CNB FINANCIAL CORP/PA
Form 10-Q
August 08, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10 - Q

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

For the quarterly period ended June 30, 2013

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 Number 000-13396

CNB FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

Pennsylvania	**25-1450605**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

1 South Second Street

P.O. Box 42

Clearfield, Pennsylvania 16830

(Address of principal executive offices)

Registrant s telephone number, including area code, (814) 765-9621

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. x 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x Yes ¨ No

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

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

The number of shares outstanding of the issuer s common stock as of August 5, 2013

COMMON STOCK NO PAR VALUE PER SHARE: 12,512,244 SHARES

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PART I.

FINANCIAL INFORMATION

PART II.

OTHER INFORMATION

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Forward-Looking Statements

This document contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, with respect to our financial condition, liquidity, results of operations, future performance and business. These forward-looking statements are intended to be covered by the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995. Forward-looking statements are those that are not historical facts. Forward-looking statements include statements with respect to 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). Forward-looking statements often include words such as believes, expects, anticipates, estimates, intends, plans or similar expre or future conditional verbs such as may, will, should, would and could. Such known and unknown risks, uncertainties and other factors that could cause the actual results to differ materially from the statements include, but are not limited to: changes in general business, industry or economic conditions or competition; changes in any applicable law, rule, regulation, policy, guideline or practice governing or affecting financial holding companies and their subsidiaries or with respect to tax or accounting principles or otherwise; adverse changes or conditions in capital and financial markets; changes in interest rates; higher than expected costs or other difficulties related to integration of combined or merged businesses; the inability to realize expected cost savings or achieve other anticipated benefits in connection with business combinations and other acquisitions, including the previously announced acquisition of FC Banc Corp.; changes in the quality or composition of our loan and investment portfolios; adequacy of loan loss reserves; increased competition; loss of certain key officers; continued relationships with major customers; deposit attrition; rapidly changing technology; unanticipated regulatory or judicial proceedings and liabilities and other costs; changes in the cost of funds, demand for loan products or demand for financial services; and other economic, competitive, governmental or technological factors affecting our operations, markets, products, services and prices. Some of these and other factors are discussed in our annual and quarterly reports filed with the Securities and Exchange Commission. Such factors could cause actual results to differ materially from those in the forward-looking statements.

The forward-looking statements are based upon management s beliefs and assumptions and are made as of the date of the filing of this document. We undertake no obligation to publicly update or revise any forward-looking statements included in this document or to update the reasons why actual results could differ from those contained in such statements, whether as a result of new information, future events or otherwise, except to the extent required by law. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this document might not occur and you should not put undue reliance on any forward-looking statements.

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Part I Financial Information

Item 1. Financial Statements

CONSOLIDATED BALANCE SHEETS

Dollars in thousands, except share data

	(unaudited) June 30, 2013	December 31, 2012
ASSETS		
Cash and due from banks	$ 20,773	$ 28,570
Interest bearing deposits with other banks	4,021	3,311
Total cash and cash equivalents	24,794	31,881
Interest bearing time deposits with other banks	277	225
Securities available for sale	724,298	737,311
Trading securities	4,729	4,459
Loans held for sale	53	2,398
Loans	986,482	931,225
Less: unearned discount	(3,535)	(3,401)
Less: allowance for loan losses	(15,500)	(14,060)
Net loans	967,447	913,764
FHLB and other equity interests	7,565	6,684
Premises and equipment, net	24,833	24,072
Bank owned life insurance	29,383	27,645
Mortgage servicing rights	696	714
Goodwill	10,946	10,946
Accrued interest receivable and other assets	14,424	12,980
TOTAL	$ 1,809,445	$ 1,773,079
LIABILITIES AND SHAREHOLDERS EQUITY		
Non-interest bearing deposits	$ 176,700	$ 175,239
Interest bearing deposits	1,369,846	1,309,764
Total deposits	1,546,546	1,485,003
FHLB and other borrowings	100,477	97,806
Subordinated debentures	20,620	20,620
Accrued interest payable and other liabilities	10,822	24,286
Total liabilities	1,678,465	1,627,715
Common stock, $0 par value; authorized 50,000,000 shares; issued 12,599,603 shares	0	0
Additional paid in capital	43,950	44,223
Retained earnings	92,080	88,960
Treasury stock, at cost (88,508 shares at June 30, 2013		

and 123,699 shares at December 31, 2012)	(1,222)	(1,743)
Accumulated other comprehensive income (loss)	(3,828)	13,924
Total shareholders equity	130,980	145,364
TOTAL	$ 1,809,445	$ 1,773,079

See Notes to Consolidated Financial Statements

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CONSOLIDATED STATEMENTS OF INCOME (unaudited)

Dollars in thousands, except per share data

	Three months ended June 30, 2013	Three months ended June 30, 2012
INTEREST AND DIVIDEND INCOME:		
Loans including fees	$ 12,281	$ 12,394
Securities:		
Taxable	3,474	3,890
Tax-exempt	965	905
Dividends	38	18
Total interest and dividend income	16,758	17,207
INTEREST EXPENSE:		
Deposits	1,955	2,946
Borrowed funds	779	787
Subordinated debentures (includes $105 and $98 accumulated other comprehensive income reclassification for change in fair value of interest rate swap agreements in 2013 and 2012, respectively)	198	200
Total interest expense	2,932	3,933
NET INTEREST INCOME	13,826	13,274
PROVISION FOR LOAN LOSSES	3,115	1,746
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	10,711	11,528
NON-INTEREST INCOME:		
Wealth and asset management fees	538	426
Service charges on deposit accounts	1,019	996
Other service charges and fees	524	468
Net realized gains on available-for-sale securities (includes $252 and $731 accumulated other comprehensive income reclassifications for net realized gains on available-for-sale securities in 2013 and 2012, respectively)	252	731
Net realized and unrealized gains (losses) on trading securities	28	(140)
Mortgage banking	271	196
Bank owned life insurance	815	262
Other	324	325
Total non-interest income	3,771	3,264
NON-INTEREST EXPENSES:		
Salaries and benefits	5,332	4,619
Net occupancy expense	1,281	1,107
Data processing	1,088	692
State and local taxes	436	365
Legal, professional, and examination fees	502	299
Advertising	246	250
FDIC insurance premiums	319	274
Other	1,589	1,227

Total non-interest expenses	10,793	8,833
INCOME BEFORE INCOME TAXES	3,689	5,959
INCOME TAX EXPENSE (includes $51 and $222 income tax expense from reclassification items in 2013 and 2012, respectively	738	1,623
NET INCOME	$ 2,951	$ 4,336
EARNINGS PER SHARE:		
Basic	$ 0.24	$ 0.35
Diluted	$ 0.24	$ 0.35
DIVIDENDS PER SHARE:		
Cash dividends per share	$ 0.165	$ 0.165

See Notes to Consolidated Financial Statements

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CONSOLIDATED STATEMENTS OF INCOME (unaudited)

Dollars in thousands, except per share data

	Six months ended June 30, 2013	Six months ended June 30, 2012
INTEREST AND DIVIDEND INCOME:		
Loans including fees	$ 24,583	$ 24,649
Federal funds sold		
Securities:		
Taxable	6,883	7,575
Tax-exempt	1,922	1,776
Dividends	74	31
Total interest and dividend income	33,462	34,031
INTEREST EXPENSE:		
Deposits	4,189	6,095
Borrowed funds	1,608	1,584
Subordinated debentures (includes $202 and $192 accumulated other comprehensive income reclassification for change in fair value of interest rate swap agreements in 2013 and 2012, respectively)	388	401
Total interest expense	6,185	8,080
NET INTEREST INCOME	27,277	25,951
PROVISION FOR LOAN LOSSES	4,045	2,850
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	23,232	23,101
NON-INTEREST INCOME:		
Wealth and asset management fees	1,112	813
Service charges on deposit accounts	1,961	1,971
Other service charges and fees	954	900
Net realized gains on available-for-sale securities (includes $328 and $1,297 accumulated other comprehensive income reclassifications for net realized gains on available-for-sale securities in 2013 and 2012, respectively)	328	1,297
Net realized and unrealized gains (losses) on trading securities	331	180
Mortgage banking	526	461
Bank owned life insurance	1,077	523
Other	553	534
Total non-interest income	6,842	6,679
NON-INTEREST EXPENSES:		
Salaries and benefits	10,529	9,344
Net occupancy expense	2,598	2,256
Data processing	1,855	1,418
State and local taxes	875	730
Legal, professional, and examination fees	1,276	528
Advertising	492	500

FDIC insurance premiums	598	533
Other	2,252	2,538
Total non-interest expenses	20,475	17,847
INCOME BEFORE INCOME TAXES	9,599	11,933
INCOME TAX EXPENSE (includes $44 and $387 income tax expense from reclassification items in 2013 and 2012, respectively	2,351	3,250
NET INCOME	$ 7,248	$ 8,683
EARNINGS PER SHARE:		
Basic	$ 0.58	$ 0.70
Diluted	$ 0.58	$ 0.70
DIVIDENDS PER SHARE:		
Cash dividends per share	$ 0.33	$ 0.33

See Notes to Consolidated Financial Statements

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (unaudited)

Dollars in thousands

	Three months ended June 30, 2013	Three months ended June 30, 2012	Six months ended June 30, 2013	Six months ended June 30, 2012
NET INCOME	$ 2,951	$ 4,336	$ 7,248	$ 8,683
Other comprehensive income (loss), net of tax:				
Net change in fair value of interest rate swap agreements designated as cash flow hedges:				
Unrealized gain (loss) on interest rate swaps, net of tax of ($101) and and $107 for the three months ended June 30, 2013 and 2012, and ($95) and $106 for the six months ended June 30, 2013 and 2012	177	(199)	188	(197)
Reclassification adjustment for losses recognized in earnings, net of tax of ($37) and ($34) for the three months ended June 30, 2013 and 2012, and ($71) and ($67) for the six months ended June 30, 2013 and 2012	68	64	131	125
	245	(135)	319	(72)
Net change in unrealized gains on securities available for sale:				
Unrealized gains (losses) on other-than-temporarily impaired securities available for sale:				
Unrealized gains arising during the period, net of tax of ($25) and ($7) for the three months ended June 30, 2013 and 2012, and ($11) and ($7) for the six months ended June 30, 2013 and 2012	47	13	20	13
Unrealized gains (losses) on other securities available for sale:				
Unrealized gains (losses) arising during the period, net of tax of $8,762 and ($2,455) for the three months ended June 30, 2013 and 2012, and $9,627 and ($1,809) for the six months ended June 30, 2013 and 2012	(16,273)	4,560	(17,878)	3,359
Reclassification adjustment for realized gains included in net income, net of tax of $88 and $256 for the three months ended June 30, 2013 and 2012, and $115 and $454 for the six months ended June 30, 2013 and 2012	(164)	(475)	(213)	(843)
	(16,437)	4,085	(18,091)	2,516
Other comprehensive income (loss)	(16,145)	3,963	(17,752)	2,457
COMPREHENSIVE INCOME (LOSS)	$ (13,194)	$ 8,299	$ (10,504)	$ 11,140

See Notes to Consolidated Financial Statements

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CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

Dollars in thousands

	Six months ended June 30, 2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 7,248	$ 8,683
Adjustments to reconcile net income to net cash provided by operations:		
Provision for loan losses	4,045	2,850
Depreciation and amortization of premises and equipment	1,120	1,055
Amortization and accretion of securities premiums and discounts, deferred loan fees and costs, and unearned income	2,117	2,125
Net realized gains on sales of available-for-sale securities	(328)	(1,297)
Net realized and unrealized gains on trading securities	(331)	(180)
Proceeds from sale of trading securities	3,818	1,850
Purchase of trading securities	(3,803)	(2,225)
Gain on sale of loans	(504)	(432)
Net gains on dispositions of premises and equipment and foreclosed assets	(77)	(19)
Proceeds from sale of loans	18,116	15,500
Origination of loans held for sale	(15,392)	(15,200)
Income on bank owned life insurance	(1,077)	(523)
Stock-based compensation expense	186	132
Contribution of treasury stock	60	60
Changes in:		
Accrued interest receivable and other assets	(141)	(1,563)
Accrued interest payable and other liabilities	(3,526)	1,648
NET CASH PROVIDED BY OPERATING ACTIVITIES	11,531	12,464
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net decrease (increase) in interest bearing time deposits with other banks	(52)	(51)
Proceeds from maturities, prepayments and calls of securities	63,596	51,504
Proceeds from sales of securities	33,672	88,617
Purchase of securities	(113,998)	(214,250)
Loan origination and payments, net	(57,734)	(58,599)
Purchase of bank owned life insurance	(2,000)	0
Purchase of FHLB and other equity interests	(881)	(311)
Purchase of premises and equipment	(1,738)	(1,038)
Proceeds from the sale of premises and equipment and foreclosed assets	429	467
NET CASH USED IN INVESTING ACTIVITIES	(78,706)	(133,661)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net change in:		
Checking, money market and savings accounts	75,382	145,689
Certificates of deposit	(13,839)	(44,119)
Proceeds from sale of treasury stock	2	528
Cash dividends paid	(4,128)	(4,102)
Proceeds from long-term borrowings	900	0

Repayment of long-term borrowings	(94)	(79)
Net change in short-term borrowings	1,865	7,805
NET CASH PROVIDED BY FINANCING ACTIVITIES	60,088	105,722
NET DECREASE IN CASH AND CASH EQUIVALENTS	(7,087)	(15,475)
CASH AND CASH EQUIVALENTS, Beginning	31,881	39,703
CASH AND CASH EQUIVALENTS, Ending	$ 24,794	$ 24,228
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest	$ 6,326	$ 8,262
Income taxes	$ 1,862	$ 3,488
SUPPLEMENTAL NONCASH DISCLOSURES:		
Transfers to other real estate owned	$ 204	$ 15
Grant of restricted stock awards from treasury stock	$ 539	$ 419
Contribution of treasury stock	$ 60	$ 60

See Notes to Consolidated Financial Statements

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CNB Financial Corporation

Notes To Consolidated Financial Statements

(Unaudited)

1. BASIS OF PRESENTATION

The accompanying consolidated financial statements have been prepared pursuant to rules and regulations of the Securities and Exchange Commission (SEC) and in compliance with accounting principles generally accepted in the United States of America (GAAP). Because this report is based on an interim period, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted.

In the opinion of management of the registrant, the accompanying consolidated financial statements as of June 30, 2013 and for the three and six month periods ended June 30, 2013 and 2012 include all adjustments, consisting of only normal recurring adjustments, necessary for a fair presentation of the financial condition and the results of operations for the periods presented. The financial performance reported for CNB Financial Corporation (the Corporation) for the three and six month periods ended June 30, 2013 is not necessarily indicative of the results to be expected for the full year. This information should be read in conjunction with the Corporation s Annual Report on Form 10-K for the period ended December 31, 2012 (the 2012 Form 10-K). All dollar amounts are stated in thousands, except share and per share data.

2. ACQUISITION OF FC BANC CORP.

On March 26, 2013, the Corporation announced the signing of a definitive merger agreement to acquire FC Banc Corp. and its subsidiary, The Farmers Citizens Bank (FC Bank), for $30.00 per share in cash and stock, or approximately $40.4 million in the aggregate. FC Bank serves the northern Ohio markets of Bucyrus, Cardington, Fredericktown, Mount Hope and Shiloh, as well as the markets of Worthington and Upper Arlington in the greater Columbus, Ohio area, with 8 branch locations and a mortgage banking business headquartered in Dublin, Ohio. The transaction is expected to close in the fourth quarter of 2013, subject to customary closing conditions, including regulatory approvals and the approval of FC Banc Corp. shareholders.

3. STOCK COMPENSATION

The Corporation has a stock incentive plan for key employees and independent directors. The stock incentive plan, which is administered by a committee of the Board of Directors, provides for aggregate grants of up to 500,000 shares of common stock in the form of nonqualified options or restricted stock. For key employees, the plan vesting is one-fourth of the granted options or restricted stock per year beginning one year after the grant date, with 100% vested on the fourth anniversary of the grant. For independent directors, the vesting schedule is one-third of the granted options per year beginning one year after the grant date, with 100% vested on the third anniversary of the grant.

At June 30, 2013, there was no unrecognized compensation cost related to nonvested stock options granted under this plan and no stock options were granted during the three or six month periods ended June 30, 2013 and 2012. At June 30, 2013 and December 31, 2012, the Corporation had 75,500 stock options that were fully vested and exercisable.

Compensation expense for the restricted stock awards is recognized over the requisite service period noted above based on the fair value of the shares at the date of grant. Nonvested restricted stock awards are recorded as a reduction of additional paid-in-capital in shareholders equity until earned. Compensation expense resulting from these restricted stock awards was $103 and $186 for the three and six months ended June 30, 2013, and $73 and $132 for the three and six months ended June 30, 2012. As of June 30, 2013, there was $888 of total unrecognized compensation cost related to unvested restricted stock awards.

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A summary of changes in nonvested restricted stock awards for the three months ended June 30, 2013 follows:

	Shares	Per Share Weighted Average Grant Date Fair Value
Nonvested at beginning of period	65,400	$ 16.24
Granted	0	0
Vested	0	0
Nonvested at end of period	65,400	$ 16.24

A summary of changes in nonvested restricted stock awards for the six months ended June 30, 2013 follows:

	Shares	Per Share Weighted Average Grant Date Fair Value
Nonvested at beginning of period	49,574	$ 15.37
Granted	31,500	17.10
Vested	(15,674)	15.23
Nonvested at end of period	65,400	$ 16.24

4. FAIR VALUE

Fair Value Measurement

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. A fair value hierarchy has also been established which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following three levels of inputs are used to measure fair value:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a company s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The fair values of most trading securities and securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather relying on the securities relationship to other benchmark quoted securities (Level 2 inputs). The fair value of one corporate bond held by the Corporation has been determined by using Level 3 inputs. The Corporation has engaged a valuation expert to price this security using a proprietary model which incorporates assumptions about certain factors that market participants would use in pricing the securities, including bid/ask spreads and liquidity and credit premiums.

The Corporation s structured pooled trust preferred security is priced using Level 3 inputs. The decline in the level of observable inputs and market activity in this class of investments by the measurement date has been significant and resulted in unreliable external pricing. Broker pricing and bid/ask spreads, when available, vary widely, and the once-active market has become comparatively inactive. The Corporation engaged a third party consultant who has developed a model for pricing this security. Information such as historical and current performance of the underlying collateral, deferral and default rates,

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collateral coverage ratios, break in yield calculations, cash flow projections, liquidity and credit premiums required by a market participant, and financial trend analysis with respect to the individual issuing financial institutions and insurance companies are utilized in determining the security valuation. Due to the current market conditions as well as the limited trading activity of these types of securities, the market value of the Corporation s structured pooled trust preferred security is highly sensitive to assumption changes and market volatility.

The Corporation s derivative instrument is an interest rate swap that is similar to those that trade in liquid markets. As such, significant fair value inputs can generally be verified and do not typically involve significant management judgments (Level 2 inputs).

Assets and liabilities measured at fair value on a recurring basis are as follows at June 30, 2013 and December 31, 2012:

		Fair Value Measurements at June 30, 2013 Using		
Description	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Securities Available For Sale:				
U.S. Treasury	$ 2,016	$ 0	$ 2,016	$ 0
U.S. Government sponsored entities	180,062	0	180,062	0
States and political subdivisions	181,235	0	181,235	0
Residential and multi-family mortgage	271,337	0	271,337	0
Commercial mortgage	983	0	983	0
Corporate notes and bonds	13,374	0	13,374	0
Pooled trust preferred	630	0	0	630
Pooled SBA	73,663	73,663	0	0
Other securities	998	998	0	0
Total Securities Available For Sale	$ 724,298	$ 74,661	$ 649,007	$ 630
Trading Securities:				
Corporate equity securities	$ 3,432	$ 3,432	$ 0	$ 0
Certificates of deposit	354	354	0	0
International mutual funds	273	273	0	0
Large cap growth mutual funds	164	164	0	0
Large cap value mutual funds	106	106	0	0
Real estate investment trust mutual funds	102	102	0	0
Corporate notes and bonds	101	0	101	0
Mid cap mutual funds	68	68	0	0
Small cap mutual funds	56	56	0	0
U.S. Government sponsored entities	54	0	54	0
Mid cap mutual funds	19	19	0	0
Total Trading Securities	$ 4,729	$ 4,574	$ 155	$ 0
Liabilities:				
Interest rate swaps	$ (1,253)	$ 0	$ (1,253)	$ 0

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		Fair Value Measurements at December 31, 2012 Using		
Description	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Securities Available For Sale:				
U.S. Treasury	$ 4,036	$ 0	$ 4,036	$ 0
U.S. Government sponsored entities	163,781	0	163,781	0
States and political subdivisions	181,279	0	181,279	0
Residential and multi-family mortgage	316,822	0	316,822	0
Commercial mortgage	1,304	0	1,304	0
Corporate notes and bonds	15,024	0	13,044	1,980
Pooled trust preferred	600	0	0	600
Pooled SBA	52,927	52,631	296	0
Other securities	1,538	1,538	0	0
Total Securities Available For Sale	$ 737,311	$ 54,169	$ 680,562	$ 2,580
Trading Securities:				
Corporate equity securities	$ 3,117	$ 3,117	$ 0	$ 0
Certificates of deposit	408	408	0	0
International mutual funds	287	287	0	0
Large cap growth mutual funds	157	157	0	0
Money market mutual funds	110	110	0	0
Large cap value mutual funds	104	104	0	0
Corporate notes and bonds	101	0	101	0
Real estate investment trust mutual funds	65	65	0	0
U.S. Government sponsored entities	58	0	58	0
Small cap mutual funds	26	26	0	0
Mid cap mutual funds	26	26	0	0
Total Trading Securities	$ 4,459	$ 4,300	$ 159	$ 0
Liabilities:				
Interest rate swaps	$ (1,745)	$ 0	$ (1,745)	$ 0

The table below presents a reconciliation and income statement classification of gains and losses for all securities available for sale measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended June 30, 2013:

	Corporate notes and bonds	Pooled trust preferred
Balance, April 1, 2013	$ 2,067	$ 558
Total gains or (losses):		
Included in other comprehensive income	(116)	72
Included in realized gains on available-for-sale securities	58	0
Sale of available-for-sale securities	(2,009)	0
Balance, June 30, 2013	$ 0	$ 630

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The table below presents a reconciliation and income statement classification of gains and losses for all securities available for sale measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the six months ended June 30, 2013:

	Corporate notes and bonds	Pooled trust preferred
Balance, January 1, 2013	$ 1,980	$ 600
Total gains or (losses):		
Included in other comprehensive income	(29)	30
Included in realized gains on available-for-sale securities	58	0
Sale of available-for-sale securities	(2,009)	0
Balance, June 30, 2013	$ 0	$ 630

The table below presents a reconciliation and income statement classification of gains and losses for all securities available for sale measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended June 30, 2012:

	Corporate notes and bonds	Pooled trust preferred
Balance, April 1, 2012	$ 2,040	$ 340
Total gains or losses:		
Included in other comprehensive income (unrealized)	31	20
Balance, June 30, 2012	$ 2,071	$ 360

The table below presents a reconciliation and income statement classification of gains and losses for all securities available for sale measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the six months ended June 30, 2012:

	Corporate notes and bonds	Pooled trust preferred
Balance, January 1, 2012	$ 2,060	$ 340
Total gains or losses:		
Included in other comprehensive income (unrealized)	11	20
Balance, June 30, 2012	$ 2,071	$ 360

The following table presents quantitative information about Level 3 fair value measurements at June 30, 2013:

	Fair value	Valuation Technique	Unobservable Inputs	Input Utilized
Pooled trust preferred	$ 630	Discounted cash flow	Collateral default rate	2% in 2013; 1.5% in 2014; 1.0% in 2015; 0.5% in 2016 and thereafter
			Yield	12%

Prepayment speed	7.2% constant prepayment rate in 2013; 2.0% constant prepayment rate in 2014 and thereafter

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The following table presents quantitative information about Level 3 fair value measurements at December 31, 2012:

	Fair value	Valuation Technique	Unobservable Inputs	Input Utilized
Corporate notes and bonds	$ 1,980	Discounted cash flow	Constant prepayment rate	0%
			Probability of default	0%
			Discount rate	9.6%
Pooled trust preferred	$ 600	Discounted cash flow	Collateral default rate	2% annually for 2 years; 0.36% thereafter
			Yield	13%
			Recovery probability	10%, lagged 2 years

At June 30, 2013, the significant unobservable inputs used in the fair value measurement of the Corporation s pooled trust preferred security are collateral default rate, yield, and prepayment speed. At December 31, 2012, the significant unobservable inputs used in the fair value measurement of the Corporation s pooled trust preferred security are collateral default rate, yield, and recovery probability. Significant increases in specific-issuer default assumptions or decreases in specific-issuer recovery assumptions would result in a significantly lower fair value measurement. Conversely, decreases in specific-issuer default assumptions or increases in specific-issuer recovery assumptions would result in a higher fair value measurement.

During the three months ended June 30, 2013 and 2012, the following available for sale securities reported as Level 1 securities as of the beginning of the period were transferred to the Level 2 category:

	2013	2012
U.S. Government sponsored entities	0	$ 26,034
States and political subdivisions	0	3,771
Residential mortgage and asset backed	0	40,473
Total	$ 0	$ 70,278

During the six months ended June 30, 2013 and 2012, the following available for sale securities reported as Level 1 securities as of the beginning of the period were transferred to the Level 2 category:

	2013	2012
U.S. Government sponsored entities	$ 0	$ 2,000
States and political subdivisions	0	4,655
Residential mortgage and asset backed	0	8,577
Total	$ 0	$ 15,232

These securities were transferred from the Level 1 category to the Level 2 category since there were no longer quoted prices for identical assets in active markets that the Corporation had the ability to access. There were no transfers from the Level 2 category to the Level 1 category during the three or six month periods ended June 30, 2013 or 2012. The Corporation s policy for determining when a transfer between the Level 1 and

Level 2 categories has occurred is to monitor and report such transfers as of each quarterly reporting period.

The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals prepared by third-parties. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Management also adjusts appraised values based on the length of time that has passed since the appraisal date and other factors. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

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Assets and liabilities measured at fair value on a non-recurring basis are as follows at June 30, 2013 and December 31, 2012:

		Fair Value Measurements at June 30, 2013 Using		
Description	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Impaired loans:				
Commercial mortgages	$ 9,921	$ 0	$ 0	$ 9,921
Commercial, industrial, and agricultural	1,610	0	0	1,610
Residential real estate	74	0	0	74

		Fair Value Measurements at December 31, 2012 Using		
Description	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Impaired loans:				
Commercial mortgages	$ 8,422	$ 0	$ 0	$ 8,422
Commercial, industrial, and agricultural	1,973	0	0	1,973
Residential real estate	402	0	0	402

Impaired loans, which are measured for impairment using the fair value of collateral for collateral dependent loans, had a recorded investment of $14,306 with a valuation allowance of $2,701 as of June 30, 2013, resulting in an additional provision for loan losses of $2,328 and $2,529 for the corresponding three and six months ended June 30, 2013. Impaired loans had a recorded investment of $12,535 with a valuation allowance of $1,738 as of December 31, 2012, and an additional provision for loan losses of $345 and $263 was recorded for the three and six months ended June 30, 2012.

The estimated fair values of impaired collateral dependent loans such as commercial or residential mortgages are determined primarily through third-party appraisals. When a collateral dependent loan, such as a commercial or residential mortgage loan, becomes impaired, a decision is made regarding whether an updated certified appraisal of the real estate is necessary. This decision is based on various considerations, including the age of the most recent appraisal, the loan-to-value ratio based on the original appraisal, and the condition of the property. Appraised values are discounted to arrive at the estimated selling price of the collateral and a further reduction for estimated costs to sell the property is applied, which results in an amount that is considered to be the estimated fair value. If a loan becomes impaired and the appraisal of related loan collateral is outdated, management applies an appropriate adjustment factor based on its experience with current valuations of similar collateral in determining the loan s estimated fair value and resulting allowance for loan losses. Third-party appraisals are not customarily obtained in respect of unimpaired loans, unless in management s view changes in circumstances warrant obtaining an updated appraisal.

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The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at June 30, 2013:

		Fair value	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
Impaired loans	commercial mortgages	$ 9,921	Sales comparison approach	Adjustment for differences between the comparable sales	9% - 10% (9%)
Impaired loans agricultural	commercial, industrial, and	1,610	Income approach	Adjustment for differences in net operating income	13% - 32% (23%)
Impaired loans	residential real estate	74	Sales comparison approach	Adjustment for differences between the comparable sales	17% - 26% (23%)

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at December 31, 2012:

		Fair value	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
Impaired loans	commercial mortgages	$ 8,422	Sales comparison approach	Adjustment for differences between the comparable sales	1% - 39% (19%)
Impaired loans agricultural	commercial, industrial, and	1,973	Income approach	Adjusting for differences in net operating income	24% - 38% (27%)
Impaired loans	residential real estate	402	Sales comparison approach	Adjustment for differences between the comparable sales	10% - 15% (11%)

Fair Value of Financial Instruments

The following table presents the carrying amount and fair value of financial instruments at June 30, 2013:

	Carrying Amount	Fair Value Measurement Using: Level 1	Level 2	Level 3	Total Fair Value
ASSETS					
Cash and cash equivalents	$ 24,794	$ 24,794	$ 0	$ 0	$ 24,794
Interest bearing time deposits with other banks	277	0	283	0	283
Securities available for sale	724,298	74,661	649,007	630	724,298
Trading securities	4,729	4,574	155	0	4,729
Loans held for sale	53	0	54	0	54
Net loans	967,447	0	0	949,183	949,183
FHLB and other equity interests	7,565	n/a	n/a	n/a	n/a
Accrued interest receivable	7,082	402	3,493	3,187	7,082
LIABILITIES					
Deposits	$ (1,546,546)	$ (1,347,442)	$ (198,971)	$ 0	$ (1,546,413)
FHLB and other borrowings	(100,477)	0	(99,872)	0	(99,872)
Subordinated debentures	(20,620)	0	(10,998)	0	(10,998)
Interest rate swaps	(1,253)	0	(1,253)	0	(1,253)
Accrued interest payable	(882)	(223)	(645)	(14)	(882)

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The following table presents the carrying amount and fair value of financial instruments at December 31, 2012:

	Carrying Amount	Fair Value Measurement Using: Level 1	Level 2	Level 3	Total Fair Value
ASSETS					
Cash and cash equivalents	$ 31,881	$ 31,881	$ 0	$ 0	$ 31,881
Interest bearing time deposits with other banks	225	0	230	0	230
Securities available for sale	737,311	54,169	680,562	2,580	737,311
Trading securities	4,459	4,300	159	0	4,459
Loans held for sale	2,398	0	2,460	0	2,460
Net loans	913,764	0	0	917,785	917,785
FHLB and other equity interests	6,684	n/a	n/a	n/a	n/a
Accrued interest receivable	6,863	278	3,498	3,087	6,863
LIABILITIES					
Deposits	$ (1,485,003)	$ (1,272,060)	$ (215,485)	$ 0	$ (1,487,545)
FHLB and other borrowings	(97,806)	0	(105,850)	0	(105,850)
Subordinated debentures	(20,620)	0	(10,682)	0	(10,682)
Interest rate swaps	(1,745)	0	(1,745)	0	(1,745)
Accrued interest payable	(1,022)	(301)	(707)	(14)	(1,022)

The methods and assumptions, not otherwise presented, used to estimate fair values are described as follows:

Cash and cash equivalents: The carrying amounts of cash and cash equivalents approximate fair values and are classified as Level 1.

Interest bearing time deposits with other banks: The fair value of interest bearing time deposits with other banks is estimated using a discounted cash flow calculation that applies interest rates currently being offered to a schedule of aggregated expected monthly maturities, resulting in a Level 2 classification.

Loans held for sale: The fair value of loans held for sale is estimated based upon binding contracts and quotes from third party investors resulting in a Level 2 classification.

Loans: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values, resulting in a Level 3 classification. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality, resulting in a Level 3 classification. Impaired loans are valued at the lower of cost or fair value as described previously. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

FHLB and other equity interests: It is not practical to determine the fair value of Federal Home Loan Bank stock and other equity interests due to restrictions placed on the transferability of these instruments.

Accrued interest receivable: The carrying amount of accrued interest receivable approximates fair value resulting in a classification that is consistent with the asset with which it is associated.

Deposits: The fair values disclosed for demand deposits are, by definition, equal to the amount payable on demand at the reporting date (i.e. their carrying amount), resulting in a Level 1 classification. Fair values for time deposits are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits, resulting in a Level 2 classification.

FHLB and other borrowings: The fair values of the Corporation s FHLB and other borrowings are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements, resulting in a Level 2 classification.

Subordinated debentures: The fair value of the Corporation s subordinated debentures are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of arrangements, resulting in a Level 3 classification.

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Accrued interest payable: The carrying amount of accrued interest payable approximates fair value resulting in a classification that is consistent with the liability with which it is associated.

While estimates of fair value are based on management s judgment of the most appropriate factors as of the balance sheet date, there is no assurance that the estimated fair values would have been realized if the assets had been disposed of or the liabilities settled at that date, since market values may differ depending on various circumstances. The estimated fair values would also not apply to subsequent dates.

In addition, other assets and liabilities that are not financial instruments, such as premises and equipment, are not included in the disclosures. Also, non-financial assets such as, among other things, the estimated earnings power of core deposits, the earnings potential of trust accounts, the trained workforce, and customer goodwill, which typically are not recognized on the balance sheet, may have value but are not included in the fair value disclosures.

5. SECURITIES

Securities available for sale at June 30, 2013 and December 31, 2012 are as follows:

	June 30, 2013				December 31, 2012			
	Amortized	Unrealized		Fair	Amortized	Unrealized		Fair
	Cost	Gains	Losses	Value	Cost	Gains	Losses	Value
U.S. Treasury	$ 2,008	$ 8	$ 0	$ 2,016	$ 4,018	$ 18	$ 0	$ 4,036
U.S. Gov t sponsored entities	181,161	3,420	(4,519)	180,062	157,965	5,977	(161)	163,781
State & political subdivisions	179,079	4,629	(2,473)	181,235	170,223	11,113	(57)	181,279
Residential & multi-family mortgage	274,041	3,195	(5,899)	271,337	308,800	8,724	(702)	316,822
Commercial mortgage	995	0	(12)	983	1,275	29	0	1,304
Corporate notes & bonds	14,989	59	(1,674)	13,374	17,368	26	(2,370)	15,024
Pooled trust preferred	800	0	(170)	630	800	0	(200)	600
Pooled SBA	73,333	1,444	(1,114)	73,663	50,667	2,277	(17)	52,927
Other securities	1,020	0	(22)	998	1,521	17	0	1,538
Total	$ 727,426	$ 12,755	$ (15,883)	$ 724,298	$ 712,637	$ 28,181	$ (3,507)	$ 737,311

At June 30, 2013, there were no holdings of securities of any one issuer, other than the U.S. Government sponsored entities, in an amount greater than 10% of shareholders equity. The Corporation s residential and multi-family mortgage securities are issued by government sponsored entities, and the Corporation holds one commercial mortgage security that is private label.

Trading securities at June 30, 2013 and December 31, 2012 are as follows:

	June 30, 2013	December 31, 2012
Corporate equity securities	$ 3,432	$ 3,117
Certificates of deposit	354	408
International mutual funds	273	287
Large cap growth mutual funds	164	157
Large cap value mutual funds	106	104
Real estate investment trust mutual funds	102	65
Corporate notes and bonds	101	101
Mid cap mutual funds	68	26
Small cap mutual funds	56	26
U.S. Government sponsored entities	54	58
Money market mutual funds	19	110

Total	$ 4,729	$ 4,459

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Securities with unrealized losses at June 30, 2013 and December 31, 2012, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, are as follows (in thousands):

June 30, 2013

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. Treasury	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
U.S. Gov t sponsored entities	110,070	(4,519)	0	0	110,070	(4,519)
State & political subdivisions	62,488	(2,460)	472	(13)	62,960	(2,473)
Residential & multi-family mortgage	158,788	(5,695)	5,575	(204)	164,363	(5,899)
Commercial mortgage	983	(12)	0	0	983	(12)
Corporate notes & bonds	1,597	(3)	9,720	(1,671)	11,317	(1,674)
Pooled trust preferred	0	0	630	(170)	630	(170)
Pooled SBA	37,325	(1,114)	0	0	37,325	(1,114)
Other securities	998	(22)	0	0	998	(22)
	$ 372,249	$ (13,825)	$ 16,397	$ (2,058)	$ 388,646	$ (15,883)

December 31, 2012

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. Treasury	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
U.S. Gov t sponsored entities	41,715	(161)	0	0	41,715	(161)
State & political subdivisions	7,857	(57)	0	0	7,857	(57)
Residential & multi-family mortgage	32,159	(688)	4,254	(14)	36,413	(702)
Commercial mortgage	0	0	0	0	0	0
Corporate notes & bonds	0	0	13,002	(2,370)	13,002	(2,370)
Pooled trust preferred	0	0	600	(200)	600	(200)
Pooled SBA	3,521	(17)	0	0	3,521	(17)
Other securities	0	0	0	0	0	0
	$ 85,252	$ (923)	$ 17,856	$ (2,584)	$ 103,108	$ (3,507)

The Corporation evaluates securities for other-than-temporary impairment on a quarterly basis, or more frequently when economic or market conditions warrant such an evaluation.

At June 30, 2013, the Corporation held one structured pooled trust preferred security with an adjusted amortized cost of $800 and a fair value of $630. The Corporation evaluated this security for other-than-temporary impairment by estimating the cash flows expected to be received, taking into account future estimated levels of deferrals and defaults by the underlying issuers, and discounting those cash flows at the appropriate accounting yield. For the three and six months ended June 30, 2013, and June 30, 2012, no other-than-temporary impairment was required to be realized in earnings. At June 30, 2013 and December 31, 2012, the Corporation held four structured pooled trust preferred securities with an adjusted amortized cost and fair value of zero.

A roll-forward of the other-than-temporary impairment amount related to credit losses for the three and six months ended June 30, 2013 and 2012 is as follows:

Balance of credit losses on debt securities for which a portion of other-than-temporary impairment was recognized in earnings, beginning of period	$ 4,054
Additional credit loss for which other-than-temporary impairment was not previously recognized	0
Additional credit loss for which other-than-temporary impairment was previously recognized	0
Balance of credit losses on debt securities for which a portion of other-than-temporary impairment was recognized in earnings, end of period	$ 4,054

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Due to the insignificance of the adjusted amortized cost balance, no further disclosures are required with respect to the Corporation s structured pooled trust preferred securities.

For the securities that comprise corporate notes and bonds and the securities that are issued by state and political subdivisions, management monitors publicly available financial information, such as filings with the Securities and Exchange Commission, in order to evaluate the securities for other-than-temporary impairment. For financial institution issuers, management monitors information from quarterly call report filings that are used to generate Uniform Bank Performance Reports. All other securities that were in an unrealized loss position at the balance sheet date were reviewed by management, and issuer-specific documents were reviewed, as appropriate given the following considerations. When reviewing securities for other-than-temporary impairment, management considers the financial condition and near-term prospects of the issuer and whether downgrades by bond rating agencies have occurred. Management also considers the length of time and extent to which fair value has been less than cost, and management does not have the intent to sell these securities and it is likely that it will not be required to sell the securities before their anticipated recovery.

As of June 30, 2013 and December 31, 2012, management concluded that the securities described in the previous paragraph were not other-than-temporarily impaired for the following reasons:

There is no indication of any significant deterioration of the creditworthiness of the institutions that issued the securities.

All contractual interest payments on the securities have been received as scheduled, and no information has come to management s attention through the processes previously described which would lead to a conclusion that future contractual payments will not be timely received.

The Corporation does not intend to sell and it is not more likely than not that it will be required to sell the securities in an unrealized loss position before recovery of its amortized cost basis.

Information pertaining to security sales is as follows:

	Proceeds	Gross Gains	Gross Losses
Three months ended June 30, 2013	$ 32,348	$ 746	$ (494)
Six months ended June 30, 2013	33,672	822	(494)
Three months ended June 30, 2012	46,468	810	(79)
Six months ended June 30, 2012	88,617	1,446	(149)

The following is a schedule of the contractual maturity of securities available for sale, excluding equity securities, at June 30, 2013:

	Amortized Cost	Fair Value
1 year or less	$ 30,013	$ 29,950
1 year 5 years	129,080	129,346
5 years 10 years	174,686	175,054
After 10 years	44,258	42,967
	378,037	377,317
Residential and multi-family mortgage	274,041	271,337
Pooled SBA	73,333	73,663
Commercial mortgage	995	983
Total debt securities	$ 726,406	$ 723,300

Mortgage and asset backed securities and pooled SBA securities are not due at a single date; periodic payments are received based on the payment patterns of the underlying collateral.

On June 30, 2013 and December 31, 2012, securities carried at $311,493 and $264,813, respectively, were pledged to secure public deposits and for other purposes as provided by law.

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6. LOANS

Total net loans at June 30, 2013 and December 31, 2012 are summarized as follows:

	June 30, 2013	December 31, 2012
Commercial, industrial, and agricultural	$ 263,749	$ 257,091
Commercial mortgages	283,654	261,791
Residential real estate	374,987	347,904
Consumer	58,718	58,668
Credit cards	4,718	4,800
Overdrafts	656	971
Less: unearned discount	(3,535)	(3,401)
allowance for loan losses	(15,500)	(14,060)
Loans, net	$ 967,447	$ 913,764

At June 30, 2013 and December 31, 2012, net unamortized loan costs of $105 and $232, respectively, have been included in the carrying value of loans.

The Corporation s outstanding loans and related unfunded commitments are primarily concentrated within Central and Western Pennsylvania. The Bank attempts to limit concentrations within specific industries by utilizing dollar limitations to single industries or customers and by entering into participation agreements with third parties. Collateral requirements are established based on management s assessment of the customer.

The Corporation maintains lending policies to control the quality of the loan portfolio. These policies delegate the authority to extend loans under specific guidelines and underwriting standards. These policies are prepared by the Corporation s management and reviewed and ratified annually by the Corporation s Board of Directors.

All relevant documentation, such as the loan application, financial statements and tax returns, required under the lending policies is summarized and provided to management and/or the Corporation s Board of Directors in connection with the loan approval process. Such documentation is subsequently electronically archived in the Corporation s document management system. Pursuant to the Corporation s lending policies, management considers a variety of factors when determining whether to extend credit to a customer, including loan-to-value ratios, FICO scores, quality of the borrower s financial statements, and the ability to obtain personal guarantees.

Commercial, industrial, and agricultural loans comprised 27% and 28% of the Corporation s total loan portfolio at June 30, 2013 and December 31, 2012, respectively. Commercial mortgage loans comprised 29% and 28% of the Corporation s total loan portfolio at June 30, 2013 and December 31, 2012, respectively. Management assigns a risk rating to all commercial loans in excess of $250,000. The loan-to-value policy guidelines for commercial, industrial, and agricultural loans are generally a maximum of 80% of the value of business equipment, a maximum of 75% of the value of accounts receivable, and a maximum of 60% of the value of business inventory. The loan-to-value policy guideline for commercial mortgage loans is generally a maximum of 85% of the appraised value of the real estate.

Residential real estate loans comprised 38% and 37% of the Corporation s total loan portfolio at June 30, 2013 and December 31, 2012, respectively. The loan-to-value policy guidelines for residential real estate loans vary depending on the collateral position and the specific type of loan. Higher loan-to-value terms may be approved with the appropriate private mortgage insurance coverage. Residential real estate loan customers are also placed in a three-tiered risk grade using their FICO score as the primary determinant. The Corporation also originates and prices loans for sale into the secondary market through Freddie Mac. The rationale for these sales is to mitigate interest rate risk associated with holding lower rate, long-term residential mortgages in the loan portfolio and to generate fee revenue from sales and servicing the loan. The Corporation also offers a variety of unsecured and secured consumer loan and credit card products which represent less than 10% of the total loan portfolio at both June 30, 2013 and December 31, 2012. Consumer loan customers are also placed in a three-tiered risk grade using their FICO scores as the primary determinant. Terms and collateral requirements vary depending on the size and nature of the loan.

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CNB has not underwritten any hybrid loans, payment option loans, or low documentation/no documentation loans. Variable rate loans are generally underwritten at the fully indexed rate. Loan underwriting policies and procedures have not changed materially between any periods presented.

Transactions in the allowance for loan losses for the three months ended June 30, 2013 were as follows:

	Commercial, Industrial, and Agricultural	Commercial Mortgages	Residential Real Estate	Consumer	Credit Cards	Overdrafts	Total
Allowance for loan losses, April 1, 2013	$ 5,271	$ 4,299	$ 2,395	$ 1,707	$ 77	$ 148	$ 13,897
Charge-offs	(84)	(923)	(169)	(346)	(17)	(44)	(1,583)
Recoveries	7	2	3	33	8	18	71
Provision (benefit) for loan losses	144	2,518	279	161	(13)	26	3,115
Allowance for loan losses, June 30, 2013	$ 5,338	$ 5,896	$ 2,508	$ 1,555	$ 55	$ 148	$ 15,500

Transactions in the allowance for loan losses for the six months ended June 30, 2013 were as follows:

	Commercial, Industrial, and Agricultural	Commercial Mortgages	Residential Real Estate	Consumer	Credit Cards	Overdrafts	Total
Allowance for loan losses, January 1, 2013	$ 4,940	$ 4,697	$ 2,466	$ 1,699	$ 83	$ 175	$ 14,060
Charge-offs	(84)	(1,530)	(341)	(677)	(29)	(91)	(2,752)
Recoveries	7	3	4	74	10	49	147
Provision (benefit) for loan losses	475	2,726	379	459	(9)	15	4,045
Allowance for loan losses, June 30, 2013	$ 5,338	$ 5,896	$ 2,508	$ 1,555	$ 55	$ 148	$ 15,500

Transactions in the allowance for loan losses for the three months ended June 30, 2012 were as follows:

	Commercial, Industrial, and Agricultural	Commercial Mortgages	Residential Real Estate	Consumer	Credit Cards	Overdrafts	Total
Allowance for loan losses, April 1, 2012	$ 4,942	$ 4,377	$ 1,997	$ 1,435	$ 96	$ 168	$ 13,015
Charge-offs	(422)	(121)	(137)	(382)	(14)	(50)	(1,126)
Recoveries	5	0	0	22	6	22	55
Provision (benefit) for loan losses	590	297	365	493	(7)	8	1,746
Allowance for loan losses, June 30, 2012	$ 5,115	$ 4,553	$ 2,225	$ 1,568	$ 81	$ 148	$ 13,690

Transactions in the allowance for loan losses for the six months ended June 30, 2012 were as follows:

	Commercial, Industrial, and Agricultural	Commercial Mortgages	Residential Real Estate	Consumer	Credit Cards	Overdrafts	Total
Allowance for loan losses, January 1, 2012	$ 4,511	$ 4,470	$ 1,991	$ 1,404	$ 71	$ 168	$ 12,615
Charge-offs	(647)	(236)	(224)	(638)	(33)	(117)	(1,895)

Recoveries	8	0	0	49	7	56	120
Provision for loan losses	1,243	319	458	753	36	41	2,850
Allowance for loan losses, June 30, 2012	$ 5,115	$ 4,553	$ 2,225	$ 1,568	$ 81	$ 148	$ 13,690

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The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and is based on the Corporation s impairment method as of June 30, 2013 and December 31, 2012. The recorded investment in loans excludes accrued interest due to its insignificance.

June 30, 2013

	Commercial, Industrial, and Agricultural	Commercial Mortgages	Residential Real Estate	Consumer	Credit Cards	Overdrafts	Total
Allowance for loan losses:							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$ 612	$ 867	$ 0	$ 0	$ 0	$ 0	$ 1,479
Collectively evaluated for impairment	4,726	3,807	2,508	1,555	55	148	12,799
Modified in a troubled debt restructuring	0	1,222	0	0	0	0	1,222
Total ending allowance balance	$ 5,338	$ 5,896	$ 2,508	$ 1,555	$ 55	$ 148	$ 15,500
Loans:							
Loans individually evaluated for impairment	$ 2,222	$ 12,788	$ 74	$ 0	$ 0	$ 0	$ 15,084
Loans collectively evaluated for impairment	260,182	261,981	374,913	55,183	4,718	656	957,633
Loans modified in a troubled debt restructuring	1,345	8,885	0	0	0	0	10,230
Total ending loans balance	$ 263.749	$ 283,654	$ 374,987	$ 55,183	$ 4,718	$ 656	$ 982,947

December 31, 2012

	Commercial, Industrial, and Agricultural	Commercial Mortgages	Residential Real Estate	Consumer	Credit Cards	Overdrafts	Total
Allowance for loan losses:							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$ 541	$ 131	$ 81	$ 0	$ 0	$ 0	$ 753
Collectively evaluated for impairment	4,399	3,467	2,385	1,699	83	175	12,208
Modified in a troubled debt restructuring	0	1,099	0	0	0	0	1,099
Total ending allowance balance	$ 4,940	$ 4,697	$ 2,466	$ 1,699	$ 83	$ 175	$ 14,060
Loans:							
Loans individually evaluated for impairment	$ 2,623	$ 10,683	$ 593	$ 0	$ 0	$ 0	$ 13,899
Loans collectively evaluated for impairment	253,048	240,907	347,311	55,267	4,800	971	902,304
Loans modified in a troubled debt restructuring	1,420	10,201	0	0	0	0	11,621
Total ending loans balance	$ 257,091	$ 261,791	$ 347,904	$ 55,267	$ 4,800	$ 971	$ 927,824

The following tables present information related to loans individually evaluated for impairment by portfolio segment as of June 30, 2013 and December 31, 2012 and for the three and six months ended June 30, 2013 and 2012:

June 30, 2013

	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
With an allowance recorded:			
Commercial, industrial, and agricultural	$ 1,843	$ 1,449	$ 612
Commercial mortgage	8,138	6,689	2,089
Residential real estate	0	0	0
With no related allowance recorded:			
Commercial, industrial, and agricultural	2,679	2,118	0
Commercial mortgage	16,758	14,984	0
Residential real estate	153	74	0
Total	$ 29,571	$ 25,314	$ 2,701

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December 31, 2012

	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
With an allowance recorded:			
Commercial, industrial, and agricultural	$ 2,542	$ 1,792	$ 541
Commercial mortgage	5,870	5,329	1,230
Residential real estate	416	381	81
With no related allowance recorded:			
Commercial, industrial, and agricultural	2,804	2,251	0
Commercial mortgage	17,285	15,555	0
Residential real estate	308	212	0
Total	$ 29,225	$ 25,520	$ 1,852

	Three Months Ended June 30, 2013			Six Months Ended June 30, 2013		
	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
With an allowance recorded:						
Commercial, industrial, and agricultural	$ 1,459	$ 1	$ 1	$ 1,621	$ 1	$ 1
Commercial mortgage	5,787	0	0	6,009	3	3
Residential real estate	62	2	2	191	3	3
With no related allowance recorded:						
Commercial, industrial, and agricultural	2,172	0	0	2,184	0	0
Commercial mortgage	14,637	0	0	15,270	0	0
Residential real estate	76	0	0	143	0	0
Total	$ 24,193	$ 3	$ 3	$ 25,418	$ 7	$ 7

	Three Months Ended June 30, 2012			Six Months Ended June 30, 2012		
	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
With an allowance recorded:						
Commercial, industrial, and agricultural	$ 3,528	$ 4	$ 4	$ 3,290	$ 4	$ 4
Commercial mortgage	6,031	0	0	5,376	0	0
Residential real estate	353	4	4	277	8	8
With no related allowance recorded:						
Commercial, industrial, and agricultural	3,537	0	0	3,458	0	0
Commercial mortgage	12,123	0	0	12,108	0	0
Residential real estate	68	0	0	45	0	0
Total	$ 25,640	$ 8	$ 8	$ 24,554	$ 12	$ 12

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The following table presents the recorded investment in nonaccrual loans and loans past due over 90 days still accruing interest by class of loans as of June 30, 2013 and December 31, 2012:

	June 30, 2013		December 31, 2012	
	Nonaccrual	Past Due Over 90 Days Still on Accrual	Nonaccrual	Past Due Over 90 Days Still on Accrual
Commercial, industrial, and agricultural	$ 2,630	$ 0	$ 3,073	$ 0
Commercial mortgages	14,240	0	8,570	109
Residential real estate	2,282	0	2,792	18
Consumer	430	193	10	217
Credit cards	0	19	0	13
Total	$ 19,582	$ 212	$ 14,445	$ 357

Nonaccrual loans and loans past due over 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time (generally six months) and the ultimate collectability of the total contractual principal and interest is no longer in doubt.

The following table presents the aging of the recorded investment in past due loans as of June 30, 2013 and December 31, 2012 by class of loans.

June 30, 2013

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial, industrial, and agricultural	$ 135	$ 127	$ 2,531	$ 2,793	$ 260,956	$ 263,749
Commercial mortgages	0	71	13,177	13,248	270,406	283,654
Residential real estate	2,153	581	2,184	4,918	370,069	374,987
Consumer	503	231	195	929	54,254	55,183
Credit cards	29	25	19	73	4,645	4,718
Overdrafts	0	0	0	0	656	656
Total	$ 2,820	$ 1,035	$ 18,106	$ 21,961	$ 960,986	$ 982,947

December 31, 2012

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial, industrial, and agricultural	$ 724	$ 157	$ 2,968	$ 3,849	$ 253,242	$ 257,091
Commercial mortgages	1,162	3,197	8,679	13,038	248,753	261,791
Residential real estate	1,390	641	2,700	4,731	343,173	347,904
Consumer	724	203	227	1,154	54,113	55,267

Credit cards	39	9	13	61	4,739	4,800
Overdrafts	0	0	0	0	971	971
Total	$ 4,039	$ 4,207	$ 14,587	$ 22,833	$ 904,991	$ 927,824

Troubled Debt Restructurings

The terms of certain loans have been modified as troubled debt restructurings. The modification of the terms of such loans included either or both of the following: a reduction of the stated interest rate of the loan or an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk.

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The following table presents the number of loans, loan balances, and specific reserves for loans that have been restructured in a troubled debt restructuring as of June 30, 2013 and December 31, 2012.

	June 30, 2013			December 31, 2012		
	Number of Loans	Loan Balance	Specific Reserve	Number of Loans	Loan Balance	Specific Reserve
Commercial, industrial, and agricultural	2	$ 1,345	$ 0	2	$ 1,420	$ 0
Commercial mortgages	9	8,885	1,222	8	10,201	1,099
Residential real estate	0	0	0	0	0	0
Consumer	0	0	0	0	0	0
Credit cards	0	0	0	0	0	0
Total	11	$ 10,230	$ 1,222	10	$ 11,621	$ 1,099

The following tables present loans by class modified as troubled debt restructurings that occurred during the six months ended June 30, 2013 and 2012. There were no loans modified as troubled debt restructurings during the three months ended June 30, 2013 or 2012.

	Six Months Ended June 30, 2013		
	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial, industrial, and agricultural	0	$ 0	$ 0
Commercial mortgages	1	346	403
Residential real estate	0	0	0
Consumer	0	0	0
Credit cards	0	0	0
Total	1	$ 346	$ 403

	Six Months Ended June 30, 2012		
	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial, industrial, and agricultural	1	$ 310	$ 310
Commercial mortgages	4	2,556	2,556
Residential real estate	0	0	0
Consumer	0	0	0
Credit cards	0	0	0
Total	5	$ 2,866	$ 2,866

The troubled debt restructurings described above increased the allowance for loan losses by $0 and $0 during the three months ended June 30, 2013 and 2012 and $0 and $0 during the six months ended June 30, 2013 and 2012.

Modifications involving a reduction of the stated interest rate of the loan were for periods ranging from 4 to 15 years. Modifications involving an extension of the maturity date were for periods ranging from 4 to 18 years.

A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms. Except as discussed below, all loans modified in troubled debt restructurings are performing in accordance with their modified terms as of June 30, 2013 and December 31, 2012 and no principal balances were forgiven in connection with the loan restructurings. In the first quarter of 2013, the Corporation recorded a partial chargeoff of $595 for a commercial mortgage loan with a balance of $1,660 that had defaulted under its restructured terms in 2012 and was placed on nonaccrual status. The Corporation recorded an additional provision for loan losses of $0 and $135 on this loan during the three and six months ended June 30, 2013. In the second quarter of 2013, a commercial mortgage loan with a balance of $1,086 defaulted under its restructured terms and was placed on nonaccrual status. The Corporation recorded an additional provision for loan losses of $588 during the three and six months ended June 30, 2013.

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In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without a loan modification. This evaluation is performed using the Corporation s internal underwriting policies. The Corporation has no further loan commitments to customers whose loans are classified as a troubled debt restructuring.

Generally, non-performing troubled debt restructurings are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time (generally six months) and the ultimate collectability of the total contractual principal and interest is no longer in doubt.

Credit Quality Indicators

The Corporation classifies commercial, industrial, and agricultural loans and commercial mortgage loans into risk categories based on relevant information about the ability of borrowers to service their debt, such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. Loans with outstanding balances greater than $1 million are analyzed at least semiannually and loans with outstanding balances of less than $1 million are analyzed at least annually.

The Corporation uses the following definitions for risk ratings:

Special Mention: Loans classified as special mention have a potential weakness that deserves management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the Corporation s credit position at some future date.

Substandard: Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Corporation will sustain some loss if the deficiencies are not corrected.

Doubtful: Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not rated as special mention, substandard, or doubtful are considered to be pass rated loans. All loans included in the following tables have been assigned a risk rating within 12 months of the balance sheet date.

June 30, 2013

	Pass	Special Mention	Substandard	Doubtful	Total
Commercial, industrial, and agricultural	$ 239,015	$ 9,052	$ 15,419	$ 263	$ 263,749
Commercial mortgages	235,746	15,436	31,776	696	283,654
Total	$ 474,761	$ 24,488	$ 47,195	$ 959	$ 547,403

December 31, 2012

	Pass	Special Mention	Substandard	Doubtful	Total
Commercial, industrial, and agricultural	$ 234,835	$ 6,641	$ 15,459	$ 156	$ 257,091
Commercial mortgages	225,294	12,294	23,501	702	261,791
Total	$ 460,129	$ 18,935	$ 38,960	$ 858	$ 518,882

The Corporation considers the performance of the loan portfolio and its impact on the allowance for loan losses. For residential real estate, consumer, and credit card loan classes, the Corporation also evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. The following table presents the recorded investment in residential, consumer, and credit card loans based on payment activity as of June 30, 2013 and December 31, 2012:

	June 30, 2013			December 31, 2012		
	Residential Real Estate	Consumer	Credit Cards	Residential Real Estate	Consumer	Credit Cards
Performing	$ 372,705	$ 54,560	$ 4,699	$ 345,094	$ 55,040	$ 4,787
Non-performing	2,282	623	19	2,810	227	13
Total	$ 374,987	$ 55,183	$ 4,718	$ 347,904	$ 55,267	$ 4,800

The Corporation considers all overdraft loans to be performing loans given their short-term duration.

The Corporation s portfolio of residential real estate and consumer loans maintained within Holiday Financial Services Corporation (Holiday), a subsidiary that offers small balance unsecured and secured loans, primarily collateralized by automobiles and equipment, to borrowers with higher risk characteristics than are typical in the Bank s consumer loan portfolio, are considered to be subprime loans.

Holiday s loan portfolio is summarized as follows at June 30, 2013 and December 31, 2012:

	June 30, 2013	December 31, 2012
Consumer	$ 21,922	$ 21,535
Residential real estate	1,169	954
Less: unearned discount	(3,535)	(3,401)
Total	$ 19,556	$ 19,088

7. DEPOSITS

Total deposits at June 30, 2013 and December 31, 2012 are summarized as follows (in thousands):

	Percentage Change	June 30, 2013	December 31, 2012
Checking, non-interest bearing	0.8%	$ 176,700	$ 175,239
Checking, interest bearing	12.6%	379,273	336,911
Savings accounts	4.2%	791,469	759,910
Certificates of deposit	(6.5%)	199,104	212,943
	4.1%	$ 1,546,546	$ 1,485,003

8. EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income by the weighted average number of shares outstanding during the applicable period, excluding outstanding participating securities. Diluted earnings per share is computed using the weighted average number of shares determined for the basic computation plus the dilutive effect of potential common shares issuable under certain stock compensation plans. For the three and six months ended June 30, 2013, 37,500 shares issuable pursuant to outstanding stock options were excluded from the diluted earnings per share calculations because the strike prices associated with the options exceeded the market price of the Corporation s common stock thus making the shares anti-dilutive. For the three and six months ended June 30, 2012, 75,500 shares issuable pursuant to outstanding stock options were excluded from the diluted earnings per share calculations because the strike prices associated with the options exceeded the market price of the Corporation s common stock thus making the shares anti-dilutive.

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Unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and are included in the computation of earnings per share pursuant to the two-class method. The Corporation has determined that its outstanding non-vested stock awards are participating securities.

The computation of basic and diluted earnings per share is shown below (in thousands except per share data):

	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Net income per consolidated statements of income	$ 2,951	$ 4,336	$ 7,248	$ 8,683
Net earnings allocated to participating securities	(15)	(17)	(34)	(34)
Net earnings allocated to common stock	$ 2,936	$ 4,319	$ 7,214	$ 8,649
Basic earnings per common share computation:				
Distributed earnings allocated to common stock	$ 2,053	$ 2,044	$ 4,107	$ 4,084
Undistributed earnings allocated to common stock	883	2,275	3,107	4,565
Net earnings allocated to common stock	$ 2,936	$ 4,319	$ 7,214	$ 8,649
Weighted average common shares outstanding, including shares considered participating securities	12,510	12,440	12,502	12,421
Less: Average participating securities	(57)	(46)	(53)	(43)
Weighted average shares	12,453	12,394	12,449	12,378
Basic earnings per common share	$ 0.24	$ 0.35	$ 0.58	$ 0.70
Diluted earnings per common share computation:				
Net earnings allocated to common stock	$ 2,936	$ 4,319	$ 7,214	$ 8,649
Weighted average common shares outstanding for basic earnings per common share	12,453	12,394	12,449	12,378
Add: Dilutive effects of assumed exercises of stock options	1	3	1	3
Weighted average shares and dilutive potential common shares	12,454	12,397	12,450	12,381
Diluted earnings per common share	$ 0.24	$ 0.35	$ 0.58	$ 0.70

9. DERIVATIVE INSTRUMENTS

The Corporation records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and the resulting designation. Derivatives used to hedge the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives used to hedge the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges.

For derivatives designated as cash flow hedges, the effective portion of the changes in the fair value of the derivative is initially reported in other comprehensive income (outside of earnings) and subsequently reclassified into earnings when the hedged transaction affects earnings, and the ineffective portion of changes in the fair value of the derivative is recognized directly in earnings. The Corporation assesses the effectiveness of each hedging relationship by comparing the changes in cash flows of the derivative hedging instrument with the changes in cash flows of the designated hedged item or transaction.

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On August 1, 2008, the Corporation executed an interest rate swap agreement with a 5 year term and an effective date of September 15, 2008 in order to hedge cash flows associated with $10 million of a subordinated note that was issued by the Corporation during 2007 and elected cash flow hedge accounting for the agreement. The Corporation s objective in using this derivative is to add stability to interest expense and to manage its exposure to interest rate risk. The interest rate swap involves the receipt of variable-rate amounts in exchange for fixed-rate payments from August 1, 2008 to September 15, 2013 without exchange of the underlying notional amount. At June 30, 2013, the variable rate on the subordinated debt was 1.82% (LIBOR plus 155 basis points) and the Corporation was paying 5.84% (4.29% fixed rate plus 155 basis points).

In anticipation of the expiration of the 5 year interest rate swap agreement discussed immediately above, on May 3, 2011, the Corporation executed an interest rate swap agreement with a 5 year term and an effective date of September 15, 2013 which, as of that effective date, will hedge cash flows associated with $10 million of the subordinated note discussed immediately above. As with the prior interest rate swap agreement, the Corporation s objective in using this derivative is to add stability to interest expense and to manage its exposure to interest rate risk. The interest rate swap involves the receipt of variable-rate amounts in exchange for fixed-rate payments from September 15, 2013 to September 15, 2018 without exchange of the underlying notional amount. On the effective date, the variable rate on the subordinated debt will be LIBOR plus 155 basis points and the Corporation will be paying 5.57% (4.02% fixed rate plus 155 basis points).

As of June 30, 2013, no derivatives were designated as fair value hedges or hedges of net investments in foreign operations. Additionally, the Corporation does not use derivatives for trading or speculative purposes and currently does not have any derivatives that are not designated as hedges.

The following tables provide information about the amounts and locations of activity related to the interest rate swaps designated as cash flow hedges within the Corporation s consolidated balance sheet and statement of income as of June 30, 2013 and December 31, 2012 and for the three and six months ended June 30, 2013 and 2012:

	Liability Derivative		
		Fair value as of	
	Balance Sheet Location	June 30, 2013	December 31, 2012
Interest rate contracts	Accrued interest and other liabilities	($1,253)	($ 1,745)

For the Three Months Ended June 30, 2013	(a)	(b)	(c)	(d)	(e)
Interest rate contracts	$245	Interest expense subordinated debentures	($105)	Other income	$ 0

For the Six Months Ended June 30, 2013	(a)	(b)	(c)	(d)	(e)
Interest rate contracts	$319	Interest expense subordinated debentures	($202)	Other income	$ 0

For the Three Months Ended June 30, 2012	(a)	(b)	(c)	(d)	(e)
Interest rate contracts	($135)	Interest expense subordinated debentures	($98)	Other income	$ 0

For the Six Months Ended June 30, 2012	(a)	(b)	(c)	(d)	(e)
Interest rate contracts	($72)	Interest expense subordinated debentures	($192)	Other income	$ 0

(a) Amount of Gain or (Loss) Recognized in Other Comprehensive Loss on Derivative (Effective Portion), net of tax

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(b) Location of Gain or (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion)
(c) Amount of Gain or (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion)
(d) Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)
(e) Amount of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)

Amounts reported in accumulated other comprehensive loss related to the interest rate swap will be reclassified to interest expense as interest payments are made on the subordinated debentures. Such amounts reclassified from accumulated other comprehensive loss to interest expense in the next twelve months are expected to be $380.

As of June 30, 2013 and December 31, 2012, a cash collateral balance in the amount of $1,950 was maintained with a counterparty to the interest rate swaps. These balances are included in interest bearing deposits with other banks on the consolidated balance sheet.

10. RECENT ACCOUNTING PRONOUNCEMENTS

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income (ASU 2013-02). ASU 2013-02 requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about these amounts. ASU 2013-02 is effective prospectively for reporting periods beginning after December 15, 2012. The effect of adopting ASU 2013-02 did not have a material effect on the Corporation s financial statements.

In February 2013, the FASB issued Accounting Standards Update 2013-04, Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation Is Fixed at the Reporting Date (ASU 2013-04). ASU 2013-04 provides guidance for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of the guidance is fixed at the reporting date, except for obligations addressed within existing guidance in U.S. GAAP. ASU 2013-04 is effective for reporting periods beginning after December 15, 2013. The Corporation is evaluating the effect that the adoption of ASU 2013-04 will have on its financial statements.

11. SUBSEQUENT EVENT

In July 2013, the Corporation recorded a loan loss recovery of $1,379 related to an impaired commercial mortgage loan. The loan loss recovery will be recorded in the third quarter of 2013. A partial chargeoff had been recorded for this loan in a prior period. At the recovery date, the carrying amount of the loan was $5,171, which was satisfied in full by the Corporation s participation in the issuance of a loan at market terms to a new borrower who purchased the property securing the loan.

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ITEM 2

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION

AND RESULTS OF OPERATIONS

The following discussion and analysis of the consolidated financial statements of CNB Financial Corporation (the Corporation) is presented to provide insight into management s assessment of financial results. The Corporation s subsidiary, CNB Bank (the Bank), provides financial services to individuals and businesses primarily within its primary market area of the Pennsylvania counties of Cambria, Cameron, Clearfield, Crawford, Elk, Erie, Indiana, McKean and Warren. The Bank s market area also includes a portion of western Centre County including Philipsburg Borough, Rush Township and the western portions of Snow Shoe and Burnside Townships and a portion of Jefferson County, consisting of the boroughs of Brockway, Falls Creek, Punxsutawney, Reynoldsville and Sykesville, and the townships of Washington, Winslow and Henderson.

The Bank is subject to regulation, supervision and examination by the Pennsylvania State Department of Banking as well as the Federal Deposit Insurance Corporation. The financial condition and results of operations of the Corporation and its consolidated subsidiaries are not necessarily indicative of future performance. CNB Securities Corporation is incorporated in Delaware and currently maintains investments in debt and equity securities. County Reinsurance Company is an Arizona corporation and provides credit life and disability insurance for customers of CNB Bank. CNB Insurance Agency, incorporated in Pennsylvania, provides for the sale of nonproprietary annuities and other insurance products. Holiday Financial Services Corporation (Holiday), incorporated in Pennsylvania, offers small balance unsecured loans and secured loans, primarily collateralized by automobiles and equipment, to borrowers with higher risk characteristics.

When we use the terms we , us and our , we mean CNB Financial Corporation and its subsidiaries. Management s discussion and analysis should be read in conjunction with the Corporation s consolidated financial statements and related notes.

PENDING ACQUISITION

On March 26, 2013, the Corporation announced the signing of a definitive merger agreement to acquire FC Banc Corp. and its subsidiary, The Farmers Citizens Bank (FC Bank), for $30.00 per share in cash and stock, or approximately $40.4 million in the aggregate. FC Bank serves the northern Ohio markets of Bucyrus, Cardington, Fredericktown, Mount Hope and Shiloh, as well as the markets of Worthington and Upper Arlington in the greater Columbus, Ohio area, with 8 branch locations and a mortgage banking business headquartered in Dublin, Ohio. The transaction is expected to close in the fourth quarter of 2013, subject to customary closing conditions, including regulatory approvals and the approval of FC Banc Corp. shareholders. FC Bank will operate as a separate and distinctly branded division of CNB Bank, with local decision making and oversight.

GENERAL OVERVIEW

In the second quarter of 2013, the Corporation opened an eleventh Holiday office in Indiana, Pennsylvania and moved one of its Holiday offices from Bellefonte, Pennsylvania to State College, Pennsylvania. Finally, the Corporation expects to open a loan production office in Columbus, Ohio in the third quarter of 2013, pending receipt of regulatory and governmental agency approvals.

Management believes that the Corporation s ERIEBANK market, along with the traditional CNB Bank and Holiday Financial Services Corporation market areas, should provide the Bank with sustained loan and deposit growth during the remainder of 2013.

Management concentrates on return on average equity and earnings per share metrics, plus other metrics, to measure the performance of the Corporation. The interest rate environment will continue to play an important role in the future earnings of the Corporation. Some compression of the net interest margin was experienced in 2012 and the net interest margin has decreased 9 basis points in the first six months of 2013 compared to the first six months of 2012 as a result of the current interest rate environment. During the past several years, in order to address the historic lows on various key interest rates such as the Prime Rate and 3-month LIBOR, the Corporation has taken a variety of measures including instituting rate floors on our commercial lines of credit and home equity lines. In addition, the Corporation decreased interest rates on certain deposit products during 2012 and the first six months of 2013 but maintained deposit growth as a result of successful marketing and business development strategies. Non-interest costs are expected to increase with the growth of the Corporation; however, management s growth strategies are expected to also result in an increase in earning assets as well as enhanced non-interest income which is expected to more than offset increases in non-interest expenses in 2013 and beyond. While past results are not an indication of future earnings, management believes the Corporation is well-positioned to sustain core earnings during 2013.

The Dodd-Frank Act, enacted into law on July 21, 2010, includes numerous provisions designed to strengthen the financial industry, enhance consumer protection, expand disclosures and provide for transparency, and significantly changed the bank regulatory structure and affected and will continue to affect the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act also created a Consumer Financial Protection Bureau (CFPB), which is authorized to write rules on a number of consumer financial products, and a Financial Services Oversight Council, which is empowered to determine which entities are systematically significant and require tougher regulations.

The Dodd-Frank Act requires various federal agencies to adopt a broad range of new rules and regulations and to prepare various studies and reports for Congress.

It is difficult to predict at this time what specific impact certain provisions of the Dodd-Frank Act and the implementing rules and regulations, many which have yet to be written, will have on the Corporation, including any regulations promulgated by the CFPB. The legislation and any implementing rules that are ultimately issued could have adverse implications on the financial industry, the competitive environment, and the Corporation s ability to conduct business. The Corporation will have to apply resources to ensure that it is in compliance with all applicable provisions of the Dodd-Frank Act and any implementing rules, which may increase its costs of operations and adversely impact its earnings.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents totaled $24.8 million at June 30, 2013 compared to $31.9 million at December 31, 2012. Cash and cash equivalents fluctuate based on the timing and amount of liquidity events that occur in the normal course of business.

Management believes the liquidity needs of the Corporation are satisfied by the current balance of cash and cash equivalents, readily available access to traditional funding sources, and the portion of the investment and loan portfolios that mature within one year. These sources of funds will enable the Corporation to meet cash obligations and off-balance sheet commitments as they come due.

SECURITIES

Securities available for sale and trading securities have combined to decrease $12.7 million or 1.7% since December 31, 2012, as the Corporation has been able to deploy cash flows from the securities portfolio in its loan portfolio. See the notes to the consolidated financial statements for additional detail concerning the composition of the Corporation s securities portfolio and the process for evaluating securities for other-than-temporary impairment.

The Corporation generally buys into the market over time and does not attempt to time its transactions. In doing this, the highs and lows of the market are averaged into the portfolio and minimize the overall effect of different rate environments. Management monitors the earnings performance and the effectiveness of the liquidity of the securities portfolio on a regular basis through meetings of the Asset/Liability Committee of the Corporation s Board of Directors (ALCO). The ALCO also reviews and manages interest rate risk for the Corporation. Through active balance sheet management and analysis of the securities portfolio, a sufficient level of liquidity is maintained to satisfy depositor requirements and various credit needs of our customers.

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LOANS

The Corporation experienced an increase in loans, net of unearned discount, of $55.1 million, or 5.9%, during the first six months of 2013. Lending efforts are focused in the west, central and northwest Pennsylvania markets and consist principally of commercial and retail lending, which includes single family residential mortgages and other consumer loans. The Corporation views commercial lending as its competitive advantage and continues to focus on this area by hiring and retaining experienced loan officers and supporting them with quality credit analysis. The Corporation expects sustained loan demand throughout the remainder of 2013.

ALLOWANCE FOR LOAN LOSSES

The allowance for loan losses is established by provisions for losses in the loan portfolio as well as overdrafts in deposit accounts. These provisions are charged against current income. Loans and overdrafts deemed not collectible are charged off against the allowance while any subsequent collections are recorded as recoveries and increase the allowance.

The table below shows activity within the allowance account for the specified periods (in thousands):

	Six months ending June 30, 2013	Year ending December 31, 2012	Six months ending June 30, 2012
Balance at beginning of period	$ 14,060	$ 12,615	$ 12,615
Charge-offs:			
Commercial, industrial, and agricultural	84	2,871	647
Commercial mortgages	1,530	401	236
Residential real estate	341	304	224
Consumer	677	1,279	638
Credit cards	29	78	33
Overdrafts	91	257	117
	2,752	5,190	1,895
Recoveries:			
Commercial, industrial, and agricultural	7	45	8
Commercial mortgages	3		
Residential real estate	4	1	
Consumer	74	91	49
Credit cards	10	18	7
Overdraft deposit accounts	49	99	56
	147	254	120
Net charge-offs	(2,605)	(4,936)	(1,775)
Provision for loan losses	4,045	6,381	2,850
Balance at end of period	$ 15,500	$ 14,060	$ 13,690
Loans, net of unearned	$ 982,947	$ 927,824	$ 906,767
Allowance to net loans	1.58%	1.52%	1.51%
Net charge-offs to average loans (annualized)	0.55%	0.55%	0.41%
Nonperforming assets	$ 19,968	$ 15,127	$ 18,519
Nonperforming % of total assets	1.10%	0.85%	1.08%

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The adequacy of the allowance for loan losses is subject to a formal analysis by the credit administrator of the Corporation. As part of the formal analysis, delinquencies and losses are monitored monthly. The loan portfolio is divided into several categories in order to better analyze the entire pool. First is a selection of classified loans that is given a specific reserve. The remaining loans are pooled, by category, into these segments:

Reviewed

- Commercial, industrial, and agricultural
- Commercial mortgages

Homogeneous

- Residential real estate
- Consumer
- Credit cards
- Overdrafts

The reviewed loan pools are further segregated into four categories: special mention, substandard, doubtful, and unclassified. Historical loss factors are calculated for each pool excluding overdrafts based on the previous eight quarters of experience. The homogeneous pools are evaluated by analyzing the historical loss factors from the most previous quarter end and the two most recent year ends.

The historical loss factors for both the reviewed and homogeneous pools are adjusted based on these six qualitative factors:

- levels of and trends in delinquencies, non-accrual loans, and classified loans;
- trends in volume and terms of loans;
- effects of any changes in lending policies and procedures;
- experience, ability and depth of management;
- national and local economic trends and conditions; and
- concentrations of credit.

The methodology described above was created using the experience of the Corporation s credit administrator, guidance from the regulatory agencies, expertise of a third-party loan review provider, and discussions with peers. The resulting factors are applied to the pool balances in order to estimate the probable risk of loss within each pool. Prudent business practices dictate that the level of the allowance, as well as corresponding charges to the provision for loan losses, should be commensurate with identified areas of risk within the loan portfolio and the attendant risks inherent therein. The quality of the credit risk management function and the overall administration of this vital segment of the Corporation s assets are critical to the ongoing success of the Corporation.

The previously mentioned analysis considered numerous historical and other factors to analyze the adequacy of the allowance and current period charges against the provision for loan losses. Management uses the analysis to compare and plot the actual level of the allowance against the aggregate amount of loans adversely classified in order to compute the estimated probable losses associated with those loans. Management then determines the current adequacy of the allowance and evaluates trends that may be developing. The volume and composition of the Corporation s loan portfolio continue to reflect growth in commercial credits including commercial real estate loans.

As mentioned in the Loans section of this analysis, management considers commercial lending to be a competitive advantage and continues to focus on this area as part of its strategic growth initiatives. However, management recognizes and considers the fact that risk is more pronounced in these types of credits and is, to a greater degree than with other loans, driven by the economic environment in which the debtor s business operates.

During the six months ended June 30, 2013, CNB recorded a provision for loan losses of $4.0 million, as compared to a provision for loan losses of $2.9 million for the six months ended June 30, 2012. A commercial mortgage loan that was impaired at December 31, 2012 was placed on nonaccrual status during the three months ended March 31, 2013, resulting in an increase in nonperforming assets of $2.9 million. No loan loss reserve was required for this loan as of March 31, 2013 or December 31, 2012. However, due to a rapid deterioration in the loan collateral value, the Corporation recorded an increase in the provision for loan losses attributable to this impaired loan of $1.7 million during the second quarter. Subsequently, the Corporation recorded a partial chargeoff on the loan of $892 thousand, resulting in a recorded investment of $2.0 million and a specific reserve of $822 thousand as of June 30, 2013.

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A loan modified in a troubled debt restructuring that was nonperforming at December 31, 2012 was partially charged off in the first quarter of 2013, resulting in a decrease in nonperforming assets of $595 thousand. An additional provision for loan losses of $135 thousand was recorded for this loan during the first quarter of 2013.

During the second quarter of 2013, a commercial mortgage loan with a balance of $1.1 million that was previously modified in a troubled debt restructuring defaulted under its modified terms, resulting in an increase in the provision for loan losses of $611 thousand. Finally, a commercial mortgage loan with a carrying value of $3.3 million defaulted in the second quarter. Based on management s evaluation of the fair value of the associated collateral, no provision for loan losses was required to be recorded for this loan relationship.

Management believes that the allowance for loan losses is reasonable and adequate to absorb probable incurred losses in its portfolio at June 30, 2013.

PREMISES AND EQUIPMENT

In the second quarter of 2013, the Corporation entered into a contractual commitment to expand its main office facility in Clearfield, Pennsylvania at an approximate cost of $4 million. Construction has commenced with approximately $794 thousand in construction-related expenditures incurred as of June 30, 2013. Completion of the project is expected by the end of the first quarter of 2014.

FUNDING SOURCES

The Corporation considers deposits, short-term borrowings, and term debt when evaluating funding sources. Traditional deposits continue to be the main source of funds in the Corporation, increasing $61.5 million from $1.49 billion at December 31, 2012 to $1.55 billion at June 30, 2013. The growth in deposits was primarily due to increases in interest-bearing demand deposits of $42.4 million and savings accounts of $31.6 million as a result of the Corporation s successful marketing and business development strategies.

Periodically, the Corporation utilizes term borrowings from the Federal Home Loan Bank (FHLB) and other lenders to meet funding needs. Management plans to maintain access to short-term and long-term borrowings as an available funding source.

SHAREHOLDERS EQUITY AND CAPITAL RATIOS AND METRICS

The Corporation s capital continued to provide a base for profitable growth through June 30, 2013. Total shareholders equity was $131.0 million at June 30, 2013 and $145.4 million at December 31, 2012. In the first six months of 2013, the Corporation earned $7.2 million and declared dividends of $4.1 million, a dividend payout ratio of 57.0% of net income. The Corporation has also complied with the standards of capital adequacy mandated by the banking regulators. Bank regulators have established risk-based capital requirements designed to measure capital adequacy. Risk-based capital ratios reflect the relative risks of various assets banks hold in their portfolios. A weight category of 0% (lowest risk assets), 20%, 50%, or 100% (highest risk assets) is assigned to each asset on the balance sheet.

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The Corporation s capital ratios, book value per share and tangible book value per share as of June 30, 2013 and December 31, 2012 are as follows:

	June 30, 2013	December 31, 2012
Total risk-based capital ratio	15.11%	15.28%
Tier 1 capital ratio	13.86%	14.03%
Leverage ratio	7.94%	8.06%
Tangible common equity/tangible assets (1)	6.67%	7.63%
Book value per share	$ 10.47	$ 11.65
Tangible book value per share (1)	9.59	10.77

(1) Tangible common equity, tangible assets and tangible book value per share are non-GAAP financial measures calculated using GAAP amounts. Tangible common equity is calculated by excluding the balance of goodwill from the calculation of shareholders equity. Tangible assets is calculated by excluding the balance of goodwill from the calculation of total assets. Tangible book value per share is calculated by dividing tangible common equity by the number of shares outstanding. The Corporation believes that these non-GAAP financial measures provide information to investors that is useful in understanding its financial condition because they are additional measures used to assess capital adequacy. Because not all companies use the same calculation of tangible common equity and tangible assets, this presentation may not be comparable to other similarly titled measures calculated by other companies. A reconciliation of these non-GAAP financial measures is provided below (dollars in thousands, except share and per share data).

	June 30, 2013	December 31, 2012
Shareholders equity	$ 130,980	$ 145,364
Less goodwill	10,946	10,946
Tangible common equity	$ 120,034	$ 134,418
Total assets	$ 1,809,445	$ 1,773,079
Less goodwill	10,946	10,946
Tangible assets	$ 1,798,499	$ 1,762,133
Ending shares outstanding	12,511,095	12,475,904
Tangible book value per share	$ 9.59	$ 10.77
Tangible common equity/tangible assets	6.67%	7.63%

The decrease in tangible common equity/tangible assets, book value per share, and tangible book value per share from December 31, 2012 to June 30, 2013 is primarily attributable to the significant decline in the fair value of the Corporation s available-for-sale investment securities in relation to book value. This decline in fair value of available-for-sale securities was expected given the increases in intermediate and long-term interest rates that occurred in the second quarter of 2013.

RECENT LEGISLATION

In July 2013, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (collectively, the Agencies) approved final rules to implement the Basel III capital framework. The Corporation is required to implement the rules effective January 1, 2015. The new capital rules call for higher quality capital with higher minimum capital level requirements. The Company is in the process of assessing the impact from these complex regulatory requirements.

Management does not expect that the adoption of the new capital rules in 2015 will have a material impact on its capital position.

In May 2013, the Securities and Exchange Commission and the Commodity Futures Trading Commission (together, the Commissions) jointly issued final rules and guidelines to require certain regulated entities to establish programs to address risks of identity theft. The rules and guidelines implement provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act. These provisions amend Section 615(e) of the Fair Credit Reporting Act and directed the Commissions to adopt rules requiring entities that are subject to the Commissions jurisdiction to address identity theft in two ways. First, the

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rules require financial institutions and creditors to develop and implement a written identity theft prevention program that is designed to detect, prevent, and mitigate identity theft in connection with certain existing accounts or the opening of new accounts. The rules include guidelines to assist entities in the formulation and maintenance of programs that would satisfy the requirements of the rules. Second, the rules establish special requirements for any credit and debit card issuers that are subject to the Commissions jurisdiction, to assess the validity of notifications of changes of address under certain circumstances.

LIQUIDITY

Liquidity measures an organization s ability to meet cash obligations as they come due. The consolidated statement of cash flows provides analysis of the Corporation s cash and cash equivalents. Additionally, management considers that portion of the loan and investment portfolio that matures within one year to be part of the Corporation s liquid assets. The Corporation s liquidity is monitored by both management and the ALCO, which establishes and monitors ranges of acceptable liquidity. Management believes the Corporation s current liquidity position is acceptable.

OFF BALANCE SHEET ACTIVITIES

Some financial instruments, such as loan commitments, credit lines, letters of credit and overdraft protection, are issued to meet customer financing needs. The contractual amount of financial instruments with off-balance sheet risk was as follows at June 30, 2013 (in thousands):

Commitments to extend credit	$ 272,933
Standby letters of credit	13,220
	$ 286,153

Results of Operations

Three Months Ended June 30, 2013 and 2012

OVERVIEW OF THE INCOME STATEMENT

The Corporation had net income of $3.0 million in the second quarter of 2013, compared to $4.3 million for the same period of 2012. The earnings per diluted share were $0.24 in the second quarter of 2013 and $0.35 in the second quarter of 2012. As described below, non-interest expenses for the three months ended June 30, 2013 include $828 thousand associated with merger related expenses.

INTEREST INCOME AND EXPENSE

Net interest income totaled $13.8 million, an increase of $552 thousand, or 4.2%, over the second quarter of 2012. Total interest and dividend income decreased by $449 thousand, or 2.6%, as compared to the second quarter of 2012. Although the Corporation s earning assets continue to grow, these increases have been offset by decreases in the yield on earning assets resulting from the continued low interest rate environment. Total interest expense decreased $1.0 million, or 25.5%, as compared to the second quarter of 2012 due to decreases in the cost of deposits.

PROVISION FOR LOAN LOSSES

The Corporation recorded a provision for loan losses of $3.1 million in the second quarter of 2013 compared to $1.7 million in the second quarter of 2012. As disclosed in the Allowance for Loan Losses section of Management s Discussion and Analysis, in the second quarter of 2013, the Corporation recorded additional provisions for loan losses associated with an impaired loan and a loan previously modified in a troubled debt restructuring that defaulted.

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Management believes the provision for loan losses was appropriate and the allowance for loan losses is adequate to absorb probable incurred losses in our portfolio as of June 30, 2013.

NON-INTEREST INCOME

Excluding the effects of the securities transactions described below, non-interest income was $3.5 million for the three months ended June 30, 2013, compared to $2.7 million for the three months ended June 30, 2012. Net realized gains on available-for-sale securities were $252 thousand during the three months ended June 30, 2013 and $731 thousand during the three months ended June 30, 2012. Net realized and unrealized gains (losses) on trading securities were $28 thousand and ($140) thousand during the three months ended June 30, 2013 and 2012, respectively.

During the three months ended June 30, 2013, the Corporation recorded $815 thousand in income from bank owned life insurance policies, including $576 thousand representing the excess of the face value of certain policies over their cash surrender values resulting from the maturity of the policies.

Wealth and asset management fees increased from $426 thousand during the three months ended June 30, 2012 to $538 thousand during the three months ended June 30, 2013 due to increases in assets under management resulting from CNB s strategic focus to grow its Wealth and Asset Management Division.

NON-INTEREST EXPENSES

Total non-interest expenses increased $2.0 million, or 22.2%, during the three months ended June 30, 2013 compared to the three months ended June 30, 2012. Merger costs, including legal fees of $441 thousand and data processing costs of $289 thousand, associated with the Corporation s acquisition of FC Banc Corp. totaled $828 thousand during the three months ended June 30, 2013. In addition, salaries and benefits expenses increased $713 thousand, or 15.4%, during the three months ended June 30, 2013 compared to the three months ended June 30, 2012, in part due to routine merit increases, an increase in average full-time equivalent employees, and increases in certain employee benefit expenses, such as health insurance costs, which continue to increase in line with market conditions.

INCOME TAX EXPENSE

Income tax expense was $738 thousand in the second quarter of 2013 as compared to $1.6 million in the second quarter of 2012, resulting in effective tax rates of 20.0% and 27.2% for the periods, respectively. The effective rates for the periods differed from the federal statutory rate of 35.0% principally as a result of tax exempt income from securities and loans as well as earnings from bank owned life insurance.

AVERAGE BALANCES AND NET INTEREST MARGIN

The table on the following page presents the average balances and net interest margin for the six months ended June 30, 2013 and 2012. This information should be reviewed in conjunction with management s discussion and analysis for the results of operations for the six months ended June 30, 2013 and 2012 that follows the table.

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CONSOLIDATED YIELD COMPARISONS

AVERAGE BALANCES AND NET INTEREST MARGIN FOR THE SIX MONTHS ENDED

Dollars in thousands

	June 30, 2013			June 30, 2012		
	Average Balance	Annual Rate	Interest Inc./Exp.	Average Balance	Annual Rate	Interest Inc./Exp.
ASSETS:						
Interest-bearing deposits with other banks	$ 4,734	0.00%	$	$ 3,920	0.05%	$
Securities:						
Taxable (1)	623,425	2.26%	6,883	599,088	2.59%	7,575
Tax-Exempt (1,2)	131,237	4.56%	2,878	111,607	5.00%	2,641
Equity Securities (1,2)	3,856	5.19%	100	2,541	3.31%	42
Total securities	758,518	2.67%	9,861	713,236	2.96%	10,258
Loans:						
Commercial (2)	305,086	4.76%	7,268	293,703	5.01%	7,359
Mortgage (2)	589,755	4.81%	14,169	527,499	5.42%	14,299
Consumer	54,163	12.64%	3,424	51,110	12.77%	3,264
Total loans (3)	949,004	5.24%	24,861	872,312	5.71%	24,922
Total earning assets	1,712,256	4.11%	$ 34,722	1,589,468	4.48%	$ 35,180
Non interest-bearing assets:						
Cash and due from banks	26,498			27,911		
Premises and equipment	24,449			24,043		
Other assets	57,586			55,130		
Allowance for loan losses	(14,254)			(13,049)		
Total non interest-bearing assets	94,279			94,035		
TOTAL ASSETS	$ 1,806,535			$ 1,683,503		
LIABILITIES AND SHAREHOLDERS EQUITY:						
Demand - interest-bearing	$ 360,226	0.42%	$ 751	$ 300,482	0.54%	$ 809
Savings	792,160	0.52%	2,072	713,618	0.91%	3,246
Time	208,015	1.31%	1,366	241,423	1.69%	2,040
Total interest-bearing deposits	1,360,401	0.62%	4,189	1,255,523	0.97%	6,095
Short-term borrowings	16,839	0.23%	19	12,539	0.11%	7
Long-term borrowings	74,993	4.24%	1,589	74,410	4.24%	1,577
Subordinated debentures	20,620	3.76%	388	20,620	3.89%	401
Total interest-bearing liabilities	1,472,853	0.84%	$ 6,185	1,363,092	1.19%	$ 8,080
Demand - non interest-bearing	168,724			161,363		
Other liabilities	20,567			22,298		

Total liabilities	1,662,144			1,546,753		
Shareholders equity	144,391			136,750		
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$ 1,806,535			$ 1,683,503		
Interest income/Earning assets		4.11%	$ 34,722		4.48%	$ 35,180
Interest expense/Interest-bearing liabilities		0.84%	6,185		1.19%	8,080
Net interest spread		3.27%	$ 28,537		3.29%	$ 27,100
Interest income/Earning assets		4.11%	34,722		4.48%	35,180
Interest expense/Earning assets		0.72%	6,185		1.01%	8,080
Net interest margin		3.38%	$ 28,537		3.47%	$ 27,100

(1) Includes unamortized discounts and premiums. Average balance is computed using the carrying value of securities. The average yield has been computed using the historical amortized cost average balance for available for sale securities.

(2) Average yields are stated on a fully taxable equivalent basis.

(3) Average outstanding includes the average balance outstanding of all non-accrual loans. Loans consist of the average of total loans less average unearned income. The amount of loan fees included in the interest income on loans is not material.

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Six Months Ended June 30, 2013 and 2012

OVERVIEW OF THE INCOME STATEMENT

The Corporation had net income of $7.2 million for the six months ended June 30, 2013, compared to $8.7 million for the same period of 2012. The earnings per diluted share were $0.58 for the six months ended June 30, 2013 and $0.70 for the six months ended June 30, 2012. The return on average assets and return on average equity for the six months ended June 30, 2013 are 0.80% and 10.04%, respectively, compared to 1.03% and 12.70%, respectively, for the same period of 2012. As described below, non-interest expenses for the six months ended June 30, 2013 include $931 thousand associated merger related expenses.

INTEREST INCOME AND EXPENSE

During the six months ended June 30, 2013, net interest income increased $1.3 million, or 5.1%, compared to the six months ended June 30, 2012. The Corporation s net interest margin on a fully tax equivalent basis was 3.38% for the six months ended June 30, 2013, compared to 3.47% for the six months ended June 30, 2012.

Total interest and dividend income was $33.5 million for the six months ended June 30, 2013, a decrease of $569 thousand, or 1.7%, as compared to the six months ended June 30, 2012. Although the Corporation s earning assets continue to grow, these increases have been offset by decreases in the yield on earning assets resulting from the continued low interest rate environment. During the six months ended June 30, 2013, total interest expense decreased $1.9 million, or 23.5%, as compared to the six months ended June 30, 2012 due to decreases in the cost of deposits.

PROVISION FOR LOAN LOSSES

The Corporation recorded a provision for loan losses of $4.0 million during the six months ended June 30, 2013 compared to $2.9 million during the six months ended June 30, 2012. As disclosed in the Allowance for Loan Losses section of Management s Discussion and Analysis, in the first six months of 2013, the Corporation recorded additional provisions for loan losses associated with an impaired loan and a loan previously modified in a troubled debt restructuring that defaulted.

Management believes the provision for loan losses was appropriate and the allowance for loan losses is adequate to absorb probable incurred losses in our portfolio as of June 30, 2013.

NON-INTEREST INCOME

Excluding the effects of the securities transactions described below, non-interest income was $6.2 million for the six months ended June 30, 2013, compared to $5.2 million for the six months ended June 30, 2012. Net realized gains on available-for-sale securities were $328 thousand during the six months ended June 30, 2013, and $1.3 million during the six months ended June 30, 2012. Net realized and unrealized gains on trading securities were $331 thousand and $180 thousand during the six months ended June 30, 2013 and 2012, respectively.

During the six months ended June 30, 2013, the Corporation recorded $815 thousand in income from bank owned life insurance policies, including $576 thousand representing the excess of the face value of certain policies over their cash surrender values resulting from the maturity of the policies.

Wealth and asset management fees increased from $813 thousand during the six months ended June 30, 2012 to $1.1 million during the six months ended June 30, 2013 due to increases in assets under management resulting from CNB s strategic focus to grow its Wealth and Asset Management Division.

NON-INTEREST EXPENSES

Total non-interest expenses increased $2.6 million, or 14.7%, during the six months ended June 30, 2013 compared to the six months ended June 30, 2012. Merger costs, including legal fees of $530 thousand and data processing costs of $289 thousand, associated with the Corporation s acquisition of FC Banc Corp. totaled $931 thousand during the six months ended

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June 30, 2013. In addition, salaries and benefits expenses increased $1.2 million, or 12.7%, during the six months ended June 30, 2013 compared to the six months ended June 30, 2012, in part due to routine merit increases, an increase in average full-time equivalent employees, and increases in certain employee benefit expenses, such as health insurance costs, which continue to increase in line with market conditions.

INCOME TAX EXPENSE

Income tax expense was $2.4 million for the six months ended June 30, 2013 as compared to $3.3 for the six months ended June 30, 2012, resulting in effective tax rates of 24.5% and 27.2% for the periods, respectively. The effective rates for the periods differed from the federal statutory rate of 35.0% principally as a result of tax exempt income from securities and loans as well as earnings from bank owned life insurance.

CRITICAL ACCOUNTING POLICIES

The Corporation s accounting and reporting policies are in accordance with GAAP and conform to general practices within the financial services industry. Accounting and reporting practices for the allowance for loan losses and fair value of securities are deemed critical since they involve the use of estimates and require significant management judgments. Application of assumptions different than those used by management could result in material changes in the Corporation s financial position or results of operations. Note 1 (Summary of Significant Accounting Policies), Note 3 (Securities), and Note 4 (Loans), of the Corporation s 2012 Form 10-K, provide detail with regard to the Corporation s accounting for the allowance for loan losses and fair value of securities. There have been no significant changes in the application of accounting policies since December 31, 2012.

ITEM 3

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a financial institution, the Corporation s primary source of market risk is interest rate risk, which is the exposure to fluctuations in the Corporation s future earnings resulting from changes in interest rates. This exposure is correlated to the repricing characteristics of the Corporation s portfolio of assets and liabilities. Each asset or liability reprices either at maturity or during the life of the instrument.

The principal purpose of asset/liability management is to maximize current and future net interest income within acceptable levels of interest rate risk while satisfying liquidity and capital requirements. Net interest income is enhanced by increasing the net interest margin and by the growth in earning assets. As a result, the primary goal of interest rate risk management is to maintain a balance between risk and reward such that net interest income is maximized while risk is maintained at an acceptable level.

The Corporation uses an asset-liability management model to measure the effect of interest rate changes on its net interest income. The Corporation s management also reviews asset-liability maturity gap and repricing analyses regularly. The Corporation does not always attempt to achieve a precise match between interest sensitive assets and liabilities because it believes that an actively managed amount of interest rate risk is inherent and appropriate in the management of the Corporation s profitability.

Asset-liability modeling techniques and simulation involve assumptions and estimates that inherently cannot be measured with precision. Key assumptions in these analyses include maturity and repricing characteristics of assets and liabilities, prepayments on amortizing assets, non-maturing deposit sensitivity, and loan and deposit pricing. These assumptions are inherently uncertain due to the timing, magnitude, and frequency of rate changes and changes in market conditions and management strategies, among other factors. However, the analyses are useful in quantifying risk and provide a relative gauge of the Corporation s interest rate risk position over time.

Management reviews interest rate risk on a quarterly basis and reports to the ALCO. This review includes earnings shock scenarios whereby interest rates are immediately increased and decreased by 100, 300, and 400 basis points. These scenarios, detailed in the table below, indicate that there would not be a significant variance in net interest income over a one-year

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period due to interest rate changes; however, actual results could vary significantly. At June 30, 2013 and December 31, 2012, all interest rate risk levels according to the model were within the tolerance limits of ALCO approved policy of +/- 25%. In addition, the table does not take into consideration changes that management would make to realign its assets and liabilities in the event of an unexpected changing interest rate environment. Due to the historically low interest rate environment, the -300 and -400 scenarios have been excluded from the table.

June 30, 2013		December 31, 2012	
Change in Basis Points	% Change in Net Interest Income	Change in Basis Points	% Change in Net Interest Income
400	-1.7%	400	-0.5%
300	0.2%	300	-0.8%
100	1.7%	100	2.3%
(100)	-4.3%	(100)	-4.0%

ITEM 4

CONTROLS AND PROCEDURES

As of the end of the period covered by this quarterly report, an evaluation was carried out under the supervision and with the participation of the Corporation s management, including the Chief Executive Officer and Principal Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) under the Securities Exchange Act of 1934) (Exchange Act). Based on their evaluation, our Chief Executive Officer and Principal Financial Officer have concluded that the Corporation s disclosure controls and procedures were effective as of the end of the period covered by this quarterly report to ensure that information required to be disclosed by the Corporation in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms. There were no changes in the Corporation s internal control over financial reporting that occurred during the period covered by this quarterly report that have materially affected, or are reasonably likely to materially affect, the Corporation s internal control over financial reporting.

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PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS None

ITEM 1A. RISK FACTORS Management of the Corporation urges the reader to understand and consider the following updated risk factor in addition to those disclosed in the Corporation s Annual Report on Form 10-K for the fiscal year ended December 31, 2012 filed with the Securities and Exchange Commission on March 8, 2013.

The risks presented by acquisitions could adversely affect our financial condition and result of operations.

Any acquisitions, including our pending acquisition of FC Banc Corp., will be accompanied by the risks commonly encountered in acquisitions including, among other things: our ability to realize anticipated cost savings and avoid unanticipated costs relating to the merger, the difficulty of integrating operations and personnel, the potential disruption of our or the acquired company s ongoing business, the inability of our management to maximize our financial and strategic position, the inability to maintain uniform standards, controls, procedures and policies, and the impairment of relationships with the acquired company s employees and customers as a result of changes in ownership and management. These risks may prevent the Corporation from fully realizing the anticipated benefits of an acquisition or cause the realization of such benefits to take longer than expected.

ITEM 6. EXHIBITS

Exhibit No.	Description
2.1	Agreement and Plan of Merger, dated as of March 26, 2013, by and between the Corporation and FC Banc Corp., filed as Exhibit 2.1 to the Corporation s Current Report on Form 8-K, filed with the SEC on March 27, 2013 and incorporated herein by reference.
3.1	Amended and Restated Articles of Incorporation of the Corporation, filed as Appendix B to the 2005 Proxy Statement, filed with the SEC on March 24, 2006, and incorporated herein by reference.
3.2	By-Laws of the Corporation, as amended and restated, filed as Appendix C to the 2005 Proxy Statement, filed with the SEC on March 24, 2006, and incorporated herein by reference.
31.1	Rule 13a 14(a)/15d 14(a) Certification of the Principal Executive Officer
31.2	Rule 13a 14(a)/15d 14(a) Certification of the Principal Financial Officer
32.1	Section 1350 Certification
32.2	Section 1350 Certification
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definitions Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

	CNB FINANCIAL CORPORATION (Registrant)
DATE: August 8, 2013	/s/ Joseph B. Bower, Jr. Joseph B. Bower, Jr. President and Director (Principal Executive Officer)
DATE: August 8, 2013	/s/ Brian W. Wingard Brian W. Wingard Treasurer (Principal Financial Officer)

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