FARMERS CAPITAL BANK CORP
Form 10-Q
May 07, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT

Pursuant to Section 13 OR 15(d) of

The Securities Exchange Act of 1934

For the quarterly period ended March 31, 2015

Farmers Capital Bank Corporation
(Exact name of registrant as specified in its charter)

Kentucky	000-14412	61-1017851
(State or other jurisdiction of incorporation or organization)	(Commission File Number)	(IRS Employer Identification No.)

P.O. Box 309

202 West Main St.	40601
Frankfort, KY (Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code – (502) 227-1668

Not Applicable

(Former name, former address and former fiscal year, if changed since last report.)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes 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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

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

Common stock, par value $0.125 per share

7,492,429 shares outstanding at May 1, 2015

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PART I – FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statement

Unaudited Condensed Consolidated Balance Sheets

(In thousands, except share data)	March 31, 2015	December 31, 2014
Assets		
Cash and cash equivalents:		
Cash and due from banks	$21,802	$26,770
Interest bearing deposits in other banks	73,189	67,152
Federal funds sold and securities purchased under agreements to resell	11,057	6,992
Money market mutual funds	12,800	-
Total cash and cash equivalents	118,848	100,914
Investment securities:		
Available for sale, amortized cost of $638,266 (2015) and $618,429 (2014)	649,038	626,388
Held to maturity, fair value of $3,905 (2015) and $3,923 (2014)	3,715	3,728
Total investment securities	652,753	630,116
Loans, net of unearned income	927,389	931,943
Allowance for loan losses	(12,606)	(13,968)
Loans, net	914,783	917,975
Premises and equipment, net	34,497	34,933
Company-owned life insurance	29,587	29,363
Intangible assets, net	337	449
Other real estate owned	29,700	31,960
Other assets	34,833	36,896
Total assets	$1,815,338	$1,782,606
Liabilities		
Deposits:		
Noninterest bearing	$305,232	$292,788
Interest bearing	1,111,144	1,094,373
Total deposits	1,416,376	1,387,161
Federal funds purchased and other short-term borrowings	26,383	28,590
Securities sold under agreements to repurchase and other long-term borrowings	119,690	119,724
Subordinated notes payable to unconsolidated trusts	48,970	48,970
Dividends payable, preferred stock	113	113
Other liabilities	26,381	25,119
Total liabilities	1,637,913	1,609,677
Shareholders' Equity		
Preferred stock, no par value		
1,000,000 shares authorized; 10,000 Series A shares issued and outstanding at March 31, 2015 and December 31, 2014; Liquidation preference of $10,000	10,000	10,000
Common stock, par value $.125 per share	936	936

14,608,000 shares authorized; 7,491,658 and 7,489,388 shares issued and outstanding at March 31, 2015 and December 31, 2014, respectively		
Capital surplus	51,400	51,344
Retained earnings	109,623	105,774
Accumulated other comprehensive income	5,466	4,875
Total shareholders’ equity	177,425	172,929
Total liabilities and shareholders’ equity	$1,815,338	$1,782,606

See accompanying notes to unaudited condensed consolidated financial statements.

Unaudited Condensed Consolidated Statements of Income

	Three Months Ended March 31,	
(In thousands, except per share data)	2015	2014
Interest Income		
Interest and fees on loans	$11,716	$12,642
Interest on investment securities:		
Taxable	2,795	3,080
Nontaxable	656	624
Interest on deposits in other banks	50	27
Interest on federal funds sold and securities purchased under agreements to resell	3	1
Total interest income	15,220	16,374
Interest Expense		
Interest on deposits	821	1,203
Interest on federal funds purchased and other short-term borrowings	10	19
Interest on securities sold under agreements to repurchase and other long-term borrowings	1,176	1,264
Interest on subordinated notes payable to unconsolidated trusts	210	209
Total interest expense	2,217	2,695
Net interest income	13,003	13,679
Provision for loan losses	(1,545)	132
Net interest income after provision for loan losses	14,548	13,547
Noninterest Income		
Service charges and fees on deposits	1,772	1,916
Allotment processing fees	1,190	1,245
Other service charges, commissions, and fees	1,267	1,235
Trust income	571	545
Investment securities gains, net	120	9
Gains on sale of mortgage loans, net	165	97
Income from company-owned life insurance	241	246
Other	115	80
Total noninterest income	5,441	5,373
Noninterest Expense		
Salaries and employee benefits	8,320	7,351
Occupancy expenses, net	1,227	1,282
Equipment expenses	618	594
Data processing and communication expenses	1,055	1,005
Bank franchise tax	605	612
Amortization of intangibles	112	101
Deposit insurance expense	400	440
Other real estate expenses, net	45	1,064
Legal expenses	212	194
Other	1,916	1,787
Total noninterest expense	14,510	14,430
Income before income taxes	5,479	4,490
Income tax expense	1,405	1,120
Net income	4,074	3,370

Less preferred stock dividends and discount accretion	225	537
Net income available to common shareholders	$3,849	$2,833
Per Common Share		
Net income - basic and diluted	$.51	$.38
Cash dividends declared	N/A	N/A
Weighted Average Common Shares Outstanding		
Basic and diluted	7,490	7,479

See accompanying notes to unaudited condensed consolidated financial statements.

Unaudited Condensed Consolidated Statements of Comprehensive Income

	Three Months Ended March 31,	
(In thousands)	2015	2014
Net Income	$4,074	$3,370
Other comprehensive income:		
Unrealized holding gain on available for sale securities arising during the period on securities held at end of period, net of tax of $1,023 and $1,957, respectively	1,899	3,635
Reclassification adjustment for prior period unrealized (gain) loss previously reported in other comprehensive income recognized during current period, net of tax of $39 and $(27), respectively	(72)	51
Change in unfunded portion of postretirement benefit obligation, net of tax of $(665) and $12, respectively	(1,236)	23
Other comprehensive income	591	3,709
Comprehensive income	$4,665	$7,079

See accompanying notes to unaudited condensed consolidated financial statements.

Unaudited Condensed Consolidated Statements of Changes in Shareholders' Equity

(In thousands, except per share data) Three months ended March 31, 2015 and 2014	Preferred Stock	Common Stock Shares	Common Stock Amount	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance at January 1, 2015	$ 10,000	7,489	$ 936	$ 51,344	$ 105,774	$ 4,875	$ 172,929
Net income	-	-	-	-	4,074	-	4,074
Other comprehensive income	-	-	-	-	-	591	591
Cash dividends declared – preferred, $22.50 per share	-	-	-	-	(225)	-	(225)
Shares issued under director compensation plan	-	1	-	18	-	-	18
Shares issued pursuant to employee stock purchase plan	-	2	-	30	-	-	30
Expense related to employee stock purchase plan	-	-	-	8	-	-	8
Balance at March 31, 2015	$ 10,000	7,492	$ 936	$ 51,400	$ 109,623	$ 5,466	$ 177,425
Balance at January 1, 2014	$ 29,988	7,479	$ 935	$ 51,102	$ 91,242	$ (3,212)	$ 170,055
Net income	-	-	-	-	3,370	-	3,370
Other comprehensive income	-	-	-	-	-	3,709	3,709
Cash dividends declared – preferred, $17.50 per share	-	-	-	-	(525)	-	(525)
Preferred stock discount accretion	12	-	-	-	(12)	-	-
Shares issued under director compensation plan	-	1	-	18	-	-	18
Shares issued pursuant to employee stock purchase plan	-	1	-	29	-	-	29
Expense related to employee stock purchase plan	-	-	-	9	-	-	9
Balance at March 31, 2014	$ 30,000	7,481	$ 935	$ 51,158	$ 94,075	$ 497	$ 176,665

See accompanying notes to unaudited condensed consolidated financial statements.

Unaudited Condensed Consolidated Statements of Cash Flows

Three months ended March 31, (In thousands)	2015	2014
Cash Flows from Operating Activities		
Net income	$4,074	$3,370
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,031	1,022
Net premium amortization of investment securities:		
Available for sale	1,045	928
Held to maturity	13	3
Provision for loan losses	(1,545)	132
Deferred income tax expense	26	1
Noncash employee stock purchase plan expense	8	9
Noncash director fee compensation	18	18
Mortgage loans originated for sale	(6,474)	(7,049)
Proceeds from sale of mortgage loans	6,858	10,293
Gain on sale of mortgage loans, net	(165)	(97)
Gain on disposal of premises and equipment, net	-	(5)
Net (gain) loss on sale and write downs of other real estate	(74)	816
Net gain on sale of available for sale investment securities	(120)	(9)
Increase in cash surrender value of company-owned life insurance	(224)	(232)
Decrease in accrued interest receivable	264	38
Decrease in other assets	1,399	1,225
Decrease in accrued interest payable	(59)	(96)
(Decrease) increase in other liabilities	(608)	846
Net cash provided by operating activities	5,467	11,213
Cash Flows from Investing Activities		
Proceeds from maturities and calls of available for sale investment securities	26,074	24,456
Proceeds from sale of available for sale investment securities	9,407	9,406
Purchase of investment securities:		
Available for sale	(56,243)	(24,054)
Held to maturity	-	(3,065)
Proceeds from sale of restricted stock investments, net	-	148
Principal collected on loans originated for investment, net	4,428	11,623
Purchase of premises and equipment	(433)	(667)
Proceeds from sale of other real estate	2,455	741
Proceeds from disposals of premises and equipment	-	5
Net cash (used in) provided by investing activities	(14,312)	18,593
Cash Flows from Financing Activities		
Net increase (decrease) in deposits	29,215	(983)
Net decrease in federal funds purchased and other short-term borrowings	(2,207)	(1,730)
Proceeds from securities sold under agreements to repurchase and other long-term borrowings	2	3
Repayments of securities sold under agreements to repurchase and other long-term borrowings	(36)	(40)
Dividends paid, preferred stock	(225)	(375)
Shares issued under employee stock purchase plan	30	29
Net cash provided by (used in) financing activities	26,779	(3,096)
Net increase in cash and cash equivalents	17,934	26,710
Cash and cash equivalents at beginning of year	100,914	68,253

Cash and cash equivalents at end of period	$118,848	$94,963
Supplemental Disclosures		
Cash paid during the period for interest	$2,276	$2,791
Transfers from loans to other real estate	175	335
Sale and financing of other real estate	85	1,160
Cash dividends payable, preferred	113	338

See accompanying notes to unaudited condensed consolidated financial statements.

Notes to Unaudited Condensed Consolidated Financial Statements

1. Basis of Presentation and Nature of Operations

The condensed consolidated financial statements include the accounts of Farmers Capital Bank Corporation (the “Company” or “Parent Company”), a bank holding company, and its bank and nonbank subsidiaries. Bank subsidiaries include Farmers Bank & Capital Trust Company (“Farmers Bank”) in Frankfort, KY, United Bank & Trust Company (“United Bank”) in Versailles, KY, First Citizens Bank, Inc. (“First Citizens”) in Elizabethtown, KY, and Citizens Bank of Northern Kentucky, Inc. (“Citizens Northern”) in Newport, KY.

Farmers Bank’s significant subsidiaries include EG Properties, Inc., Leasing One Corporation (“Leasing One”), and Farmers Capital Insurance Corporation (“Farmers Insurance”). EG Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of Farmers Bank. Leasing One is a commercial leasing company in Frankfort, KY, and Farmers Insurance is an insurance agency in Frankfort, KY. United Bank has one wholly-owned subsidiary, EGT Properties, Inc. EGT Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of United Bank. First Citizens has one wholly-owned subsidiary, HBJ Properties, LLC. HBJ Properties, LLC is involved in real estate management and liquidation for certain repossessed properties of First Citizens. Citizens Northern has one wholly-owned subsidiary, ENKY Properties, Inc. ENKY Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of Citizens Northern.

The Company has two active nonbank subsidiaries, FCB Services, Inc. (“FCB Services”), and FFKT Insurance Services, Inc. (“FFKT Insurance”). FCB Services is a data processing subsidiary located in Frankfort, KY that provides services to the Company’s banks as well as unaffiliated entities. FFKT Insurance is a captive property and casualty insurance company insuring primarily deductible exposures and uncovered liability related to properties of the Company. The Company has three subsidiaries organized as Delaware statutory trusts that are not consolidated into its financial statements. These trusts were formed for the purpose of issuing trust preferred securities.

The Company provides financial services at its 36 locations in 23 communities throughout Central and Northern Kentucky to individual, business, agriculture, government, and educational customers. Its primary deposit products are checking, savings, and term certificate accounts. Its primary lending products are residential mortgage, commercial lending, and consumer installment loans. Substantially all loans are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Commercial loans and leases are expected to be repaid from cash flow from operations of businesses. Other services include, but are not limited to, cash management services, issuing letters of credit, safe deposit box rental, and providing funds transfer services. Other financial instruments, which potentially represent concentrations of credit risk, include deposit accounts in other financial institutions and federal funds sold.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates used in the preparation of the condensed financial statements are based on various factors including the current interest rate environment and the general strength of the local and state economy. Changes in the overall interest rate environment can significantly affect the Company's net interest income and the value of its recorded assets and liabilities. Actual results could differ from those estimates used in the preparation of the condensed financial statements. The allowance for loan losses, carrying value of other real estate owned, actuarial assumptions used to calculate postretirement benefits, and the fair values of financial instruments are estimates that are particularly subject to change.

The consolidated balance sheet as of December 31, 2014 has been derived from the audited financial statements of the Company as of that date. For further information, refer to the consolidated financial statements and footnotes thereto for the year ended December 31, 2014 included in the Company's annual report on Form 10-K. The accompanying condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X and do not include all of the information and the footnotes required by U.S. GAAP for complete statements. In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of such condensed financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year. All significant intercompany transactions and balances are eliminated in consolidation.

2. Reclassifications

Certain reclassifications have been made to the consolidated financial statements of prior periods to conform to the current period presentation. These reclassifications do not affect net income or total shareholders' equity as previously reported.

3. Accumulated Other Comprehensive Income

The following table presents changes in accumulated other comprehensive income by component, net of tax, for the periods indicated.

	Three Months Ended March 31, 2015			Three Months Ended March 31, 2014		
(In thousands)	Unrealized Gains and Losses on Available for Sale Investment Securities	Postretirement Benefit Obligation	Total	Unrealized Gains and Losses on Available for Sale Investment Securities	Postretirement Benefit Obligation	Total
Beginning balance	$5,174	$ (299)	$4,875	$(3,623)	$ 411	$(3,212)
Other comprehensive income (loss) before reclassifications	1,899	(1,251)	648	3,635	-	3,635
Amounts reclassified from accumulated other comprehensive income	(72)	15	(57)	51	23	74
Net current-period other comprehensive income (loss)	1,827	(1,236)	591	3,686	23	3,709
Ending balance	$7,001	$ (1,535)	$5,466	$63	$ 434	$497

The following table presents amounts reclassified out of accumulated other comprehensive income by component for the periods indicated. Line items in the statement of income affected by the reclassification are also presented.

(In thousands)	Amount Reclassified from Accumulated Other Comprehensive Income Three Months Ended March 31, 2015	Three Months Ended March 31, 2014	Affected Line Item in the Statement Where Net Income is Presented
Unrealized gains and losses on available for sale investment securities	$ 111	$ (78)	Investment securities gains, net
	(39)	27	Income tax expense
	$ 72	$ (51)	Net of tax
Amortization related to postretirement benefits			
Prior service costs	$ (13)	$ (52)	Salaries and employee benefits
Actuarial (losses) gains	(10)	17	Salaries and employee benefits
	(23)	(35)	Total before tax
	8	12	Income tax benefit
	$ (15)	$ (23)	Net of tax
Total reclassifications for the period	$ 57	$ (74)	Net of tax

4. Accounting Policy

Loans and Interest Income

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their unpaid principal amount outstanding adjusted for any charge-offs and deferred fees or costs on originated loans. Interest income on loans is recognized using the interest method based on loan principal amounts outstanding during the period. Interest income also includes amortization and accretion of any premiums or discounts over the expected life of acquired loans at the time of purchase or business acquisition. Loan origination fees, net of certain direct origination costs, are deferred and amortized as yield adjustments over the contractual term of the loans.

The Company disaggregates certain disclosure information related to loans, the related allowance for loan losses, and credit quality measures by either portfolio segment or by loan class. The Company segregates its loan portfolio segments based on similar risk characteristics as follows: real estate loans, commercial loans, and consumer loans. Portfolio segments are further disaggregated into classes for certain required disclosures as follows:

Portfolio Segment	Class
Real estate loans	Real estate mortgage – construction and land development
	Real estate mortgage – residential
	Real estate mortgage – farmland and other commercial enterprises
Commercial loans	Commercial and industrial
	Depository institutions
	Agriculture production and other loans to farmers
	States and political subdivisions
	Leases
	Other
Consumer loans	Secured
	Unsecured

The Company has a loan policy in place that is amended and approved from time to time as needed to reflect current economic conditions and product offerings in its markets. The policy establishes written procedures concerning areas such as the lending authorities of loan officers, committee review and approval of certain credit requests, underwriting criteria, policy exceptions, appraisal requirements, and loan review. Credit is extended to borrowers based primarily on their ability to repay as demonstrated by income and cash flow analysis.

Loans secured by real estate make up the largest segment of the Company’s loan portfolio. If a borrower fails to repay a loan secured by real estate, the Company may liquidate the collateral in order to satisfy the amount owed. Determining the value of real estate is a key component to the lending process for real estate backed loans. If the fair value of real estate (less estimated cost to sell) securing a collateral dependent loan declines below the outstanding loan amount, the Company will write down the carrying value of the loan and thereby incur a loss. The Company uses independent third party state certified or licensed appraisers in accordance with its loan policy to mitigate risk when underwriting real estate loans. Cash flow analysis of the borrower, loan to value limits as adopted by loan policy, and other customary underwriting standards are also in place which are designed to maximize credit quality and mitigate risks associated with real estate lending.

Commercial loans are made to businesses and are secured mainly by assets such as inventory, accounts receivable, machinery, fixtures and equipment, or other business assets. Commercial lending involves significant risk, as loan repayments are more dependent on the successful operation or management of the business and its cash flows. Consumer lending includes loans to individuals mainly for personal autos, boats, or a variety of other personal uses and may be secured or unsecured. Loan repayment associated with consumer loans is highly dependent upon the borrower’s continuing financial stability, which is heavily influenced by local unemployment rates. The Company mitigates its risk exposure to each of its loan segments by analyzing the borrower’s repayment capacity, imposing restrictions on the amount it will loan compared to estimated collateral values, limiting the payback periods, and following other customary underwriting practices as adopted in its loan policy.

The accrual of interest on loans is discontinued when it is determined that the collection of interest or principal is doubtful, or when a default of interest or principal has existed for 90 days or more, unless such loan is well secured and in the process of collection. Past due status is based on the contractual terms of the loan. Interest accrued but not received for a loan placed on nonaccrual status is reversed against interest income. Cash payments received on nonaccrual loans generally are applied to principal until qualifying for return to accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. The Company’s policy for placing a loan on nonaccrual status or subsequently returning a loan to accrual status does not differ based on its portfolio class or segment.

Commercial and real estate loans delinquent in excess of 120 days and consumer loans delinquent in excess of 180 days are charged off, unless the collateral securing the debt is of such value that any loss appears to be unlikely. In all cases, loans are charged off at an earlier date if classified as loss under the Company’s loan grading process or as a result of regulatory examination. The Company’s charge-off policy for impaired loans does not differ from the charge-off policy for loans outside the definition of impaired.

Provision and Allowance for Loan Losses

The provision for loan losses represents charges or credits made to earnings to maintain an allowance for loan losses at a level considered adequate to provide for probable incurred credit losses at the balance sheet date. The allowance for loan losses is a valuation allowance increased by the provision for loan losses and decreased by net charge-offs. Loan losses are charged against the allowance when management believes the uncollectibility of a loan is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The Company estimates the adequacy of the allowance using a risk-rated methodology which is based on the Company's past loan loss experience, known and inherent risks in the loan portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral securing loans, composition of the loan portfolio, current economic conditions, and other relevant factors. This evaluation is inherently subjective as it requires significant judgment and the use of estimates that may be susceptible to change.

The allowance for loan losses consists of specific and general components. The specific component relates to loans that are individually classified as impaired. The general component covers non-impaired loans and is based on historical loss experience adjusted for current risk factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off. Actual loan losses could differ significantly from the amounts estimated by management.

The general portion of the Company's loan portfolio is segregated into portfolio segments having similar risk characteristics identified as follows: real estate loans, commercial loans, and consumer loans. Each of these portfolio segments is assigned a loss percentage based on their respective sixteen quarter rolling historical loss rates, adjusted for the qualitative risk factors summarized below.

The qualitative risk factors used in the methodology are consistent with the guidance in the most recent Interagency Policy Statement on the Allowance for Loan Losses issued. Each factor is supported by a detailed analysis performed at each subsidiary bank and is both measureable and supportable. Some factors include a minimum allocation in some instances where loss levels are extremely low and it is determined to be prudent from a safety and soundness perspective. Qualitative risk factors that are used in the methodology include the following for each loan portfolio segment:

- Delinquency trends
- Trends in net charge-offs
- Trends in loan volume
- Lending philosophy risk
- Management experience risk
- Concentration of credit risk
- Economic conditions risk

A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

The Company accounts for impaired loans in accordance with Accounting Standards Codification ("ASC") Topic 310, *"Receivables."* ASC Topic 310 requires that impaired loans be measured at the present value of expected future cash flows, discounted at the loan's effective interest rate, at the loan's observable market price, or at the fair value of the collateral if the loan is collateral dependent. Impaired loans may also be classified as nonaccrual. In many circumstances, however, the Company continues to accrue interest on an impaired loan. Cash receipts on accruing impaired loans are applied to the recorded investment in the loan, including any accrued interest receivable. Cash payments received on nonaccrual impaired loans generally are applied to principal until qualifying for return to accrual status. Loans that are part of a large group of smaller-balance homogeneous loans, such as residential mortgage, consumer, and smaller-balance commercial loans, are collectively evaluated for impairment. Troubled debt restructurings are measured at the present value of estimated future cash flows using the loan's effective interest rate at inception, or at the fair value of collateral. The Company determines the amount of reserve for troubled debt restructurings that subsequently default in accordance with its accounting policy for the allowance for loan losses.

Recently Issued Accounting Standards

In January 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2015-01, *"Income Statement—Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items."* This ASU amends U.S. GAAP by removing the concept of extraordinary items, including deleting the definition of "extraordinary items" from the FASB Master Glossary. The revised guidance provides that the nature and financial effects of each event or transaction that is unusual in nature or occurs infrequently or both shall be presented as a separate component of income from continuing operations or, alternatively, disclosed in notes to the financial statements.

The amendments are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015, with early adoption permitted. A reporting entity may apply the amendments prospectively or retrospectively. The Company does not expect there to be a material impact on its consolidated financial position, results of operations, or cash flows upon adoption.

In April 2015, the FASB issued ASU No. 2015-03, *"Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs."* This ASU addresses balance sheet presentation requirements for debt issuance costs and debt discount and premiums. ASU No. 2015-03 requires that debt issuance costs related to a recognized debt liability be presented on the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This ASU is effective for financial statements issued for fiscal years beginning after December 15, 2015, and for interim periods within those fiscal years. The Company does not expect there to be a material impact on its consolidated financial position, results of operations, or cash flows upon adoption.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company's financial position, results of operations or cash flows.

5. Net Income Per Common Share

Basic net income per common share is determined by dividing net income available to common shareholders by the weighted average total number of common shares issued and outstanding. Net income available to common shareholders represents net income adjusted for preferred stock dividends including dividends declared, accretion of discounts on preferred stock issuances, and cumulative dividends related to the current dividend period that have not been declared as of the end of the period.

Diluted net income per common share is determined by dividing net income available to common shareholders by the total weighted average number of common shares issued and outstanding plus amounts representing the dilutive effect of stock options outstanding. The effects of stock options outstanding are excluded from the computation of diluted earnings per common share in periods in which the effect would be antidilutive. Dilutive potential common shares are calculated using the treasury stock method.

Net income per common share computations was as follows for the periods indicated.

	Three Months Ended March 31,	
(In thousands, except per share data)	2015	2014
Net income, basic and diluted	$4,074	$3,370
Less preferred stock dividends and discount accretion	225	537
Net income available to common shareholders, basic and diluted	$3,849	$2,833

Average common shares issued and outstanding, basic and diluted	7,490	7,479
Net income per common share, basic and diluted	$ .51	$ .38

Stock options for 20,049 shares of common stock were not included in the determination of diluted net income per common share for 2014 because they were antidilutive. All previous outstanding options expired during the fourth quarter of 2014.

6. Investment Securities

The following tables summarize the amortized costs and estimated fair value of the securities portfolio at March 31, 2015 and December 31, 2014. The summary is divided into available for sale and held to maturity investment securities.

March 31, 2015 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available For Sale				
Obligations of U.S. government-sponsored entities	$ 135,491	$ 539	$ 367	$ 135,663
Obligations of states and political subdivisions	139,835	2,944	282	142,497
Mortgage-backed securities – residential	343,541	8,993	620	351,914
Mortgage-backed securities – commercial	11,669	138	-	11,807
Corporate debt securities	6,881	26	526	6,381
Mutual funds and equity securities	849	4	77	776
Total securities – available for sale	$ 638,266	$ 12,644	$ 1,872	$ 649,038
Held To Maturity				
Obligations of states and political subdivisions	$ 3,715	$ 190	$ -	$ 3,905

December 31, 2014 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available For Sale				
Obligations of U.S. government-sponsored entities	$ 110,094	$ 369	$ 1,015	$ 109,448
Obligations of states and political subdivisions	133,563	2,600	397	135,766
Mortgage-backed securities – residential	363,729	7,959	1,199	370,489
Mortgage-backed securities – commercial	2,515	7	10	2,512
Corporate debt securities	6,639	26	358	6,307
Mutual funds and equity securities	1,889	2	25	1,866
Total securities – available for sale	$ 618,429	$ 10,963	$ 3,004	$ 626,388
Held To Maturity				
Obligations of states and political subdivisions	$ 3,728	$ 195	$ -	$ 3,923

The amortized cost and estimated fair value of the debt securities portfolio at March 31, 2015, by contractual maturity, are detailed below. The summary is divided into available for sale and held to maturity securities. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Mutual funds and equity securities in the available for sale portfolio consist of investments attributed to the Company’s captive insurance subsidiary. These securities have no stated maturity and are not included in the maturity schedule that follows.

Mortgage-backed securities are stated separately due to the nature of payment and prepayment characteristics of these securities, as principal is not due at a single date.

	Available For Sale		Held To Maturity	
March 31, 2015 (In thousands)	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$13,764	$13,797	$-	$ -
Due after one year through five years	154,900	156,299	-	-
Due after five years through ten years	98,195	99,409	705	787
Due after ten years	15,348	15,036	3,010	3,118
Mortgage-backed securities	355,210	363,721	-	-
Total	$637,417	$648,262	$3,715	$ 3,905

Gross realized gains and losses on the sale of available for sale investment securities were as follows:

(In thousands)	Three Months Ended March 31, 2015	2014
Gross realized gains	$130	$159
Gross realized losses	10	150
Net realized gain	$120	$9

Investment securities with unrealized losses at March 31, 2015 and December 31, 2014 not recognized in income are presented in the tables below. The tables segregate investment securities that have been in a continuous unrealized loss position for less than twelve months from those that have been in a continuous unrealized loss position for twelve months or more. The tables also include the fair value of the related securities.

	Less than 12 Months		12 Months or More		Total	
March 31, 2015 (In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. government-sponsored entities	$50,220	$ 184	$19,720	$ 183	$69,940	$ 367
Obligations of states and political subdivisions	25,634	175	8,103	107	33,737	282
Mortgage-backed securities – residential	39,182	160	23,363	460	62,545	620
Corporate debt securities	133	3	5,363	523	5,496	526
Mutual funds and equity securities	423	65	70	12	493	77
Total	$115,592	$ 587	$56,619	$ 1,285	$172,211	$ 1,872

	Less than 12 Months		12 Months or More		Total	
December 31, 2014 (In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. government-sponsored entities	$22,696	$ 76	$60,892	$ 939	$83,588	$ 1,015
Obligations of states and political subdivisions	20,746	81	21,272	316	42,018	397
Mortgage-backed securities – residential	37,451	82	71,311	1,117	108,762	1,199
Mortgage-backed securities – commercial	-	-	723	10	723	10
Corporate debt securities	76	4	5,525	354	5,601	358
Mutual funds and equity securities	305	11	95	14	400	25

Total	$81,274	$ 254	$159,818	$ 2,750	$241,092	$ 3,004

Unrealized losses included in the tables above have not been recognized in income since they have been identified as temporary. The Company evaluates investment securities for other-than-temporary impairment ("OTTI") at least quarterly, and more frequently when economic or market conditions warrant. Many factors are considered, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was effected by macroeconomic conditions, and (4) whether the Company has the intent to sell the security or more likely than not will be required to sell the security before its anticipated recovery. The assessment of whether an OTTI charge exists involves a high degree of subjectivity and judgment and is based on the information available to the Company at a point in time.

Corporate debt securities in the Company's investment securities portfolio at March 31, 2015 include single-issuer trust preferred capital securities with an unrealized loss of $523 thousand and a carrying value of $5.4 million. At year-end 2014, these securities had an unrealized loss of $354 thousand. These securities were issued by a national and global financial services firm and purchased by the Company during 2007. The securities are currently performing and continue to be rated as investment grade by major rating agencies. The issuer of the securities announced in the first quarter of 2015 an increase in per share common dividend payments and authorization of a common equity repurchase plan. The Company does not intend to sell these securities nor does the Company believe it is likely that it will be required to sell these securities prior to their anticipated recovery. The Company believes these securities are not impaired due to reasons of credit quality or other factors, but rather the unrealized loss is primarily attributed to continuing uncertainties in both international and domestic economies and market volatility. The Company believes that it will collect all amounts due according to the contractual terms of these securities and that the fair values of these securities will continue to recover as they approach their maturity dates.

The Company attributes the unrealized losses in other sectors of its investment securities portfolio to changes in market interest rates and volatility. Investment securities with unrealized losses at March 31, 2015 are performing according to their contractual terms, and the Company does not expect to incur a loss on these securities unless they are sold prior to maturity. The Company does not have the intent to sell these securities nor does it believe it is likely that it will be required to sell these securities prior to their anticipated recovery. The Company does not consider any of the securities to be impaired due to reasons of credit quality or other factors.

7. Loans and Allowance for Loan Losses

Major classifications of loans outstanding are summarized as follows:

(In thousands)	March 31, 2015	December 31, 2014
Real Estate		
Real estate mortgage – construction and land development	$96,805	$97,045
Real estate mortgage – residential	354,530	361,022
Real estate mortgage – farmland and other commercial enterprises	375,120	375,277
Commercial		
Commercial and industrial	53,085	47,112
States and political subdivisions	21,874	22,369
Lease financing	115	159
Other	13,147	15,547
Consumer		
Secured	7,516	7,963
Unsecured	5,198	5,450
Total loans	927,390	931,944

Less unearned income	1	1
Total loans, net of unearned income	$927,389	$931,943

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Activity in the allowance for loan losses by portfolio segment was as follows for the periods indicated.

Three months ended March 31, 2015

(In thousands)	Real Estate	Commercial	Consumer	Total
Balance, beginning of period	$12,542	$ 1,153	$ 273	$13,968
Provision for loan losses	(1,211)	(290)	(44)	(1,545)
Recoveries	286	16	37	339
Loans charged off	(95)	(13)	(48)	(156)
Balance, end of period	$11,522	$ 866	$ 218	$12,606

Three months ended March 31, 2014

(In thousands)	Real Estate	Commercial	Consumer	Total
Balance, beginning of period	$18,716	$ 1,409	$ 452	$20,577
Provision for loan losses	(756)	925	(37)	132
Recoveries	168	27	35	230
Loans charged off	(1,014)	(1,160)	(75)	(2,249)
Balance, end of period	$17,114	$ 1,201	$ 375	$18,690

The following tables present individually impaired loans by class of loans for the dates indicated.

March 31, 2015 (In thousands)	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Allowance for Loan Losses Allocated
Real Estate					
Real estate mortgage – construction and land development	$ 12,385	$ 6,436	$ 3,284	$ 9,720	$ 532
Real estate mortgage – residential	10,442	3,494	6,815	10,309	1,216
Real estate mortgage – farmland and other commercial enterprises	25,217	5,497	19,635	25,132	986
Commercial					
Commercial and industrial	391	327	64	391	64
Consumer					
Unsecured	22	-	22	22	22
Total	$48,457	$ 15,754	$ 29,820	$ 45,574	$ 2,820

December 31, 2014 (In thousands)	Unpaid Principal	Recorded Investment	Recorded Investment	Total Recorded	Allowance

	Balance	With No Allowance	With Allowance	Investment	for Loan Losses Allocated
Real Estate					
Real estate mortgage – construction and land development	$ 13,656	$ 6,902	$ 3,917	$ 10,819	$ 744
Real estate mortgage – residential	10,256	3,473	6,649	10,122	1,172
Real estate mortgage – farmland and other commercial enterprises	23,003	5,247	17,649	22,896	1,359
Commercial					
Commercial and industrial	93	22	71	93	71
Consumer					
Unsecured	25	-	25	25	25
Total	$ 47,033	$ 15,644	$ 28,311	$ 43,955	$ 3,371

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Three Months Ended March 31, 2015 (In thousands)	Average	Interest Income Recognized	Cash Basis Interest Recognized
Real Estate			
Real estate mortgage – construction and land development	$11,124	$ 81	$ 80
Real estate mortgage – residential	10,453	121	121
Real estate mortgage – farmland and other commercial enterprises	25,417	280	277
Commercial			
Commercial and industrial	435	1	1
Consumer			
Unsecured	24	-	-
Total	$47,453	$ 483	$ 479

Three Months Ended March 31, 2014 (In thousands)	Average	Interest Income Recognized	Cash Basis Interest Recognized
Real Estate			
Real estate mortgage – construction and land development	$15,623	$ 113	$ 111
Real estate mortgage – residential	11,713	115	109
Real estate mortgage – farmland and other commercial enterprises	34,193	254	244
Commercial			
Commercial and industrial	249	1	-
Consumer			
Secured	18	-	-
Unsecured	70	4	3
Total	$61,866	$ 487	$ 467

The following tables present the balance of the allowance for loan losses and the recorded investment in loans by portfolio segment based on impairment method as of March 31, 2015 and December 31, 2014.

March 31, 2015 (In thousands)	Real Estate	Commercial	Consumer	Total
Allowance for Loan Losses				
Ending allowance balance attributable to loans:				
Individually evaluated for impairment	$2,734	$ 64	$ 22	$2,820
Collectively evaluated for impairment	8,788	802	196	9,786
Total ending allowance balance	$11,522	$ 866	$ 218	$12,606
Loans				
Loans individually evaluated for impairment	$45,161	$ 391	$ 22	$45,574
Loans collectively evaluated for impairment	781,294	87,829	12,692	881,815

Total ending loan balance, net of unearned income	$826,455	$ 88,220	$ 12,714	$927,389

December 31, 2014 (In thousands)	Real Estate	Commercial	Consumer	Total
Allowance for Loan Losses				
Ending allowance balance attributable to loans:				
Individually evaluated for impairment	$3,275	$ 71	$ 25	$3,371
Collectively evaluated for impairment	9,267	1,082	248	10,597
Total ending allowance balance	$12,542	$ 1,153	$ 273	$13,968
Loans				
Loans individually evaluated for impairment	$43,837	$ 93	$ 25	$43,955
Loans collectively evaluated for impairment	789,507	85,093	13,388	887,988
Total ending loan balance, net of unearned income	$833,344	$ 85,186	$ 13,413	$931,943

The following tables present the recorded investment in nonperforming loans by class of loans as of March 31, 2015 and December 31, 2014.

March 31, 2015 (In thousands)	Nonaccrual	Restructured Loans	Loans Past Due 90 Days or More and Still Accruing
Real Estate			
Real estate mortgage – construction and land development	$ 3,165	$ 3,679	$ -
Real estate mortgage – residential	3,443	4,408	-
Real estate mortgage – farmland and other commercial enterprises	4,401	17,738	-
Commercial			
Commercial and industrial	76	-	-
Other	9	-	-
Consumer			
Secured	13	-	-
Unsecured	6	8	2
Total	$ 11,113	$ 25,833	$ 2

December 31, 2014 (In thousands)	Nonaccrual	Restructured Loans	Loans Past Due 90 Days or More and Still Accruing
Real Estate			
Real estate mortgage – construction and land development	$ 3,744	$ 3,742	$ -
Real estate mortgage – residential	3,474	4,674	-
Real estate mortgage – farmland and other commercial enterprises	4,202	16,004	-
Commercial			
Commercial and industrial	81	-	-
Other	7	-	-
Consumer			
Unsecured	-	9	-
Total	$ 11,508	$ 24,429	$ -

The Company has allocated $1.7 million and $2.2 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings and that are in compliance with those terms as of March 31, 2015 and December 31, 2014, respectively. The Company had no commitments to lend additional amounts to customers with outstanding loans that are classified as troubled debt restructurings at March 31, 2015 and December 31, 2014.

The Company had no credits during 2015 or 2014 that were modified as troubled debt restructurings. Troubled debt restructurings increased during the first quarter of 2015 resulting from the purchase of a previously-participated portion of a loan to a nonaffiliated bank. This loan was participated prior to it being restructured. The purchase price paid represented a discount of $428 thousand or 15% of the purchased principal amount. The loan is performing under the terms of the restructuring and the borrower's financial position has steadily improved. The discount is being accreted into interest income over the remaining four month contractual life ending in June 2015. The total outstanding balance related to this credit was $11.4 million at March 31, 2015. This represents 44.3% of the Company's total restructured loans and is the largest such individual credit. This credit was restructured in 2012 following an interest rate concession and extended amortization term.

The tables below present an age analysis of past due loans 30 days or more by class of loans as of the dates indicated. Past due loans that are also classified as nonaccrual are included in their respective past due category.

March 31, 2015 (In thousands)	30-89 Days Past Due	90 Days or More Past Due	Total	Current	Total Loans
Real Estate					
Real estate mortgage – construction and land development	$12	$272	$284	$96,521	$96,805
Real estate mortgage – residential	1,323	1,588	2,911	351,619	354,530
Real estate mortgage – farmland and other commercial enterprises	306	2,861	3,167	371,953	375,120
Commercial					
Commercial and industrial	21	13	34	53,051	53,085
States and political subdivisions	-	-	-	21,874	21,874
Lease financing, net	-	-	-	114	114
Other	9	-	9	13,138	13,147
Consumer					
Secured	34	-	34	7,482	7,516
Unsecured	21	8	29	5,169	5,198
Total	$1,726	$4,742	$6,468	$920,921	$927,389

December 31, 2014 (In thousands)	30-89 Days Past Due	90 Days or More Past Due	Total	Current	Total Loans
Real Estate					
Real estate mortgage – construction and land development	$-	$272	$272	$96,773	$97,045
Real estate mortgage – residential	1,395	1,595	2,990	358,032	361,022
Real estate mortgage – farmland and other commercial enterprises	75	3,484	3,559	371,718	375,277
Commercial					
Commercial and industrial	-	13	13	47,099	47,112
States and political subdivisions	-	-	-	22,369	22,369
Lease financing, net	-	-	-	158	158
Other	40	7	47	15,500	15,547
Consumer					
Secured	58	-	58	7,905	7,963
Unsecured	16	1	17	5,433	5,450

Total	$1,584	$5,372	$6,956	$924,987	$931,943

The Company categorizes 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 and conditions. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis includes large-balance loans and non-homogeneous loans, such as commercial real estate and certain residential real estate loans. Loan rating grades, as described further below, are assigned based on a continuous process. The amount and adequacy of the allowance for loan loss is determined on a quarterly basis. The Company uses the following definitions for its 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 borrower’s repayment ability, weaken the collateral or inadequately protect the Company’s credit position at some future date. These credits pose elevated risk, but their weaknesses do not yet justify a substandard classification.

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 Company will sustain some loss if the deficiencies are not corrected.

Doubtful. Loans classified as doubtful have all the weaknesses inherent of 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 meeting the criteria above which are analyzed individually as part of the above described process are considered to be pass rated loans and are considered to have a low risk of loss. Based on the most recent analysis performed, the risk category of loans by class of loans is as follows for the dates indicated. Each of the following tables excludes immaterial amounts attributed to accrued interest receivable.

March 31, 2015 (In thousands)	Real Estate			Commercial			
	Real Estate Mortgage -Construction and Land Development	Real Estate Mortgage-Residential	Real Estate Mortgage-Farmland and Other Commercial Enterprises	Commercial and Industrial	States and Political Subdivisions	Lease Financing	Other
Credit risk profile by internally assigned rating grades							
Pass	$80,171	$ 320,605	$ 327,347	$51,589	$ 21,874	$ 114	$13,123
Special Mention	4,085	15,244	28,999	1,006	-	-	-
Substandard	12,549	18,681	18,321	490	-	-	24
Doubtful	-	-	453	-	-	-	-
Total	$96,805	$ 354,530	$ 375,120	$53,085	$ 21,874	$ 114	$13,147

December 31, 2014 (In thousands)	Real Estate			Commercial			
	Real Estate Mortgage -Construction and Land Development	Real Estate Mortgage-Residential	Real Estate Mortgage-Farmland and Other Commercial Enterprises	Commercial and Industrial	States and Political Subdivisions	Lease Financing	Other
Credit risk profile by internally assigned rating grades							
Pass	$81,438	$ 326,124	$ 327,019	$45,665	$ 22,369	$ 158	$15,526

Special Mention	2,674	16,429	27,855	946	-	-	14
Substandard	12,933	18,469	19,941	501	-	-	7
Doubtful	-	-	462	-	-	-	-
Total	$97,045	$ 361,022	$ 375,277	$47,112	$ 22,369	$ 158	$15,547

The Company considers the performance of the loan portfolio and its impact on the allowance for loan losses. For consumer loan classes, the Company evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. The following table presents the consumer loans outstanding based on payment activity as of March 31, 2015 and December 31, 2014.

	March 31, 2015		December 31, 2014	
	Consumer		Consumer	
(In thousands)	Secured	Unsecured	Secured	Unsecured
Credit risk profile based on payment activity				
Performing	$7,503	$ 5,182	$7,963	$ 5,441
Nonperforming	13	16	-	9
Total	$7,516	$ 5,198	$7,963	$ 5,450

8. Other Real Estate Owned

Other real estate owned ("OREO") was as follows as of the date indicated:

(In thousands)	March 31, 2015	December 31, 2014
Construction and land development	$16,239	$ 17,628
Residential real estate	1,685	2,219
Farmland and other commercial enterprises	11,776	12,113
Total	$29,700	$ 31,960

OREO activity for the three months ended March 31, 2015 and 2014 was as follows:

Three months ended March 31, (In thousands)	2015	2014
Beginning balance	$31,960	$37,826
Transfers from loans and other increases	206	335
Proceeds from sales	(2,540)	(1,901)
Gain on sales, net	74	90
Write downs and other decreases, net	-	(906)
Ending balance	$29,700	$35,444

At March 31, 2015, the Company had a total of $1.4 million of loans secured by residential real estate mortgages that were in the process of foreclosure.

9. Postretirement Medical Benefits

The Company provides lifetime medical and dental benefits upon retirement for certain employees meeting the eligibility requirements as of December 31, 1989 ("Plan 1"). Additional participants are not eligible to be included in Plan 1 unless they met the requirements on this date. During 2003, the Company implemented an additional postretirement health insurance program ("Plan 2"). Under Plan 2, any employee meeting the service requirement of 20 years of full time service to the Company and is at least age 55 upon retirement is eligible to continue their health insurance coverage. Under both plans, retirees not yet eligible for Medicare have coverage identical to the coverage offered to active employees. Under both plans, Medicare-eligible retirees are provided with a Medicare Advantage plan. The Company pays 100% of the cost of Plan 1. The Company and the retirees each pay 50% of the cost under Plan 2. Both plans are unfunded.

The following disclosures of the net periodic benefit cost components of Plan 1 and Plan 2 were measured at January 1, 2015 and 2014.

Three months ended March 31, (In thousands)	2015	2014
Service cost	$185	$121
Interest cost	162	143
Recognized prior service cost	13	52
Recognized net actuarial loss (gain)	10	(17)
Net periodic benefit cost	$370	$299

The Company expects benefit payments of $359 thousand for 2015, of which $71 thousand have been made during the first three months of 2015.

10. Regulatory Matters

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

In July 2013, U.S. banking regulators adopted final rules related to standards on bank capital adequacy and liquidity (commonly referred to "Basel III"). The new rules were effective for the Company beginning on January 1, 2015, subject to a phase-in period for certain provisions extending through January 1, 2019. The rules include a new common equity Tier 1 capital ratio, an increase to the minimum Tier 1 capital ratio, an increase to risk-weightings of certain assets, implementation of a new capital conservation buffer in excess of the required minimum (which is set to be phased in beginning in 2016), and changes to how regulatory capital is defined. The Company and each of its bank subsidiaries meet the minimum capital ratios and a fully phased-in capital conservation buffer under the new rules.

The regulatory ratios of the consolidated Company and its subsidiary banks were as follows for the dates indicated.

	March 31, 2015				December 31, 2014			
	Common Equity Tier 1 Risk-based Capital[1]	Tier 1 Risk-based Capital[1]	Total Risk-based Capital[1]	Tier 1 Leverage[2]	Common Equity Tier 1 Risk-based Capital[1]	Tier 1 Risk-based Capital[1]	Total Risk-based Capital[1]	Tier 1 Leverage[2]
Consolidated	14.48 %	19.62 %	20.75 %	12.12 %	N/A	19.75 %	21.00 %	12.04 %
Farmers Bank	17.33	17.33	18.25	9.48	N/A	17.71	18.70	9.40
United Bank	19.04	19.04	20.29	11.92	N/A	18.00	19.26	11.08
First Citizens	14.61	14.61	15.24	10.09	N/A	13.66	14.30	9.44
Citizens Northern	14.14	14.14	15.39	9.72	N/A	14.46	15.71	10.11

[1]Common Equity Tier 1 Risked-based, Tier 1 Risk-based, and Total Risk-based Capital ratios are computed by dividing a bank's Common Equity Tier 1, Tier 1 or Total Capital, as defined by regulation, by a risk-weighted sum of the bank's assets, with the risk weighting determined by general standards established by regulation. The safest assets (e.g., government obligations) are assigned a weighting of 0% with riskier assets receiving higher ratings (e.g., ordinary commercial loans are assigned a weighting of 100%).

[2]Tier 1 Leverage ratio is computed by dividing a bank's Tier 1 Capital, as defined by regulation, by its total quarterly average assets.

N/A – Not applicable.

On May 5, 2015, the Company announced that it received approval from its banking regulators to repurchase the final 10,000 shares of its remaining outstanding Series A preferred stock. The Company will redeem the preferred shares at the stated liquidation value of $1,000 per share, plus any accrued dividends. The timing of the repurchase is expected to occur during the second quarter of 2015. The total redemption amount will be $10.0 million, plus accrued dividends at 9.0% per share.

The Company originally issued 30,000 shares of its Series A preferred stock in 2009. The current action will be the third and final partial redemption of the original shares issued. No additional debt or equity was issued in connection with the previous redemptions. Likewise, none will be issued in connection with the current redemption.

Summary of Regulatory Agreements

The Company has one subsidiary bank, Citizens Northern, which is currently under an agreement with its primary banking regulators. This agreement is summarized below.

Citizens Northern

The Federal Deposit Insurance Corporation ("FDIC") and Kentucky Department of Financial Institutions ("KDFI") entered into a Memorandum of Understanding ("Memorandum") with Citizens Northern in September 2010. The Memorandum was terminated and updated in July 2013. The updated Memorandum contains many of the same provisions included in the terminated Memorandum, with a new requirement that Citizens Northern maintain a Tier 1 leverage ratio at or above 9.0%. In addition, the updated Memorandum requires having and retaining qualified management in the areas of loan administration and collection. It also requires Citizens Northern to address credit underwriting and administration weaknesses identified in the most recent examination of the bank by the FDIC and KDFI.

Other parts of the regulatory order include the development and documentation of plans for reducing problem loans, providing progress reports on compliance with the Memorandum, and for the development and implementation of a written profit plan and strategic plans. It also restricts the bank from extending additional credit to borrowers with credits classified as substandard, doubtful or special mention in the report of examination.

Regulators continue to monitor the Company's progress and compliance with the regulatory agreement through periodic on-site examinations, regular communications, and quarterly data analysis. The Company believes it is adequately addressing all issues of the regulatory agreement. However, only the regulatory agencies can determine if compliance with the agreement has been met. The Company believes that Citizens Northern is in compliance with the requirements identified in its regulatory agreement as of March 31, 2015.

The Parent Company maintains cash available to fund a certain amount of additional injections of capital to its bank subsidiaries as determined by management or if required by its regulators. If needed, further amounts in excess of available cash may be funded by future public or private sales of securities, although the Parent Company is currently under no directive by its regulators to raise any additional capital.

11. Fair Value Measurements

ASC Topic 820, *"Fair Value Measurements and Disclosures,"* defines fair value, establishes a framework for measuring fair value, and sets forth disclosures about fair value measurements. ASC Topic 825, *"Financial Instruments,"* allows entities to choose to measure certain financial assets and liabilities at fair value. The Company has not elected the fair value option for any of its financial assets or liabilities.

ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. It also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. This Topic describes three levels of inputs that may be used to measure fair value:

Level 1:	Quoted prices for identical assets or liabilities in active markets that the entity has the ability to access at 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 for substantially the full term of the assets or liabilities.
Level 3:	Significant unobservable inputs that reflect a reporting entity's own assumptions supported by little or no market activity, about the assumptions that market participants would use in pricing the asset or liability.

Following is a description of the valuation method used for financial instruments measured at fair value on a recurring basis. For this disclosure, the Company only has available for sale investment securities that meet the requirement.

Available for sale investment securities

Valued primarily by independent third party pricing services under the market valuation approach that include, but are not limited to, the following inputs:

Mutual funds and equity securities are priced utilizing real-time data feeds from active market exchanges for identical securities and are considered Level 1 inputs.

Government-sponsored agency debt securities, obligations of states and political subdivisions, mortgage-backed securities, corporate bonds, and other similar investment securities are priced with available market information through processes using benchmark yields, matrix pricing, prepayment speeds, cash flows, live trading data, and market spreads sourced from new issues, dealer quotes, and trade prices, among others sources and are considered Level 2 inputs.

Available for sale investment securities are the Company's only balance sheet item that meets the disclosure requirements for instruments measured at fair value on a recurring basis. Disclosures as of March 31, 2015 and December 31, 2014 are as follows:

(In thousands) Available For Sale Investment Securities	Fair Value	Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
March 31, 2015				
Obligations of U.S. government-sponsored entities	$135,663	$-	$ 135,663	$ -
Obligations of states and political subdivisions	142,497	-	142,497	-
Mortgage-backed securities – residential	351,914	-	351,914	-
Mortgage-backed securities – commercial	11,807	-	11,807	-
Corporate debt securities	6,381	-	6,381	-
Mutual funds and equity securities	776	776	-	-
Total	$649,038	$776	$ 648,262	$ -

(In thousands) Available For Sale Investment Securities	Fair Value	Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2014				
Obligations of U.S. government-sponsored entities	$109,448	$-	$ 109,448	$ -
Obligations of states and political subdivisions	135,766	-	135,766	-
Mortgage-backed securities – residential	370,489	-	370,489	-
Mortgage-backed securities – commercial	2,512	-	2,512	-
Corporate debt securities	6,307	-	6,307	-
Mutual funds and equity securities	1,866	1,866	-	-
Total	$626,388	$1,866	$ 624,522	$ -

The Company is required to measure and disclose certain other assets and liabilities at fair value on a nonrecurring basis in periods following their initial recognition. The Company's disclosure about assets and liabilities measured at fair value on a nonrecurring basis consists of impaired loans and OREO. The carrying value of these assets are adjusted to fair value on a nonrecurring basis through impairment charges as described more fully below.

Impairment charges on collateral-dependent loans are recorded by either an increase to the provision for loan losses and related allowance or by direct loan charge-offs. The fair value of collateral-dependent impaired loans with specific allocations of the allowance for loan losses is measured based on recent appraisals of the underlying collateral. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Appraisers take absorption rates into consideration and adjustments are routinely made in the appraisal process to identify differences between the comparable sales and income data available. Such adjustments consist mainly of estimated costs to sell that are not included in certain appraisals or to update appraised collateral values as a result of market declines of similar properties for which a newer appraisal is available. These adjustments can be significant and typically result in a Level 3 classification of the inputs for determining fair value.

OREO includes properties acquired by the Company through, or in lieu of, actual loan foreclosures and is carried at fair value less estimated costs to sell. Fair value of OREO at acquisition is generally based on third party appraisals of the property that includes comparable sales data and is considered as Level 3 inputs. The carrying value of each OREO property is updated at least annually and more frequently when market conditions significantly impact the value of the property. If the carrying amount of the OREO exceeds fair value less estimated costs to sell, an impairment loss is recorded through noninterest expense.

The following table represents the carrying amount of assets measured at fair value on a nonrecurring basis and still held by the Company as of the dates indicated. The amounts in the table only represent assets whose carrying amount has been adjusted by impairment charges during the period in a manner as described above; therefore, these amounts will differ from the total amounts outstanding. Collateral-dependent impaired loan amounts in the tables below exclude restructured loans since they are measured based on present value techniques, which are outside the scope of the fair value reporting framework.

(In thousands)		Fair Value Measurements Using		
Description	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
March 31, 2015				
Collateral-dependent Impaired Loans				
Real estate mortgage – residential	$ 177	$ -	$ -	$ 177
Real estate mortgage – farmland and other commercial enterprises	242	-	-	242
Total	$ 419	$ -	$ -	$ 419
OREO				
Total	$ -	$ -	$ -	$ -

(In thousands)		Fair Value Measurements Using		
Description	Fair Value	Quoted Prices in Active Markets	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)

		for Identical Assets (Level 1)		
December 31, 2014				
Collateral-dependent Impaired Loans				
Real estate mortgage - construction and land development	$284	$-	$ -	$ 284
Real estate mortgage - residential	946	-	-	946
Real estate mortgage - farmland and other commercial enterprises	340	-	-	340
Total	$1,570	$-	$ -	$ 1,570
OREO				
Construction and land development	$8,123	$-	$ -	$ 8,123
Residential real estate	863	-	-	863
Farmland and other commercial enterprises	5,459	-	-	5,459
Total	$14,445	$-	$ -	$ 14,445

The following table represents impairment charges recorded in earnings for the periods indicated on assets measured at fair value on a nonrecurring basis.

(In thousands)		
Three months ended March 31,	2015	2014
Impairment charges:		
Collateral-dependent impaired loans	$ 49	$ 940
OREO	-	906
Total	$ 49	$ 1,846

The following table presents quantitative information about unobservable inputs for assets measured on a nonrecurring basis using Level 3 measurements. As described above, the fair value of real estate securing collateral-dependent impaired loans and OREO are based on current third party appraisals. It is often necessary, however, for the Company to discount the appraisal amounts supporting its impaired loans and OREO. These discounts relate primarily to marketing and other holding costs that are not included in certain appraisals or to update values as a result of market declines of similar properties for which newer appraisals are available. Discounts also result from contracts to sell properties entered into during the period. The range of discounts is presented in the table below for 2015.

(In thousands)	Fair Value at March 31, 2015	Valuation Technique	Unobservable Inputs	Range		Average	
Collateral-dependent impaired loans	$ 419	Discounted appraisals	Marketability discount	0%-10.0	%	8.3	%
OREO	$ -	Discounted appraisals	Marketability discount	-	%	-	%

Fair Value of Financial Instruments

The table that follows represents the estimated fair values of the Company’s financial instruments made in accordance with the requirements of ASC Topic 825, *“Financial Instruments.”* ASC Topic 825 requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet for which it is practicable to estimate that value. The estimated fair value amounts have been determined by the Company using available market information and present value or other valuation techniques. These derived fair values are subjective in nature, involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. ASC Topic 825 excludes certain financial instruments and all nonfinancial instruments from the disclosure requirements. Accordingly, the aggregate fair value amounts presented are not intended to represent the underlying value of the Company.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments not presented elsewhere for which it is practicable to estimate that value.

Cash and Cash Equivalents, Accrued Interest Receivable, and Accrued Interest Payable

The carrying amount is a reasonable estimate of fair value due to the relatively short time between the origination of the instrument and its expected realization or settlement.

Investment Securities Held to Maturity

Fair value is based on quoted market price, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities or with available market information through processes using benchmark yields, matrix pricing, prepayment speeds, cash flows, live trading data, and market spreads sourced from new issues, dealer quotes, and trade prices, among others sources.

Loans

The fair value of loans is estimated by discounting expected future cash flows using current discount rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. Expected future cash flows are projected based on contractual cash flows adjusted for estimated prepayments.

Federal Home Loan Bank and Federal Reserve Bank Stock

It is not practical to determine the fair value of Federal Home Loan Bank and Federal Reserve Bank stock due to restrictions placed on its transferability.

Deposit Liabilities

The fair value of demand deposits, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date and fair value approximates carrying value. The fair value of fixed maturity certificates of deposit is estimated by discounting the expected future cash flows using the rates currently offered for certificates of deposit with similar remaining maturities.

Federal Funds Purchased and Other Short-term Borrowings

The carrying amount is the estimated fair value for these borrowings which reprice frequently in the near term.

Securities Sold Under Agreements to Repurchase, Subordinated Notes Payable, and Other Long-term Borrowings

The fair value of these borrowings is estimated by discounting the expected future cash flows using rates currently available for debt with similar terms and remaining maturities. For subordinated notes payable, the Company uses its best estimate to determine an appropriate discount rate since active markets for similar debt transactions are very limited.

Commitments to Extend Credit and Standby Letters of Credit

Pricing of these financial instruments is based on the credit quality and relationship, fees, interest rates, probability of funding, compensating balance, and other covenants or requirements. Loan commitments generally have fixed expiration dates, variable interest rates and contain termination and other clauses that provide for relief from funding in the event there is a significant deterioration in the credit quality of the customer. Many loan commitments are expected to, and typically do, expire without being drawn upon. The rates and terms of the Company's commitments to lend and standby letters of credit are competitive with others in the various markets in which the Company operates. There are no unamortized fees relating to these financial instruments, as such the carrying value and fair value are both zero.

The following table presents the estimated fair values of the Company's financial instruments and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2015 and December 31, 2014. Information for available for sale investment securities is presented within this footnote in greater detail above.

			Fair Value Measurements Using		
(In thousands)	Carrying Amount	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
March 31, 2015					
Assets					
Cash and cash equivalents	$118,848	$118,848	$118,848	$ -	$ -
Held to maturity investment securities	3,715	3,905	-	3,905	-
Loans, net	914,783	917,747	-	-	917,747
Accrued interest receivable	5,361	5,361	-	5,361	-
Federal Home Loan Bank and Federal Reserve Bank Stock	9,368	N/A	-	-	-
Liabilities					
Deposits	1,416,376	1,417,528	1,041,526	-	376,002
Federal funds purchased and other short-term borrowings	26,383	26,383	-	26,383	-
Securities sold under agreements to repurchase and other long-term borrowings	119,690	129,110	-	129,110	-
Subordinated notes payable to unconsolidated trusts	48,970	22,471	-	-	22,471
Accrued interest payable	885	885	-	885	-
December 31, 2014					
Assets					
Cash and cash equivalents	$100,914	$100,914	$100,914	$ -	$ -
Held to maturity investment securities	3,728	3,923	-	3,923	-
Loans, net	917,975	918,697	-	-	918,697
Accrued interest receivable	5,625	5,625	-	5,625	-
Federal Home Loan Bank and Federal Reserve Bank Stock	9,368	N/A	-	-	-
Liabilities					
Deposits	1,387,161	1,388,614	991,630	-	396,984
Federal funds purchased and other short-term borrowings	28,590	28,590	-	28,590	-
Securities sold under agreements to repurchase and other long-term borrowings	119,724	129,244	-	129,244	-

Subordinated notes payable to unconsolidated trusts	48,970	22,594	-	-	22,594
Accrued interest payable	944	944	-	944	-

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements with the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), under the Private Securities Litigation Reform Act of 1995 that involve risks and uncertainties. Statements in this report that are not statements of historical fact are forward-looking statements. In general, forward-looking statements relate to a discussion of future financial results or projections, future economic performance, future operational plans and objectives, and statements regarding the underlying assumptions of such statements. Although management of Farmers Capital Bank Corporation (the "Company" or "Parent Company") believes that the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate, and therefore, there can be no assurance that the forward-looking statements included herein will prove to be accurate.

Various risks and uncertainties may cause actual results to differ materially from those indicated by the Company's forward-looking statements. In addition to the risks described under Part 1, Item 1A *"Risk Factors"* in the Company's most recent annual report on Form 10-K, factors that could cause actual results to differ from the results discussed in the forward-looking statements include, but are not limited to: economic conditions (both generally and more specifically in the markets in which the Company and its subsidiaries operate) and lower interest margins; competition for the Company's customers from other providers of financial services; deposit outflows or reduced demand for financial services and loan products; government legislation, regulation, and changes in monetary and fiscal policies (which changes from time to time and over which the Company has no control); changes in interest rates; changes in prepayment speeds of loans or investment securities; trends in the provision and allowance for loan losses; inflation; material unforeseen changes in the liquidity, results of operations, or financial condition of the Company's customers; changes in the level of non-performing assets and charge-offs; changes in the number of common shares outstanding; the capability of the Company to successfully enter into a definitive agreement for and close anticipated transactions; unexpected claims or litigation against the Company; expected insurance or other recoveries; technological or operational difficulties; the impact of new accounting pronouncements and changes in policies and practices that may be adopted by regulatory agencies; acts of war or terrorism; the ability of the Parent Company to receive dividends from its subsidiaries; the impact of larger or similar financial institutions encountering difficulties, which may adversely affect the banking industry or the Company; the Company or its subsidiary banks' ability to maintain required capital levels and adequate funding sources and liquidity; and other risks or uncertainties detailed in the Company's filings with the Securities and Exchange Commission, all of which are difficult to predict and many of which are beyond the control of the Company.

The Company's forward-looking statements are based on information available at the time such statements are made. The Company expressly disclaims any intent or obligation to update any forward-looking statements to reflect changes in underlying assumptions or factors, new information, future events, or other changes.

RESULTS OF OPERATIONS

First Quarter 2015 Compared to First Quarter 2014

The Company reported net income of $4.1 million for the quarter ended March 31, 2015, an increase of $704 thousand or 20.9% compared with net income of $3.4 million for the first quarter of 2014. On a per common share basis, net income was $.51 and $.38 for the current and year-ago quarters, respectively. This represents an increase of $.13 or 34.2%. Selected income statement amounts and related data are summarized in the table below.

(In thousands except per share data)

Three Months Ended March 31,	2015	2014	Increase (Decrease)
Interest income	$15,220	$16,374	$ (1,154)
Interest expense	2,217	2,695	(478)
Net interest income	13,003	13,679	(676)
Provision for loan losses	(1,545)	132	(1,677)
Net interest income after provision for loan losses	14,548	13,547	1,001
Noninterest income	5,441	5,373	68
Noninterest expenses	14,510	14,430	80
Income before income taxes	5,479	4,490	989
Income tax expense	1,405	1,120	285
Net income	4,074	3,370	704
Less preferred stock dividends and discount accretion	225	537	(312)
Net income available to common shareholders	$3,849	$2,833	$ 1,016
Basic and diluted net income per common share	$.51	$.38	$ .13
Weighted average common shares outstanding – basic and diluted	7,490	7,479	11
Return on average assets	.91 %	.75 %	16 bp
Return on average equity	9.39 %	7.77 %	162 bp

bp – basis points.

The $704 thousand increase in net income is attributed primarily to a lower provision for loan losses of $1.7 million and lower net other real estate expense of $1.0 million or 96%. Salaries and employee benefits increased $969 thousand and net interest income decreased $676 thousand or 4.9%. The $.13 increase in net income per common share was boosted $.04 by a decrease in preferred stock dividends related to share redemptions. Further information related to the more significant components making up the increase in net income follows.

Net Interest Income

The overall interest rate environment at March 31, 2015, as measured by the Treasury yield curve, remains at very low levels when compared with historical trends. Since year-end 2014, yields for the three and six-month maturities were relatively unchanged, while the two and three-year maturities decreased 13 and 22 basis points, respectively. Yields on longer-term maturities declined 26 and 22 basis points for the ten and thirty-year maturity periods, respectively. At March 31, 2015, the short-term federal funds target interest rate remained between zero and 0.25%, unchanged since December 2008. The Federal Reserve Board ("Federal Reserve") has indicated that it will be appropriate to raise the federal funds target interest rate when it sees further improvement in the labor market and is reasonably confident that inflation will return to its two percent objective over the medium term. At March 31, 2015, the national and Kentucky unemployment rate was 5.5% and 5.1%, respectively. However, labor force participation rates remain near 30-year lows. The national inflation rate at March 31, 2015 was minus 0.07%.

Net interest income was $13.0 million for the first three months of 2015, a decrease of $676 thousand or 4.9% compared to $13.7 million a year earlier. The decrease in net interest income was driven by a decrease in interest income of $1.2 million or 7.0%, which exceeded a decline in interest expense of $478 thousand or 17.7%. Interest income on loans and investment securities decreased $926 thousand or 7.3% and $253 thousand or 6.8%, respectively. Interest expense on deposits decreased $382 thousand or 31.8% and interest on borrowed funds declined $96 thousand or 6.4%.

The decrease to interest income on loans resulted from a decline in average balances outstanding. The average rate on loans was unchanged in the comparison. The decrease in loan volume has been accelerated by early payoffs of several larger balance credits that were refinanced by competitors with terms below the Company's underwriting standards. In recent years, the Company has focused on strengthening its credit underwriting standards, which has improved the overall credit quality of the loan portfolio.

Interest income on investment securities is down due mainly to lower rates, partially offset by higher volume. In periods when quality loan demand is low, available funds are invested in lower yielding investment securities or cash equivalents, or otherwise used to manage liquidity, such as for deposit outflows or for the repayment of long-term debt. Average investment securities for the quarter increased $30.6 million or 4.9% from a year ago.

The decrease in interest expense on deposits was driven by rate declines and lower average outstanding balances. Overall declines in interest income on loans and interest paid on deposits are the result of a slow growing economy and related low interest rate environment, competitive pressures, and the Company's strategy of being more selective in pricing its loans and deposits. The goal of this strategy is to improve credit quality, net interest income, overall profitability, and the capital position.

The Company is generally earning and paying less interest from its earning assets and funding sources as the average rates earned and paid have decreased. This includes repricing of variable and floating rate assets and liabilities that have reset to overall lower amounts since their previous repricing date as well as activity related to new earning assets and funding sources in a low interest rate environment. The Company continues to reprice its higher-rate maturing time deposits downward to lower market rates or allowing them to mature without renewal, as liquidity has been adequate.

The net interest margin on a taxable equivalent basis was 3.25% for the current quarter, a decrease of 16 basis points compared with 3.41% a year earlier. Net interest spread decreased 16 basis points to 3.09% compared to 3.25% a year ago. The Company expects its net interest margin to remain relatively flat in the near term according to internal modeling using expectations about future market interest rates, the maturity structure of the Company's earning assets and liabilities, and other factors. Future results could be significantly different than current expectations.

The following tables present an analysis of net interest income for the quarterly periods ended March 31.

Distribution of Assets, Liabilities and Shareholders' Equity: Interest Rates and Interest Differential

Three Months Ended March 31,	2015				2014			
(In thousands)	Average Balance	Interest	Average Rate		Average Balance	Interest	Average Rate	
Earning Assets								
Investment securities								
Taxable	$527,342	$2,795	2.15	%	$507,013	$3,080	2.46	%
Nontaxable[1]	126,044	977	3.14		115,787	926	3.24	
Interest bearing deposits in banks, federal funds sold and securities purchased under agreements to resell	100,876	53	.21		56,091	28	.20	
Loans[1,2,3]	923,420	11,816	5.19		994,050	12,727	5.19	
Total earning assets	1,677,682	$15,641	3.78	%	1,672,941	$16,761	4.06	%
Allowance for loan losses	(13,791)				(19,598)			
Total earning assets, net of allowance for loan losses	1,663,891				1,653,343			
Nonearning Assets								
Cash and due from banks	23,642				23,297			
Premises and equipment, net	34,709				36,172			
Other assets	87,318				99,824			
Total assets	$1,809,560				$1,812,636			
Interest Bearing Liabilities								
Deposits								
Interest bearing demand	$347,014	$50	.06	%	$322,969	$50	.06	%
Savings	376,058	116	.13		349,485	158	.18	
Time	386,143	655	.69		462,656	995	.87	
Federal funds purchased and other short-term borrowings	28,871	10	.14		33,753	19	.23	
Securities sold under agreements to repurchase and other long-term borrowings	167,907	1,386	3.35		176,070	1,473	3.39	
Total interest bearing liabilities	1,305,993	$2,217	.69	%	1,344,933	$2,695	.81	%
Noninterest Bearing Liabilities								
Demand deposits	301,129				266,939			
Other liabilities	26,465				24,878			
Total liabilities	1,633,587				1,636,750			
Shareholders' equity	175,973				175,886			
Total liabilities and shareholders' equity	$1,809,560				$1,812,636			
Net interest income		13,424				14,066		
TE basis adjustment		(421)				(387)		
Net interest income		$13,003				$13,679		
Net interest spread			3.09	%			3.25	%
Impact of noninterest bearing sources of funds			.16				.16	

Net interest margin	3.25	%	3.41	%

[1]Income and yield stated at a fully tax equivalent basis using the marginal corporate Federal tax rate of 35%.

[2]Loan balances include principal balances on nonaccrual loans.

[3]Loan fees included in interest income amounted to $269 thousand and $239 thousand in 2015 and 2014, respectively.

Analysis of Changes in Net Interest Income (tax equivalent basis)

(In thousands)	Variance	Variance Attributed to	
Three Months Ended March 31,	2015/2014[1]	Volume	Rate
Interest Income			
Taxable investment securities	$ (285)	$690	$(975)
Nontaxable investment securities[2]	51	210	(159)
Interest bearing deposits in banks, federal funds sold and securities purchased under agreements to resell	25	23	2
Loans[2]	(911)	(911)	-
Total interest income	(1,120)	12	(1,132)
Interest Expense			
Interest bearing demand deposits	-	-	-
Savings deposits	(42)	66	(108)
Time deposits	(340)	(151)	(189)
Federal funds purchased and other short-term borrowings	(9)	(2)	(7)
Securities sold under agreements to repurchase and other long-term borrowings	(87)	(69)	(18)
Total interest expense	(478)	(156)	(322)
Net interest income	$ (642)	$168	$(810)
Percentage change	100.0 %	(26.2)%	126.2 %

[1]The changes that are not solely due to rate or volume are allocated on a percentage basis using the absolute values of rate and volume variances as a basis for allocation.

[2]Income stated at fully tax equivalent basis using the marginal corporate Federal tax rate of 35%.

Provision for Loan Losses

The provision for loan losses represents charges or credits to earnings that are necessary to maintain an allowance for loan losses at an adequate level to cover credit losses specifically identified in the loan portfolio, as well as management's best estimate of incurred probable loan losses in the remainder of the portfolio at the balance sheet date. The credit quality of the Company's loan portfolio continues to improve, as certain credit quality metrics are at or near recent quarterly bests.

The Company recorded a credit to the provision for loan losses in the amount of $1.5 million for the first quarter of 2015 compared to a provision expense of $132 thousand for the first quarter of 2014. The allowance for loan losses as a percentage of outstanding loans was 1.36% at March 31, 2015 compared to 1.50% and 1.90% at year-end 2014 and March 31, 2014, respectively. The decrease in the provision for loan losses is attributed to continuing improvement in the credit quality of the loan portfolio and a decline in outstanding loans. The Company recorded net recoveries of $183 thousand in the current quarter compared with net charge-offs of $2.0 million a year ago. Loan charge-offs for the first quarter of 2014 include $1.0 million related to a group of fraudulent loans and $755 thousand related to one credit secured by commercial real estate.

Nonperforming and watch list loans declined when compared with a year earlier. Historical loss rates have also improved as lower recent charge-off activity has replaced the higher levels experienced in the early part of the Company's rolling quarterly four year look-back period used when evaluating the allowance for loan losses. For further information about improvements in the Company's overall credit quality, please refer to the discussion under the captions *"Allowance for Loan Losses"* and *"Nonperforming Loans"* that follows.

Noninterest Income

The components of noninterest income are as follows for the periods indicated:

Three Months Ended March 31, (In thousands)	2015	2014	Increase (Decrease)	%
Service charges and fees on deposits	$1,772	$1,916	$ (144)	(7.5)%
Allotment processing fees	1,190	1,245	(55)	(4.4)
Other service charges, commissions, and fees	1,267	1,235	32	2.6
Trust income	571	545	26	4.8
Investment securities gains, net	120	9	111	NM
Gain on sale of mortgage loans, net	165	97	68	70.1
Income from company-owned life insurance	241	246	(5)	(2.0)
Other	115	80	35	43.5
Total noninterest income	$5,441	$5,373	$ 68	1.3 %

NM – not meaningful.

Noninterest income was relatively unchanged in the comparison. The more significant components that changed include higher net gains on the sale of investment securities, higher net gains on the sale of loans, and lower service charge and fees on deposits. The increase in net gains on the sale of investment securities is attributed to normal asset/liability management strategies which result in periodic sales at irregular intervals based on current strategies. Net gains on the sale of loans for the first quarter of 2014 included $92 thousand of nonrecurring losses, $46 thousand related to a group of loans reclassified from held for sale to held for investment and $46 thousand related to a group of mortgage loans sold. Service charges and fees on deposits decreased primarily due to lower overdraft fees of $153 thousand or 13.8% due to lower volume.

Noninterest Expense

The components of noninterest expense are as follows for the periods indicated:

Three Months Ended March 31, (In thousands)	2015	2014	Increase (Decrease)	%
Salaries and employee benefits	$8,320	$7,351	$ 969	13.2 %
Occupancy expenses, net	1,227	1,282	(55)	(4.3)
Equipment expenses	618	594	24	4.0
Data processing and communication expenses	1,055	1,005	50	5.0
Bank franchise tax	605	612	(7)	(1.1)
Amortization of intangibles	112	101	11	10.9

Deposit insurance expenses	400	440	(40)	(9.1)
Other real estate expenses, net	45	1,064	(1,019)	(95.8)
Legal expenses	212	194	18	9.3
Other	1,916	1,787	129	7.2
Total noninterest expense	$14,510	$14,430	$ 80	.6 %

Noninterest expense was relatively unchanged in the comparison. The more significant components that changed include higher salaries and employee benefits expense and lower expenses related to repossessed real estate. The increase in salaries and employee benefits is attributed to higher benefit expenses of $600 thousand or 49.3% and higher salaries and related payroll taxes of $371 thousand or 6.1%. The increase in benefit expense is attributed mainly to higher claims related to the Company's self-funded health insurance plan and, to a lesser degree, an increase in the actuary-determined postretirement benefit expense. The Company had 508 full time equivalent employees at quarter-end, relatively unchanged from a year ago. The decrease in repossessed real estate expenses is primarily the result of impairment charges of $906 thousand recorded in the first quarter of 2014. There were no impairment charges for the current quarter. Expenses related to development, operating, and maintenance of repossessed properties decreased $129 thousand or 52.0%.

Income Taxes

Income tax expense was $1.4 million for the first quarter of 2015, an increase of $285 thousand or 25.4% compared to $1.1 million for the first quarter of 2014. The effective income tax rates were 25.6% and 24.9% for the current and year-ago quarters, respectively.

FINANCIAL CONDITION

Total assets were $1.8 billion at March 31, 2015, an increase of $32.7 million or 1.8% from year-end 2014. Investment securities and cash and cash equivalents increased $22.6 million or 3.6% and $17.9 million or 17.8%, respectively. Loans and other real estate owned (“OREO”) decreased $4.6 million or 0.5% and $2.3 million or 7.1%, respectively.

Cash and cash equivalents and investment securities remain elevated as a result of the Company’s overall net funding position and a lack of high quality loan demand. The fair market value adjustment related to investment securities in the available for sale portfolio increased $2.8 million during the quarter due mainly to favorable changes in market interest rates, primarily on longer dated maturities. Generating high quality loan demand remains a challenge, and the decrease in outstanding loans has been accelerated by early payoffs of several larger balance credits. OREO decreased primarily due to property sales, which outpaced new additions.

Total liabilities were $1.6 billion at March 31, 2015, an increase of $28.2 million or 1.8% compared to December 31, 2014. The increase in total liabilities is mainly attributed to a $29.2 million or 2.1% increase in total deposits, primarily from savings and interest bearing demand deposits. Short-term borrowings decreased $2.2 million or 7.7%. Long-term borrowings were unchanged at $169 million.

Shareholders’ equity was $177 million at March 31, 2015, an increase of $4.5 million or 2.6% compared to $173 million at year-end 2014. The increase in shareholders’ equity was primarily due to net income of $4.1 million and other comprehensive income of $591 thousand. The increase in other comprehensive income was driven by an increase in the after-tax unrealized gain related to the available for sale investment securities portfolio of $1.8 million, partially offset by a $1.2 million decline in the after-tax amount related to the Company’s liability for postretirement medical benefits plan.

Selected balance sheet amounts and related data are presented in the table below and discussion that follows.

(Dollars in thousands, except per share data)	March 31, 2015	December 31, 2014	Increase (Decrease)	%
Cash and cash equivalents	$118,848	$100,914	$ 17,934	17.8 %
Investment securities	652,753	630,116	22,637	3.6
Loans, net of allowance of $12,606 and $13,968	914,783	917,975	(3,192)	(0.3)
Other real estate owned	29,700	31,960	(2,260)	(7.1)
Other assets	99,254	101,641	(2,387)	(2.3)
Total assets	$1,815,338	$1,782,606	$ 32,732	1.8 %
Deposits	$1,416,376	$1,387,161	$ 29,215	2.1 %
Federal funds purchased and other short-term borrowings	26,383	28,590	(2,207)	(7.7)
Other borrowings	168,660	168,694	(34)	-
Other liabilities	26,494	25,232	1,262	5.0
Total liabilities	1,637,913	1,609,677	28,236	1.8
Preferred stock	10,000	10,000	-	-
Common stock	936	936	-	-
Capital surplus	51,400	51,344	56	.1
Retained earnings	109,623	105,774	3,849	3.6
Accumulated other comprehensive income (loss)	5,466	4,875	591	12.1
Total shareholders' equity	177,425	172,929	4,496	2.6
Total liabilities and shareholders' equity	$1,815,338	$1,782,606	$ 32,732	1.8 %
End of period tangible book value per common share[1]	$22.30	$21.69	$ .61	2.8 %
End of period per common share closing price	23.25	23.29	(.04)	(.2)

[1]Represents total common equity less intangible assets divided by the number of common shares outstanding at the end of the period.

Temporary Investments

Temporary investments consist of interest bearing deposits in other banks, federal funds sold and securities purchased under agreements to resell, and money market mutual funds. The Company uses these funds in the management of liquidity and interest rate sensitivity or as a short-term holding prior to subsequent movement into other investments with higher yields or for other purposes. At March 31, 2015, temporary investments were $97.0 million, an increase of $22.9 million or 30.9% from year-end 2014.

Investment Securities

The investment securities portfolio is comprised primarily of residential mortgage-backed securities, tax-exempt securities of states and political subdivisions, and debt securities issued by U.S. government-sponsored agencies. Substantially all of the Company's investment securities are designated as available for sale. Proceeds received from maturing or called investment securities not needed to fund higher-earning loans are either reinvested in similar investments or used to manage liquidity, such as for deposit outflows or other payment obligations. Total investment securities had a carrying amount of $653 million at March 31, 2015, an increase of $22.6 million or 3.6% compared to $630 million at year-end 2014.

The increase in investment securities was driven by net purchases totaling $20.8 million and an increase in the market value adjustment related to the available for sale portfolio of $2.8 million, partially offset by net premium amortization of $1.1 million. The increase in the value of the available for sale securities portfolio is attributed to higher bond prices related to longer term maturity periods. Yields for the five, ten and 30-year Treasury securities each declined during the first three months of 2015. Generally, as market interest rates decrease, the value of fixed rate investments increases.

Investment securities include single-issuer trust preferred capital securities of a U.S. based global financial services firm. The amortized cost and estimated fair value of this investment at March 31, 2015 was $5.9 million and $5.4 million, respectively. This represents a decrease in fair value of $162 thousand or 2.9% compared to $5.5 million at year-end 2014.

The Company's investment in the single-issuer trust preferred capital securities continues to perform according to contractual terms and the issuer of these securities is rated as investment grade by major rating agencies. The issuer of the securities announced in the first quarter of 2015 an increase in per share common dividend payments and authorization of a common equity repurchase plan. The Company does not intend to sell these securities nor does the Company believe it is likely that it will be required to sell these securities prior to their anticipated recovery. The Company believes these securities are not impaired due to reasons of credit quality or other factors, but rather the unrealized loss is primarily attributed to continuing uncertainties in both international and domestic economies and market volatility. The Company believes that it will collect all amounts due according to the contractual terms of these securities and that the fair values of these securities will continue to recover as they approach their maturity dates.

Loans

Loans were $927 million at March 31, 2015, a decrease of $4.6 million or 0.5% compared to year-end 2014. High quality loan demand remains weak, and the Company continues a measured and cautious approach to loan originations while working to further reduce its level of nonperforming assets in a slow growth economy. Generating high quality loan demand continues to be a challenge, and the decrease in outstanding loans has been accelerated by early payoffs of several larger balance credits. Early payoffs include five larger credits ranging between $1.2 million to $4.2 million, which were refinanced by competitors with terms below the Company's underwriting standards. Loan payments include $884 thousand related to nonaccrual loans during the quarter.

The composition of the loan portfolio is summarized in the table below.

	March 31, 2015		December 31, 2014	
(Dollars in thousands)	Amount	%	Amount	%
Real estate mortgage – construction and land development	$96,805	10.4 %	$97,045	10.4 %
Real estate mortgage – residential	354,530	38.2	361,022	38.7
Real estate mortgage – farmland and other commercial enterprises	375,120	40.5	375,277	40.3
Commercial, financial, and agriculture	88,106	9.5	85,028	9.1
Installment	12,714	1.4	13,413	1.5
Lease financing	114	-	158	-
Total	$927,389	100.0%	$931,943	100.0%

On an average basis, loans represented 55.0% of earning assets for the first three months of 2015, a decrease of 326 basis points compared to 58.3% for the year 2014. The decrease in the level of loans as a percentage of earning assets reflects the overall lack of high quality loan demand which the Company desires. As loan demand changes, available funds are reallocated between temporary investments or investment securities, which typically involve a decrease in credit risk and result in lower yields.

Allowance for Loan Losses

The allowance for loan losses is maintained at a level believed to be adequate by management to cover probable losses in the loan portfolio. The calculation of the appropriate level of allowance for loan losses requires significant judgment in order to reflect credit losses specifically identified in the Company’s loan portfolio as well as management's best estimate of probable incurred credit losses in the loan portfolio at the balance sheet date. The allowance for loan losses is a valuation allowance increased by the provision for loan losses and decreased by net charge-offs. Loan losses are charged against the allowance when management believes the uncollectibility of a loan is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses and the related provision for loan losses generally fluctuate as the relative level of nonperforming and impaired loans vary. However, other factors impact the amount of the allowance for loan losses such as the Company’s historical loss experience, the borrowers’ financial condition, general economic conditions, and other risk factors as described in greater detail in the Company’s most recent annual report on Form 10-K.

The allowance for loan losses was $12.6 million or 1.36% of outstanding loans at March 31, 2015. This compares to $14.0 million or 1.50% of net loans outstanding at year-end 2014. The decrease in the allowance as a percentage of net loans outstanding from the prior year-end is resulted primarily from a credit to the provision for loan losses of $1.5 million. As a percentage of nonperforming loans, the allowance for loan losses was 34.1% at March 31, 2015 compared to 38.9% at year-end 2014. The relatively low amount of the allowance for loan losses as a percentage of nonperforming loans is due mainly to the makeup of nonperforming loans.

Nonperforming loans include $25.8 million of accruing restructured loans representing 70% of total nonperforming loans at the end of the quarter. At year-end 2014, this amount was $24.4 million or 68%. The allowance attributed to credits that are restructured with lower interest rates generally represents the difference in the present value of future cash flows calculated at the loan's original effective interest rate and the new lower rate. This typically results in a reserve for loan losses that is less severe than for other loans that are collateral dependent. The allowance specifically allocated to impaired loans, which includes restructured loans, was $2.8 million or 6.2% and $3.4 million or 7.7% of such loans at quarter-end and year-end, respectively. As a percentage of nonaccrual loans and loans past due 90 days or more and still accruing, the allowance for loan losses was 113% and 121% for the current quarter and year-end 2014, respectively.

The overall improvement in the credit quality of the loan portfolio experienced during 2014 continued during the first three months of 2015. Certain credit quality measures are summarized in the table that follows for the periods indicated. Several of these measures are at the best level in the last three years.

(In thousands)	March 31, 2015	December 31, 2014	March 31, 2014	Three-year High[1]	Three-year Low[1]
Nonperforming loans	$36,948	$35,937	$51,098	$72,167	$35,937
Nonaccrual loans	11,113	11,508	24,720	54,598	11,113
Loans past due 30-89 days and still accruing	1,357	1,352	2,465	11,940	1,352
Loans graded substandard or below	50,518	52,313	76,852	126,503	50,518
Impaired loans	45,574	43,955	58,460	92,228	43,955
Loans, net of unearned income	927,389	931,943	983,919	1,040,439	927,389

[1]Based on quarter-end balances over the previous three years.

Nonperforming Loans

Nonperforming loans consist of nonaccrual loans, accruing restructured loans, and loans 90 days or more past due and still accruing interest. The accrual of interest on loans is discontinued when it is determined that the collection of interest or principal is doubtful, or when a default of interest or principal has existed for 90 days or more, unless such loan is well secured and in the process of collection. Restructured loans occur when a lender, because of economic or legal reasons related to a borrower's financial difficulty, grants a concession to the borrower that it would not otherwise consider. Restructured loans typically include a reduction of the stated interest rate or an extension of the maturity date, among other possible concessions. The Company gives careful consideration to identifying which of its challenged credits merit a restructuring of terms that it believes will result in maximum loan repayments and mitigate possible losses. Cash flow projections are carefully scrutinized prior to restructuring any credits; past due credits are typically not granted concessions.

Nonperforming loans were $36.9 million at March 31, 2015, an increase of $1.0 million or 2.8% compared to $35.9 million at year-end 2014. Restructured loans were up $1.4 million or 5.7%, which was partially offset by a decrease in nonaccrual loans of $395 thousand or 3.4%. Accruing restructured loans make up $25.8 million or 70% of the Company's nonperforming loans at March 31, 2015 compared with $11.1 million or 30% related to nonaccrual loans. Nonaccrual loans have decreased to the lowest level since the third quarter of 2007. Nonperforming loans, presented by class, were as follows for the periods indicated.

Nonperforming Loans

(In thousands)	March 31, 2015	December 31, 2014
Nonaccrual Loans		
Real Estate		
Real estate mortgage – construction and land development	$3,165	$3,744
Real estate mortgage – residential	3,443	3,474
Real estate mortgage – farmland and other commercial enterprises	4,401	4,202
Commercial		
Commercial and industrial	76	81
Other	9	7
Consumer		
Secured	13	-
Unsecured	6	-
Total nonaccrual loans	$11,113	$11,508
Restructured Loans		
Real Estate		
Real estate mortgage – construction and land development	$3,679	$3,742
Real estate mortgage – residential	4,408	4,674
Real estate mortgage – farmland and other commercial enterprises	17,738	16,004
Consumer		
Unsecured	8	9
Total restructured loans	$25,833	$24,429
Past Due 90 Days or More and Still Accruing		
Consumer		
Unsecured	$2	$ -
Total past due 90 days or more and still accruing	$2	$ -
Total nonperforming loans	$36,948	$35,937
Ratio of total nonperforming loans to total loans	4.0 %	3.9 %

The most significant components of nonperforming loans include nonaccrual and restructured loans. Activity during 2015 related to these two components was as follows:

(In thousands)	Nonaccrual Loans	Restructured Loans
Balance at December 31, 2014	$ 11,508	$ 24,429
Additions	762	2,740
Principal paydowns	(884)	(1,336)
Transfers to other real estate owned/other foreclosed assets	(175)	-
Charge-offs	(98)	-

Balance at March 31, 2015	$ 11,113	$ 25,833

The Company's comprehensive risk-grading and loan review program includes a review of loans to assess risk and assign a grade to those loans, a review of delinquencies, and an assessment of loans for needed charge-offs or placement on nonaccrual status. The Company had loans in the amount of $62.4 million and $64.7 million at March 31, 2015 and year-end 2014, respectively, which were performing but considered potential problem loans and are not included in the nonperforming loan totals in the table above. These loans, however, are considered in establishing an appropriate allowance for loan losses. The balance outstanding for potential problem credits is mainly attributed to lingering weaknesses in the overall economy which continue to strain many of the Company's customers. Potential problem loans include a variety of borrowers and are secured primarily by various types of real estate including commercial, construction properties, and residential real estate developments. At March 31, 2015, the five largest potential problem credits were $13.8 million in the aggregate compared to $13.9 million at year-end 2014.

Potential problem loans are identified on the Company's watch list and consist of loans that require close monitoring by management. Credits may be considered as a potential problem loan for reasons that are temporary or correctable, such as for a deficiency in loan documentation or absence of current financial statements of the borrower. Potential problem loans may also include credits where adverse circumstances are identified that may affect the borrower's ability to comply with the contractual terms of the loan. Other factors which might indicate the existence of a potential problem loan include the delinquency of a scheduled loan payment, deterioration in a borrower's financial condition identified in a review of periodic financial statements, a decrease in the value of the collateral securing the loan, or a change in the economic environment in which the borrower operates. Certain loans on the Company's watch list are also considered impaired and specific allowances related to these loans are established in accordance with the appropriate accounting guidance.

Other Real Estate

OREO includes real estate properties acquired by the Company through, or in lieu of, actual foreclosure. At March 31, 2015, OREO was $29.7 million, a decrease of $2.3 million or 7.1% compared to $32.0 million at year-end 2014. The decrease was driven by sales activity, including one larger-balance residential real estate development property that sold for $986 thousand and one larger-balance residential real estate property that sold for $525 thousand. OREO has declined $22.9 million or 43.5% from its peak of $52.6 million, which occurred at year-end 2012. A summary of OREO activity for 2015 follows.

(In thousands)	Amount
Balance at December 31, 2014	$31,960
Transfers from loans and other increases	206
Proceeds from sales	(2,540)
Net gain on sales	74
Balance at March 31, 2015	$29,700

Deposits

A summary of the Company's deposits are as follows for the periods indicated.

	End of Period			Average		
(In thousands)	March 31, 2015	December 31, 2014	Increase (Decrease)	Three Months March 31, 2015	Twelve Months December 31, 2014	Increase (Decrease)
Noninterest Bearing	$305,232	$292,788	$ 12,444	$301,129	$281,025	$ 20,104

Interest Bearing						
Demand	353,498	335,657	17,841	347,014	320,947	26,067
Savings	382,796	363,185	19,611	376,058	357,156	18,902
Time	374,850	395,531	(20,681)	386,143	433,756	(47,613)
Total interest bearing	1,111,144	1,094,373	16,771	1,109,215	1,111,859	(2,644)
Total Deposits	$1,416,376	$1,387,161	$29,215	$1,410,344	$1,392,884	$17,460

The increase in total end of period deposits was driven by higher savings deposit and interest bearing demand deposits of $19.6 million or 5.4% and $17.8 million or 5.3%, respectively. Noninterest bearing deposit balances increased $12.4 million or 4.3% and time deposits decreased $20.7 million or 5.2%. The decrease in time deposits is a result of the Company's overall high liquidity position and a strategy to lower overall funding costs, mainly by allowing higher-rate certificates of deposit to roll off or reprice at lower interest rates. Many of those balances have been rolled into interest and noninterest bearing demand accounts or savings accounts by the customer. As rates have decreased throughout the deposit portfolio, many customers have opted to transfer funds from maturing time deposits or investments from other sources into short-term demand or savings accounts. The Company has not sought out or accepted brokered deposits in the past nor does it have plans to do so in the future.

Borrowed Funds

Total borrowed funds were $195 million at March 31, 2015, a decrease of $2.2 million or 1.1% from year-end 2014. The decrease in borrowed funds was driven by a $2.2 million or 7.7% decrease in short-term borrowings. The decrease is attributed to a decline in repurchase agreements with commercial depositors in the normal course of business. Short-term borrowings primarily represent funds that have been swept out of the deposit accounts of certain qualifying commercial customers into repurchase agreements and accounted for as secured borrowings by the Company. Long-term borrowings were unchanged at $169 million.

LIQUIDITY

The primary source of funds for the Parent Company is the receipt of dividends from its subsidiary banks, balances of cash and cash equivalents maintained, and borrowings from nonaffiliated sources. Payment of dividends by the Company’s subsidiary banks is subject to certain regulatory restrictions as set forth in national and state banking laws and regulations. Furthermore Citizens Bank of Northern Kentucky, Inc. (“Citizens Northern”) must obtain regulatory approval to declare or pay dividends to the Parent Company in connection with a prior regulatory agreement. Capital ratios at each of the Company’s four subsidiary banks exceed regulatory established “well-capitalized” status at March 31, 2015 under the prompt corrective action regulatory framework; however, Citizens Northern is required to maintain capital ratios at a higher level as outlined in its regulatory agreement. The capital ratios at Citizens Northern exceeded the required higher amounts at March 31, 2015.

The Parent Company’s primary uses of cash include the payment of dividends to its preferred and common shareholders, injecting capital into subsidiaries, paying interest expense on borrowings, and payments for general operating expenses. The Company is no longer required to receive permission from its banking regulators to make interest payments on its trust preferred securities or to pay dividends on its common and preferred stock. However, the Company’s current goal is to redeem all of its outstanding preferred stock before considering the payment of a dividend on its common stock. The Company redeemed 20,000 shares, or two-thirds, of its outstanding preferred stock during 2014. On May 5, 2015, the Company announced that it received approval from its banking regulators to redeem the final 10,000 outstanding shares. The Company expects to complete the redemption during the second quarter of 2015.

The Parent Company had cash and cash equivalents of $32.0 million and $32.1 million at March 31, 2015 and year-end 2014, respectively. Significant cash receipts of the Parent Company for 2015 include a return of capital from a nonbank subsidiary of $855 thousand and management fees from subsidiaries of $609 thousand. Significant cash payments by the Parent Company in 2015 include $800 thousand for salaries, payroll taxes, and employee benefits, $225 thousand for the payment of dividends on outstanding preferred stock, and $210 thousand for the payment of interest expense on subordinated notes payable.

The Company's objective as it relates to liquidity is to ensure that its subsidiary banks have funds available to meet deposit withdrawals and credit demands without unduly penalizing profitability. In order to maintain a proper level of liquidity, the subsidiary banks have several sources of funds available on a daily basis. For assets, those sources of funds include liquid assets that are readily marketable or that can be pledged, or which mature in the near future. These assets primarily include cash and due from banks, federal funds sold, investment securities, and cash flow generated by the repayment of principal and interest on loans and investment securities. For liabilities, sources of funds primarily include the subsidiary banks' core deposits, Federal Home Loan Bank (“FHLB”) and other borrowings, and federal funds purchased and securities sold under agreements to repurchase. While maturities and scheduled amortization of loans and investment securities are generally a predictable source of funds, deposit outflows and mortgage prepayments are influenced significantly by general interest rates, economic conditions, and competition in our local markets.

As of March 31, 2015, the Company had $227 million of additional borrowing capacity under various FHLB, federal funds, and other borrowing agreements. However, there is no guarantee that these sources of funds will continue to be available to the Company, or that current borrowings can be refinanced upon maturity, although the Company is not aware of any events or uncertainties that are likely to cause a decrease in the Company’s liquidity from these sources. The Company’s borrowing capacity was $224 million at year-end 2014.

For the longer term, the liquidity position is managed by balancing the maturity structure of the balance sheet. This process allows for an orderly flow of funds over an extended period of time. The Company’s Asset and Liability Management Committee, both at the bank subsidiary level and on a consolidated basis, meets regularly and monitors the composition of the balance sheet to ensure comprehensive management of interest rate risk and liquidity.

Liquid assets consist of cash and cash equivalents and available for sale investment securities. At March 31, 2015, consolidated liquid assets were $768 million, up $40.6 million or 5.6% compared to $727 million at year-end 2014. The Company's liquidity position remains elevated mainly as a result of the Company's overall net funding position and weak, high-quality loan demand. The overall funding position of the Company changes as loan demand, deposit levels, and other sources and uses of funds fluctuate.

Net cash provided by operating activities was $5.5 million and $11.2 million for the first three months of 2015 and 2014, respectively. This represents a decrease of $5.7 million or 51.2%, led by a decrease in proceeds from the sale of mortgage loans of $3.4 million. Net cash flow used in investing activities was $14.3 million for 2015 compared with net inflows of $18.6 million for 2014. This represents a change of $32.9 million and was driven by investment securities and loan activity. The Company had net cash outflows of $20.8 million related to investment securities for 2015 compared with net cash inflows of $6.7 million in the year-ago period. Net cash outflows for the current period represent purchases in excess of proceeds from the sale, maturity, and call of investment securities. For loans, net repayments were $4.4 million for 2015, down $7.2 million or 61.9% compared to $11.6 million a year ago. During 2015, excess funds, primarily from deposits, have been used more to purchase investment securities as high quality loan demand remains low.

Net cash provided by financing activities was $26.8 million for the first three months of 2015 compared with a net use of cash of $3.1 million for the comparable period a year earlier. The change was driven primarily by deposit activity. For 2015, deposits increased $29.2 million or 2.1% compared with a decrease of $983 thousand for 2014. Net repayments on short-term borrowings were $2.2 million and $1.7 million for 2015 and 2014, respectively.

Commitments to extend credit are entered into with customers in the ordinary course of providing traditional banking services and are considered in addressing the Company's liquidity management. The Company does not expect these commitments to significantly affect the liquidity position in future periods. The Company has not entered into any contracts for financial derivative instruments such as futures, swaps, options, or similar instruments.

CAPITAL RESOURCES

Shareholders' equity was $177 million at March 31, 2015, an increase of $4.5 million or 2.6% compared to $173 million at year-end 2014. The increase in shareholders' equity was driven by net income of $4.1 million and higher other comprehensive income of $591 thousand, partially offset by dividends on preferred stock of $225 thousand. Other comprehensive income includes an increase of $1.8 million related to the after-tax amount in the unrealized gain on available for sale investment securities, partially offset by a decrease of $1.2 million attributed to the after-tax amount related to the Company's liability for postretirement medical benefits plan. The increase in the unrealized gain on available for sale investment securities correlates to a general decline in long term market interest rates. As market interest rates fall, the value of fixed rate investments increases. The decrease related to postretirement medical benefits reflects changes in actuarial assumptions attributed to plan valuation.

On January 9, 2009, the Company issued 30,000 shares of Series A, no par value cumulative perpetual preferred stock. The Company redeemed 20,000 of the preferred shares during 2014. On May 5, 2015, the Company announced that it received approval from its banking regulators to redeem the final 10,000 outstanding shares. The Company expects to complete the redemption during the second quarter of 2015.

At March 31, 2015, the Company's tangible capital ratio was 9.76%, an increase of eight basis points compared to 9.68% at year-end 2014. The tangible capital ratio represents tangible equity as a percentage of tangible assets, which excludes intangible assets. Tangible common equity to tangible assets, which further excludes outstanding preferred stock, was 9.21% and 9.12% at March 31, 2015 and year-end 2014, respectively. This represents an increase of nine basis points in the comparison.

In July 2013, U.S. banking regulators adopted final rules related to standards on bank capital adequacy and liquidity (commonly referred to as "Basel III"). The new rules were effective for the Company beginning on January 1, 2015, subject to a phase-in period for certain provisions extending through January 1, 2019. The rules include a new common equity Tier 1 capital ratio, an increase to the minimum Tier 1 capital ratio, an increase to risk-weightings of certain assets, implementation of a new capital conservation buffer in excess of the required minimum (which is set to be phased in beginning in 2016), and changes to how regulatory capital is defined. The Company and each of its bank subsidiaries meet the minimum capital ratios and a fully phased-in capital conservation buffer under the new rules.

Consistent with the objective of operating a sound financial organization, the Company's goal is to maintain capital ratios well above the regulatory minimum requirements. The capital ratios of the Company and its subsidiary banks are presented in the following table for the dates indicated.

	March 31, 2015				December 31, 2014			
	Common Equity Tier 1 Risk-based Capital[1]	Tier 1 Risk-based Capital[1]	Total Risk-based Capital[1]	Tier 1 Leverage[2]	Common Equity Tier 1 Risk-based Capital[1]	Tier 1 Risk-based Capital[1]	Total Risk-based Capital[1]	Tier 1 Leverage[2]
Consolidated	14.48 %	19.62 %	20.75 %	12.12 %	N/A	19.75 %	21.00 %	12.04 %
Farmers Bank & Capital Trust Company	17.33	17.33	18.25	9.48	N/A	17.71	18.70	9.40
United Bank & Trust Company	19.04	19.04	20.29	11.92	N/A	18.00	19.26	11.08
First Citizens Bank, Inc.	14.61	14.61	15.24	10.09	N/A	13.66	14.30	9.44
Citizens Northern[3]	14.14	14.14	15.39	9.72	N/A	14.46	15.71	10.11
Regulatory minimum	4.50	6.00	8.00	4.00	N/A	4.00	8.00	4.00
Well-capitalized status	6.50	8.00	10.00	5.00	N/A	6.00	10.00	5.00

[1]Common Equity Tier 1 Risked-based, Tier 1 Risk-based, and Total Risk-based Capital ratios are computed by dividing a bank's Common Equity Tier 1, Tier 1 or Total Capital, as defined by regulation, by a risk-weighted sum of the bank's assets, with the risk weighting determined by general standards established by regulation. The safest assets (e.g., government obligations) are assigned a weighting of 0% with riskier assets receiving higher ratings (e.g., ordinary commercial loans are assigned a weighting of 100%).

[2]Tier 1 Leverage ratio is computed by dividing a bank's Tier 1 Capital, as defined by regulation, by its total quarterly average assets.

[3]See Note 10 to the Company's unaudited condensed consolidated financial statements included as part of this Form 10-Q for minimum capital ratios required as part of the banks regulatory agreement.

N/A – Not applicable.

Regulatory Agreements

Citizens Northern is party to a supervisory agreement with its primary banking regulator. This agreement is summarized in Note 10 to the unaudited condensed consolidated financial statements of this Form 10-Q. The agreement is discussed in significantly greater detail in the Company's Annual Report on Form 10-K for the year ended December 31, 2014 under the caption *"Capital Resources"* in Item 7, *"Management's Discussion and Analysis of Financial Condition and Results of Operations."*

There have been no changes to the regulatory agreement at Citizens Northern in 2015. The Company believes it is adequately addressing all issues of the regulatory agreement to which it is subject and is in compliance with the agreement. However, only the regulatory agencies can determine if compliance with the applicable regulatory agreements have been met. Regulators continue to monitor the Company's progress and compliance with the regulatory agreement through periodic on-site examinations, regular communications, and quarterly data analysis. The results of these examinations and communications show satisfactory progress toward meeting the requirements included in the regulatory agreement.

The agreement entered into during 2009 between the United Bank & Trust Company and its primarily regulators was terminated during the first quarter 2015 as a result of continued satisfactory compliance.

The Parent Company maintains cash available to fund a certain amount of additional injections of capital to its bank subsidiaries if necessary. If needed, further amounts in excess of available cash may be funded by future public or private sales of securities, although the Parent Company is currently under no directive by its regulators to raise any additional capital.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company uses a simulation model as a tool to monitor and evaluate interest rate risk exposure. The model is designed to measure the sensitivity of net interest income and net income to changing interest rates over future time periods. Forecasting net interest income and its sensitivity to changes in interest rates requires the Company to make assumptions about the volume and characteristics of many attributes, including assumptions relating to the replacement of maturing earning assets and liabilities. Other assumptions include, but are not limited to, projected prepayments, projected new volume, and the predicted relationship between changes in market interest rates and changes in customer account balances. These effects are combined with the Company’s estimate of the most likely rate environment to produce a forecast of net interest income and net income. The forecasted results are then adjusted for the effect of a gradual increase and decrease in market interest rates on the Company’s net interest income and net income. Because assumptions are inherently uncertain, the model cannot precisely estimate net interest income and net income or the effect of interest rate changes on net interest income and net income. Actual results could differ significantly from simulated results.

At March 31, 2015, the model indicated that if rates were to gradually increase by 150 basis points during the remainder of the calendar year, then net interest income and net income would decrease 0.01% and 0.2%, respectively for the year ending December 31, 2015 when compared to the forecasted results for the most likely rate environment. The model indicated that if rates were to gradually decrease by 150 basis points over the same period, then net interest income and net income would decrease 1.2% and 3.1%, respectively.

Item 4. Controls and Procedures

The Company’s Chief Executive Officer and Chief Financial Officer have reviewed and evaluated the effectiveness of the Company’s disclosure controls and procedures as of the end of the period covered by this report, and have concluded that the Company’s disclosure controls and procedures were adequate and effective to ensure that all material information required to be disclosed in this report has been made known to them in a timely fashion.

The Company’s Chief Executive Officer and Chief Financial Officer have also concluded that there were no significant changes during the quarter ended March 31, 2015 in the Company’s internal control over financial reporting or in other factors that have materially affected, or are reasonably likely to materially affect, the registrant’s internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

As of March 31, 2015, there were various pending legal actions and proceedings against the Company arising from the normal course of business and in which claims for damages are asserted. It is the opinion of management, after discussion with legal counsel, that the disposition or ultimate resolution of such claims and legal actions will not have a material effect upon the consolidated financial statements of the Company.

Item 2. Unregistered Sales of Equity Securities and Use of Protocols

During 2014, the Company changed the form of payment to its directors for board meeting and quarterly fees from 100% cash to 50% in cash and 50% in Company common stock. The shares are issued as part of a plan adopted by the board of directors. Each director has elected to participate by entering into an agreement with the Company to accept common stock in lieu of cash for 50% of the director's board meeting and quarterly fees. As the shares are only issued to directors as part of a plan approved by the board, the shares are exempt from the registration requirements of the Securities Act of 1933, as amended (the "1933 Act"), as a sale not involving any public offering under Section 4(2) of the 1933 Act. Attendance for committee meetings continue to be paid completely in cash. As employee directors are not paid director's fees, only non-employee directors receive stock under this plan.

In the quarter ended March 31, 2015, the Company issued a total of 770 shares of common stock to its non-employee directors under this plan as compensation for $18 thousand of director fees. The cash retained by the Company by issuing common stock in lieu of paying cash is used for general corporate purposes. There are no brokers involved in the issuance of stock to directors and no commissions or other broker fees are paid.

At various times, the Company's Board of Directors has authorized the purchase of shares of the Company's outstanding common stock. No stated expiration dates have been established under any of the previous authorizations. There were no shares of common stock repurchased by the Company during the quarter ended March 31, 2015. There are 84,971 shares that may still be purchased under the various authorizations, although no shares have been purchased since 2008.

Item 6. Exhibits

List of Exhibits

3.1	Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation (incorporated by reference to the Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006 (File No. 000-14412)).
3.2	Articles of Amendment to Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation dated January 6, 2009 (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).
3.3	Articles of Amendment to Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation dated November 16, 2009 (incorporated by reference to the Current Report on Form 8-K dated November 17, 2009 (File No. 000-14412)).
3.4	Amended and Restated Bylaws of Farmers Capital Bank Corporation (incorporated by reference to the Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2009 (File No. 000-14412)).
4.1*	Junior Subordinated Indenture, dated as of July 21, 2005, between Farmers Capital Bank Corporation and Wilmington Trust Company, as Trustee, relating to unsecured junior subordinated deferrable interest notes that mature in 2035.
4.2*	Amended and Restated Trust Agreement, dated as of July 21, 2005, among Farmers Capital Bank Corporation, as Depositor, Wilmington Trust Company, as Property and Delaware Trustee, the Administrative Trustees (as named therein), and the Holders (as defined therein).
4.3*	Guarantee Agreement, dated as of July 21, 2005, between Farmers Capital Bank Corporation, as Guarantor, and Wilmington Trust Company, as Guarantee Trustee.

4.4*	Junior Subordinated Indenture, dated as of July 26, 2005, between Farmers Capital Bank Corporation and Wilmington Trust Company, as Trustee, relating to unsecured junior subordinated deferrable interest notes that mature in 2035.
4.5*	Amended and Restated Trust Agreement, dated as of July 26, 2005, among Farmers Capital Bank Corporation, as Depositor, Wilmington Trust Company, as Property and Delaware Trustee, the Administrative Trustees (as named therein), and the Holders (as defined therein).
4.6*	Guarantee Agreement, dated as of July 26, 2005, between Farmers Capital Bank Corporation, as Guarantor, and Wilmington Trust Company, as Guarantee Trustee.
4.7*	Indenture, dated as of August 14, 2007 between Farmers Capital Bank Corporation, as Issuer, and Wilmington Trust Company, as Trustee, relating to fixed/floating rate junior subordinated debt due 2037.
4.8*	Amended and Restated Declaration of Trust, dated as of August 14, 2007, by Farmers Capital Bank Corporation, as Sponsor, Wilmington Trust Company, as Delaware and Institutional Trustee, the Administrative Trustees (as named therein), and the Holders (as defined therein).

4.9*	Guarantee Agreement, dated as of August 14, 2007, between Farmers Capital Bank Corporation, as Guarantor, and Wilmington Trust Company, as Guarantee Trustee.
4.10	Form of Certificate for Fixed Rate Cumulative Perpetual Preferred Stock, Series A (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).
4.11	Letter Agreement, dated January 9, 2009, between Farmers Capital Bank Corporation and the United States Treasury, with respect to the issuance and sale of the Series A Preferred Stock and the Warrant, and Securities Purchase Agreement-Standard Terms attached thereto as Exhibit A (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).
10.1	Employee Stock Purchase Plan of Farmers Capital Bank Corporation (incorporated by reference to Form S-8 effective June 24, 2004 (File No. 333-116801)).
10.2	Employment agreement dated December 10, 2012 between Farmers Capital Bank Corporation and Lloyd C. Hillard, Jr. (incorporated by reference to Exhibit 10.1 to Form 8-K/A filed December 26, 2012 (File No. 000-14412)).
10.3	Amendment No. 1 to Employment agreement dated December 10, 2012 between Farmers Capital Bank Corporation and Lloyd C. Hillard, Jr. (incorporated by reference to Exhibit 10.1 to Form 8-K filed December 30, 2013 (File No. 000-14412)).
10.4	Amendment No. 2 to Employment agreement dated December 10, 2012 between Farmers Capital Bank Corporation and Lloyd C. Hillard, Jr. (incorporated by reference to Exhibit 10.1 to Form 8-K filed December 8, 2014).
10.5	Employment agreement dated December 17, 2013 between Farmers Capital Bank Corporation and Rickey D. Harp (incorporated by reference to Exhibit 10.1 to Form 8-K filed December 30, 2013 (File No. 000-14412)).
10.6	Employment agreement dated October 28, 2014 between Farmers Capital Bank Corporation and Mark A. Hampton (incorporated by reference to Exhibit 10.1 to Form 8-K filed October 28, 2014 (File No. 000-14412)).
31.1**	CEO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2**	CFO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32**	CEO & CFO Certifications Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	Interactive Data Files

* Exhibit not included pursuant to Item 601(b)(4)(iii) and (v) of Regulation S-K. The Company will provide a copy of such exhibit to the Securities and Exchange Commission upon request.

** Filed with this Quarterly Report on Form 10-Q.

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.

Date:	May 6, 2015	*/s/ Lloyd C. Hillard, Jr.* Lloyd C. Hillard, Jr. President and CEO (Principal Executive Officer)
Date:	May 6, 2015	*/s/ Mark A. Hampton* Mark A. Hampton Executive Vice President, CFO, and Secretary (Principal Financial and Accounting Officer)