the time of purchase based on its intent. Held-to-maturity securities are carried at amortized cost, while available-for-sale securities are carried at fair value, with unrealized holding gains and losses reported as a component of shareholders' equity in accumulated other comprehensive income (loss), net of tax. At December 31, 2016 and 2015, all securities were classified as available-for-sale. Decisions to purchase or sell investment securities are based upon management's current assessment of long- and short-term economic and financial conditions, including the interest rate environment and asset/liability management and tax planning strategies. Securities with limited marketability and/or restrictions, such as FHLB of Pittsburgh stock, are carried at cost.

At December 31, 2016, FNCB's investment portfolio was comprised principally of fixed-rate securities issued by U.S. government or U.S. government-sponsored agencies, which include residential 1-4 family and multi-family mortgage-backed securities, residential and commercial CMOs and single-maturity bonds, and fixed-rate taxable obligations of state and political subdivisions. Except for U.S. government and government-sponsored agencies, there were no securities of any individual issuer that exceeded 10.0% of shareholders' equity as of December 31, 2016.

Because of the predominantly fixed-rate nature of the portfolio, FNCB's debt securities are inherently subject to interest rate risk, defined as the risk that an investment's value will change due to a change in interest rates, in the spread between two rates and in the shape of the yield curve. A security's value is usually affected inversely by changes in rates. U.S. Treasury rates, which fell to near-historical lows mid-2016 following the United Kingdom's referendum to exit the European Union, rebounded after the U.S. presidential election due to expectations of a more expansionary fiscal policy. The 2-year treasury rate, which was 1.06% at December 31, 2015, fell 48 basis points to 0.58% at June 30, 2016 and then rose 61 basis points to 1.19% at December 31, 2016. Similarly, the 10-year treasury rate, which decreased 71 basis points from 2.18% at December 31, 2015 to 1.47% at June 30, 2016, rebounded 98 basis points to 2.45% at December 31, 2016. The change in interest rates resulted in an aggregate $2.3 million decrease in the fair value of FNCB's available-for-sale securities portfolio. FNCB reported a net unrealized holding loss of $1.8 million, net of income taxes of $796 thousand, at December 31, 2016, compared to an unrealized holding loss of $238 thousand, net of income taxes of $123 thousand, at December 31, 2015. Any additional increases in interest rates could result in further depreciation in the fair value of FNCB's securities portfolio and capital position.

The following table presents the carrying value of securities, all of which were classified as available-for-sale and carried at fair value at December 31, 2016, 2015 and 2014:

Composition of the Investment Portfolio

	December 31,		
(in thousands)	**2016**	**2015**	**2014**
Available-for-sale			
Obligations of U.S. government agencies	$12,188	$44,043	$29,276
Obligations of state and political subdivisions	117,873	75,407	24,509
U.S. government/government-sponsored agencies:			
Collateralized mortgage obligations - residential	18,084	22,269	26,231
Collateralized mortgage obligations - commercial	99,350	89,423	61,256
Mortgage-backed securities	20,576	18,098	74,098
Corporate debt securities	453	423	420
Negotiable certificates of deposit	3,216	3,162	2,232
Equity securities	936	948	967
Total available-for-sale securities	$272,676	$253,773	$218,989

Management actions with respect to the investment portfolio during 2016 reflected ongoing tax planning strategies which focused on the generation of taxable income in order to utilize $50.4 million in available NOL carryforwards. In addition, management's investment strategies in 2016 took into consideration market opportunities that were presented due to changes in market conditions and addressed FNCB's ongoing liquidity needs.

Changing market conditions throughout 2016 allowed management to sell lower-yielding securities of U.S. government agencies and reinvest the proceeds from the sales, as well as normal monthly cash flows from the portfolio, into higher-yielding taxable obligations of state and political subdivisions and multi-family mortgage-backed securities and CMOs of U.S. government/government-sponsored agencies. During 2016, FNCB sold eight of its available-for-sale securities, all of which were single-maturity obligations of U.S. government agencies. The securities sold had an aggregate amortized cost of $31.6 million and a weighted-average yield of 1.90%. Gross proceeds received totaled $32.6 million, with net gains of $1.0 million realized upon the sales and included in non-interest income.

Securities purchased during the year ended December 31, 2016 totaled $60.3 million, including $45.6 million in obligations of state and political subdivisions, $11.5 million in commercial CMOs of U.S. government-sponsored agencies, and $3.2 million of multi-family mortgage-backed securities of U.S. government-sponsored agencies, with weighted-average yields of 2.53%, 2.35% and 2.36%, respectively.

The following table presents the maturities of available-for-sale securities, based on carrying value at December 31, 2016, and the weighted average yields of such securities calculated on the basis of the amortized cost and effective yields weighted for the scheduled maturity of each security. The yields on tax-exempt obligations of states and political subdivisions are presented on a tax-equivalent basis using an effective tax rate of 34.0%. Because residential and commercial collateralized mortgage obligations and residential mortgage-backed securities are not due at a single maturity date, they are not included in the maturity categories in the following summary.

Maturity Distribution of the Investment Portfolio

	December 31, 2016						
(dollars in thousands)	**Within One Year**	**> 1 – 5 Years**	**6-10 Years**	**Over 10 Years**	**Collateralized Mortgage Obligations and Mortgage-Backed Securities**	**No Fixed Maturity**	**Total**
Available-for-sale							

Obligations of U.S. government agencies	$-	$4,743	$7,445	$-	$ -	$ -	$12,188
Yield		2.01 %	2.29 %				2.18 %
Obligations of state and political subdivisions	-	21,939	90,772	5,162	-	-	117,873
Yield		2.43 %	2.73 %	5.00 %			2.77 %
U.S. government/government-sponsored agencies:							
Collateralized mortgage obligations - residential	-	-	-	-	18,084	-	18,084
Yield					2.63 %		2.63 %
Collateralized mortgage obligations - commercial	-	-	-	-	99,350	-	99,350
Yield					2.25 %		2.25 %
Mortgage-backed securities	-	-	-	-	20,576	-	20,576
Yield					2.61 %		2.61 %
Corporate debt securities	-	-	-	453	-	-	453
Yield				1.51 %			1.51 %
Negotiable certificates of deposit	249	2,967	-	-	-	-	3,216
Yield	1.45%	2.09 %					2.04 %
Equity securities	-	-	-	-	-	936	936
Yield						3.46 %	3.46 %
Total securities available-for-sale	$249	$29,649	$98,217	$5,615	$ 138,010	$ 936	$272,676
Weighted yield	1.45%	2.33 %	2.70 %	4.72 %	2.35 %	3.46 %	2.53 %

OTTI Evaluation

There was no OTTI recognized during the years ended December 31, 2016, 2015 and 2014. For additional information regarding management’s evaluation of securities for OTTI, see Note 4, “Securities” of the notes to consolidated financial statements included in Item 8, “Financial Statement and Supplementary Data” to this Annual Report on Form 10-K.

Investments in FHLB of Pittsburgh and Federal Reserve Bank of Philadelphia (“FRB”) stock have limited marketability and are carried at cost. FNCB’s investment in FHLB of Pittsburgh stock totaled $3.3 million and $6.3 million at December 31, 2016 and 2015, respectively. During the year ended December 31, 2016, as part of its conversion to a state charter, the Bank canceled its membership with the FRB, and as a result, the entire balance of FRB stock totaling $1.3 million was redeemed. FRB stock of $1.3 million is included in other assets in the consolidated statements of financial condition at December 31, 2015. Management noted no indicators of impairment for the FHLB of Pittsburgh stock at December 31, 2016.

Loans

FNCB experienced moderate demand for its retail lending products; however, payoffs related to several large commercial lending relationships almost entirely outpaced originations, resulting in a modest $0.6 million, or 0.1%, increase in total loans to $731.8 million at December 31, 2016 from $731.2 million at December 31, 2015. The most prominent growth was exhibited in the residential real estate lending category, which was driven by a $7.5 million, or 21.4%, increase in demand for FNCB's proprietary "WOW" mortgage product, a non-saleable mortgage with maturity terms of 7.5 to 14.5 years. This product offers customers an attractive fixed interest rate, low closing costs and a guaranteed 30-day close.

Historically, commercial lending activities have represented a significant portion of FNCB's loan portfolio. Commercial lending includes commercial and industrial loans, commercial real estate loans and construction, land acquisition and development loans, and represented 56.8% and 58.2% of total loans at December 31, 2016 and December 31, 2015, respectively.

From a collateral standpoint, a majority of FNCB's loan portfolio consists of loans secured by real estate. Real estate secured loans, which include commercial real estate, construction, land acquisition and development, residential real estate loans and home equity lines of credit ("HELOCs"), decreased by $3.6 million, or 0.8%, to $430.1 million at December 31, 2016 from $433.7 million at December 31, 2015. The majority of the decrease was concentrated in the commercial sector, as several large commercial real estate loans were paid off during 2016. Real estate secured loans represented 58.8% of total gross loans at December 31, 2016 and 59.3% at December 31, 2015.

Commercial and industrial loans increased $3.9 million, or 2.6%, during the year to $153.8 million at December 31, 2016 from $149.8 million at December 31, 2015. Commercial and industrial loans consist primarily of equipment loans, working capital financing, automobile floor plans, revolving lines of credit and loans secured by cash and marketable securities. Loans secured by commercial real estate decreased $1.4 million, or 0.6%, to $243.8 million at December 31, 2016 from $245.2 million at December 31, 2015. Commercial real estate loans include long-term commercial mortgage financing and are primarily secured by first or second lien mortgages. Construction, land acquisition and development loans decreased $12.5 million, or 40.5%, during the year to $18.4 million at December 31, 2016, from $30.9 million at December 31, 2015, as several large projects reached completion and converted to permanent financing.

Residential real estate loans totaled $144.3 million at December 31, 2016, an increase of $13.6 million, or 10.4%, from $130.7 million at December 31, 2015. The components of residential real estate loans include fixed-rate and variable-rate mortgage loans. HELOCs are not included in this category but are included in consumer loans. FNCB primarily underwrites fixed-rate purchase and refinance of residential mortgage loans for sale in the secondary market to reduce interest rate risk and provide funding for additional loans. During 2016, management continued a campaign to promote FNCB's "WOW" residential mortgage product. FNCB continued to experience favorable demand in 2016 for its “WOW” mortgages, which increased $7.5 million, or 21.4%, to $42.5 million at December 31, 2016 from $35.0 million at December 31, 2015 and accounted for the majority of the growth in residential real estate loans.

Consumer loans totaled $127.8 million at December 31, 2016, a decrease of $0.7 million, or 0.5%, from $128.5 million at December 31, 2015. Loans to state and municipal governments decreased $2.4 million, or 5.2%, to $43.7 million at December 31, 2016 from $46.1 million at December 31, 2015.

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

Loan Portfolio Detail

(in thousands)	December 31, 2016	2015	2014	2013	2012
Residential real estate	$144,260	$130,696	$122,832	$114,925	$90,228
Commercial real estate	243,830	245,198	233,473	218,524	221,591
Construction, land acquisition and development	18,357	30,843	18,835	24,382	32,502
Commercial and industrial	153,758	149,826	132,057	127,021	109,693
Consumer	127,844	128,533	122,092	118,645	109,783
State and political subdivisions	43,709	46,056	40,205	39,875	33,978
Total loans, gross	731,758	731,152	669,494	643,372	597,775
Unearned income	(48)	(98)	(98)	(143)	(103)
Net deferred loan costs	2,569	2,662	871	668	260
Allowance for loan and lease losses	(8,419)	(8,790)	(11,520)	(14,017)	(18,536)
Loans, net	$725,860	$724,926	$658,747	$629,880	$579,396

The following table presents the maturity distribution and interest rate information of the loan portfolio by major category as of December 31, 2016:

Maturity Distribution of the Loan Portfolio

(in thousands)	December 31, 2016 Within One Year	One to Five Years	Over Five Years	Total
Residential real estate	$1,365	$6,574	$136,321	$144,260
Commercial real estate	27,703	30,171	185,956	243,830
Construction, land acquisition and development	9,111	1,470	7,776	18,357
Commercial and industrial	90,319	42,975	20,464	153,758
Consumer	6,597	71,369	49,878	127,844
State and political subdivisions	4,780	7,868	31,061	43,709
Total	$139,875	$160,427	$431,456	$731,758
Loans with predetermined interest rates	$27,145	$117,412	$171,690	$316,247
Loans with floating rates	112,730	43,015	259,766	415,511
Total	$139,875	$160,427	$431,456	$731,758

Under industry regulations, a concentration is considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities which would cause them to be similarly impacted by economic or other conditions. Typically industry guidelines require disclosure of concentrations of loans exceeding 10.0% of total loans outstanding. FNCB had no such concentrations at December 31, 2016, 2015 and 2014. In addition to industry guidelines, FNCB's internal policy considers a concentration to exist in its loan portfolio if an aggregate loan balance outstanding to borrowers within a specific industry exceeds 25.0% of capital. However, management regularly reviews loans by all industry categories to determine if a potential concentration exists.

The following table presents loans by industry, the percentage to gross loans and indicates concentrations greater than 25.0% of capital at December 31, 2016, 2015 and 2014:

Loan Concentrations	**December 31, 2016**		**2015**		**2014**	
(dollars in thousands)	**Amount**	**% of Gross Loans**	**Amount**	**% of Gross Loans**	**Amount**	**% of Gross Loans**
Retail space/shopping centers*	$38,573	5.27 %	$35,292	4.83 %	$33,140	4.95 %
Automobile dealers*	31,989	4.37 %	34,594	4.73 %	24,194	3.61 %
1-4 family residential investment properties*	24,413	3.34 %	18,957	2.59 %	12,764	1.91 %
Office complexes/units	14,257	1.95 %	18,487	2.53 %	17,249	2.58 %
Physicians	15,058	2.06 %	10,677	1.46 %	13,636	2.04 %
Colleges and Universities	14,021	1.92 %	18,540	2.54 %	16,680	2.49 %
Land subdivision	11,975	1.64 %	12,673	1.73 %	15,220	2.27 %

* Concentration exceeds 25.0% of capital at December 31, 2016