

OHIO VALLEY BANC CORP  
Form 10-Q  
May 10, 2016

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, 2016

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 0-20914

OHIO VALLEY BANC CORP.  
(Exact name of registrant as specified in its charter)

Ohio  
(State of Incorporation)

31-1359191  
(I.R.S. Employer Identification No.)

420 Third Avenue  
Gallipolis, Ohio  
(Address of principal executive offices)

45631  
(ZIP Code)

(740) 446-2631  
(Issuer's telephone number, including area code)

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 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. (Check one):

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Large accelerated filer   
Non-accelerated filer

Accelerated filer   
Smaller reporting company

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

The number of common shares of the registrant outstanding as of May 10, 2016 was 4,142,247.

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## OHIO VALLEY BANC CORP.

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## PART I - FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

OHIO VALLEY BANC CORP.  
CONSOLIDATED BALANCE SHEETS  
(dollars in thousands, except share and per share data)

|   | March 31,<br>2016<br>UNAUDITED | December<br>31,<br>2015 |
|---|--------------------------------|-------------------------|
| <b>ASSETS</b>   |                                |                         |
| Cash and noninterest-bearing deposits with banks  | \$ 10,311                      | \$9,475                 |
| Interest-bearing deposits with banks  | 128,993                        | 36,055                  |
| Total cash and cash equivalents   | 139,304                        | 45,530                  |
| Certificates of deposit in financial institutions   | 1,470                          | 1,715                   |
| Securities available for sale   | 87,979                         | 91,651                  |
| Securities held to maturity (estimated fair value: 2016 - \$20,527; 2015 - \$20,790)  | 19,506                         | 19,903                  |
| Federal Home Loan Bank and Federal Reserve Bank stock   | 6,576                          | 6,576                   |
| Total loans   | 585,845                        | 585,752                 |
| Less: Allowance for loan losses   | (6,946 )                       | (6,648 )                |
| Net loans   | 578,899                        | 579,104                 |
| Premises and equipment, net   | 10,372                         | 10,404                  |
| Other real estate owned   | 2,179                          | 2,358                   |
| Accrued interest receivable   | 1,778                          | 1,819                   |
| Goodwill  | 1,267                          | 1,267                   |
| Bank owned life insurance and annuity assets  | 28,561                         | 28,352                  |
| Other assets  | 5,626                          | 7,606                   |
| Total assets  | \$ 883,517                     | \$796,285               |
| <b>LIABILITIES</b>  |                                |                         |
| Noninterest-bearing deposits  | \$ 240,642                     | \$176,499               |
| Interest-bearing deposits   | 500,363                        | 484,247                 |
| Total deposits  | 741,005                        | 660,746                 |
| Other borrowed funds  | 28,133                         | 23,946                  |
| Subordinated debentures   | 8,500                          | 8,500                   |
| Accrued liabilities   | 12,248                         | 12,623                  |
| Total liabilities   | 789,886                        | 705,815                 |
| COMMITMENTS AND CONTINGENT LIABILITIES (See Note 5)   | ----                           | ----                    |
| <b>SHAREHOLDERS' EQUITY</b>   |                                |                         |
| Common stock (\$1.00 stated value per share, 10,000,000 shares authorized;<br>2016 - 4,801,986 shares issued; 2015 - 4,777,414 shares issued) | 4,802                          | 4,777                   |

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|  |            |           |
|--|------------|-----------|
| Additional paid-in capital                 | 35,868     | 35,318    |
| Retained earnings                          | 67,749     | 65,782    |
| Accumulated other comprehensive income     | 924        | 305       |
| Treasury stock, at cost (659,739 shares)   | (15,712 )  | (15,712 ) |
| Total shareholders' equity                 | 93,631     | 90,470    |
| Total liabilities and shareholders' equity | \$ 883,517 | \$796,285 |

See accompanying notes to consolidated financial statements

OHIO VALLEY BANC CORP.  
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)  
(dollars in thousands, except per share data)

|  | Three months ended<br>March 31, |          |
|--|---------------------------------|----------|
|  | 2016                            | 2015     |
| Interest and dividend income:                            |                                 |          |
| Loans, including fees                                    | \$ 8,927                        | \$ 8,899 |
| Securities:  |                                 |          |
| Taxable  | 488                             | 449      |
| Tax exempt   | 114                             | 139      |
| Dividends  | 74                              | 74       |
| Other Interest   | 167                             | 66       |
|  | 9,770                           | 9,627    |
| Interest expense:  |                                 |          |
| Deposits   | 498                             | 535      |
| Other borrowed funds                                     | 125                             | 121      |
| Subordinated debentures                                  | 47                              | 41       |
|  | 670                             | 697      |
| Net interest income                                      | 9,100                           | 8,930    |
| Provision for loan losses                                | 479                             | (78 )    |
| Net interest income after provision for loan losses      | 8,621                           | 9,008    |
| Noninterest income:                                      |                                 |          |
| Service charges on deposit accounts                      | 405                             | 353      |
| Trust fees   | 60                              | 58       |
| Income from bank owned life insurance and annuity assets | 209                             | 176      |
| Mortgage banking income                                  | 57                              | 59       |
| Electronic refund check / deposit fees                   | 1,754                           | 2,095    |
| Debit / credit card interchange income                   | 586                             | 538      |
| Gain (loss) on other real estate owned                   | (5 )                            | 15       |
| Other  | 169                             | 195      |
|  | 3,235                           | 3,489    |
| Noninterest expense:                                     |                                 |          |
| Salaries and employee benefits                           | 4,570                           | 4,400    |
| Occupancy  | 429                             | 402      |
| Furniture and equipment                                  | 185                             | 178      |
| Professional fees  | 337                             | 356      |
| Marketing expense  | 247                             | 234      |
| FDIC insurance   | 149                             | 166      |
| Data processing  | 353                             | 368      |
| Software   | 292                             | 247      |
| Foreclosed assets  | 65                              | 35       |
| Merger related expenses                                  | 227                             | ----     |
| Other  | 1,115                           | 1,041    |
|  | 7,969                           | 7,427    |

|                            |                 |                 |
|----------------------------|-----------------|-----------------|
| Income before income taxes | 3,887           | 5,070           |
| Provision for income taxes | 1,055           | 1,446           |
| <b>NET INCOME</b>          | <b>\$ 2,832</b> | <b>\$ 3,624</b> |
| Earnings per share         | \$ .69          | \$ .88          |

See accompanying notes to consolidated financial statements

OHIO VALLEY BANC CORP.  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)  
(dollars in thousands)

|  | Three months ended<br>March 31, |         |
|--|---------------------------------|---------|
|  | 2016                            | 2015    |
| Net Income   | \$2,832                         | \$3,624 |
| Other comprehensive income:                                |                                 |         |
| Change in unrealized gain on available for sale securities | 938                             | 455     |
| Related tax (expense)                                      | (319 )                          | (154 )  |
| Total other comprehensive income, net of tax               | 619                             | 301     |
| Total comprehensive income                                 | \$3,451                         | \$3,925 |

See accompanying notes to consolidated financial statements



OHIO VALLEY BANC CORP.  
 CONDENSED CONSOLIDATED STATEMENTS OF CHANGES  
 IN SHAREHOLDERS' EQUITY (UNAUDITED)  
 (dollars in thousands, except share and per share data)

|  | Three months ended<br>March 31, |          |
|--|---------------------------------|----------|
|  | 2016                            | 2015     |
| Balance at beginning of period             | \$90,470                        | \$86,216 |
| Net income                                 | 2,832                           | 3,624    |
| Other comprehensive income, net of tax     | 619                             | 301      |
| Common stock issued to ESOP, 24,572 shares | 575                             | ----     |
| Cash dividends                             | (865 )                          | (865 )   |
| Balance at end of period                   | \$93,631                        | \$89,276 |
| Cash dividends per share                   | \$.21                           | \$.21    |

See accompanying notes to consolidated financial statements

OHIO VALLEY BANC CORP.  
CONDENSED CONSOLIDATED STATEMENTS OF  
CASH FLOWS (UNAUDITED)  
(dollars in thousands)

|   | Three months ended<br>March 31, |            |
|---|---------------------------------|------------|
|   | 2016                            | 2015       |
| Net cash provided by operating activities:                                    | \$5,344                         | \$12,738   |
| Investing activities:   |                                 |            |
| Proceeds from maturities of securities available for sale                     | 4,538                           | 3,619      |
| Purchases of securities available for sale                                    | ----                            | (8,019 )   |
| Proceeds from maturities of securities held to maturity                       | 466                             | 360        |
| Purchases of securities held to maturity                                      | (80 )                           | (285 )     |
| Proceeds from maturities of certificates of deposit in financial institutions | 245                             | ----       |
| Net change in loans   | (304 )                          | 94         |
| Proceeds from sale of other real estate owned                                 | 205                             | 260        |
| Purchases of premises and equipment   | (221 )                          | (317 )     |
| Net cash provided by (used in) investing activities                           | 4,849                           | (4,288 )   |
| Financing activities:   |                                 |            |
| Change in deposits  | 80,259                          | 77,578     |
| Cash dividends  | (865 )                          | (865 )     |
| Proceeds from Federal Home Loan Bank borrowings                               | 4,527                           | ----       |
| Repayment of Federal Home Loan Bank borrowings                                | (329 )                          | (324 )     |
| Change in other short-term borrowings   | (11 )                           | ----       |
| Net cash provided by financing activities                                     | 83,581                          | 76,389     |
| Change in cash and cash equivalents   | 93,774                          | 84,839     |
| Cash and cash equivalents at beginning of period                              | 45,530                          | 30,977     |
| Cash and cash equivalents at end of period                                    | \$139,304                       | \$1115,816 |
| Supplemental disclosure:  |                                 |            |
| Cash paid for interest  | \$649                           | \$665      |
| Cash paid for income taxes  | ----                            | ----       |
| Transfers from loans to other real estate owned                               | 30                              | 221        |
| Other real estate owned sales financed by the Bank                            | 274                             | ----       |

See accompanying notes to consolidated financial statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(dollars in thousands, except per share data)

NOTE 1- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**BASIS OF PRESENTATION:** The accompanying consolidated financial statements include the accounts of Ohio Valley Banc Corp. (“Ohio Valley”) and its wholly-owned subsidiaries, The Ohio Valley Bank Company (the “Bank”), Loan Central, Inc. (“Loan Central”), a consumer finance company, Ohio Valley Financial Services Agency, LLC (“Ohio Valley Financial Services”), an insurance agency, and OVBC Captive, Inc. (“the Captive”), a limited purpose property and casualty insurance company. Ohio Valley and its subsidiaries are collectively referred to as the “Company”. All material intercompany accounts and transactions have been eliminated in consolidation.

These interim financial statements are prepared by the Company without audit and reflect all adjustments of a normal recurring nature which, in the opinion of management, are necessary to present fairly the consolidated financial position of the Company at March 31, 2016, and its results of operations and cash flows for the periods presented. The results of operations for the three months ended March 31, 2016 are not necessarily indicative of the operating results to be anticipated for the full fiscal year ending December 31, 2016. The accompanying consolidated financial statements do not purport to contain all the necessary financial disclosures required by U.S. generally accepted accounting principles (“US GAAP”) that might otherwise be necessary in the circumstances. The Annual Report of the Company for the year ended December 31, 2015 contains consolidated financial statements and related notes which should be read in conjunction with the accompanying consolidated financial statements.

The consolidated financial statements for 2015 have been reclassified to conform to the presentation for 2016. These reclassifications had no effect on the net results of operations or shareholders’ equity.

**USE OF ESTIMATES IN THE PREPARATION OF FINANCIAL STATEMENTS:** The accounting and reporting policies followed by the Company conform to US GAAP established by the Financial Accounting Standards Board (“FASB”). The preparation of financial statements in conformity with US 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. Actual results could differ from those estimates. Areas involving the use of management’s estimates and assumptions that are more susceptible to change in the near term involve the allowance for loan losses, mortgage servicing rights, deferred tax assets, the fair value of certain securities, the fair value of financial instruments and the determination and carrying value of impaired loans and other real estate owned.

**INDUSTRY SEGMENT INFORMATION:** Internal financial information is primarily reported and aggregated in two lines of business, banking and consumer finance.

**EARNINGS PER SHARE:** Earnings per share are computed based on net income divided by the weighted average number of common shares outstanding during the period. The weighted average common shares outstanding were 4,127,666 for the three months ended March 31, 2016 and 4,117,675 for the three months ended March 31, 2015. Ohio Valley had no dilutive effect and no potential common shares issuable under stock options or other agreements for any period presented.

**NEW ACCOUNTING PRONOUNCEMENTS:** In May 2014, the FASB issued Accounting Standards Update (“ASU”) 2014-09, “Revenue from Contracts with Customers (Topic 606)”. The ASU creates a new topic, Topic 606, to provide guidance on revenue recognition for entities that enter into contracts with customers to transfer goods or services or enter into contracts for the transfer of nonfinancial assets. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Additional disclosures

are required to provide quantitative and qualitative information regarding the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The new guidance is effective for annual reporting periods, and interim reporting periods within those annual periods, beginning after December 15, 2018, with early adoption permitted on January 1, 2017. Management is currently evaluating the impact of the adoption of this guidance on the Company's financial statements.

In January 2016, the FASB issued ASU No. 2016-01, "Recognition and Measurement of Financial Assets and Financial Liabilities". The update provides updated accounting and reporting requirements for both public and non-public entities. The most significant provisions that will impact the Company are: 1) equity securities available for sale will be measured at fair value, with the changes in fair value recognized in the income statement; 2) eliminate the requirement to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments at amortized cost on the balance sheet; 3) utilization of the exit price notion when measuring the fair value of financial instruments for disclosure purposes; and 4) require separate presentation of both financial assets and liabilities by measurement category and form of financial asset on the balance sheet or accompanying notes to the financial statements. The update will be effective for interim and annual periods beginning after December 15, 2017, using a cumulative-effect adjustment to the balance sheet as of the beginning of the year of adoption. Early adoption is not permitted.

In February 2016, the FASB issued an update (ASU 2016-02, Leases) which will require lessees to record most leases on their balance sheet and recognize leasing expenses in the income statement. Operating leases, except for short-term leases that are subject to an accounting policy election, will be recorded on the balance sheet for lessees by establishing a lease liability and corresponding right-of-use asset. The guidance in this ASU will become effective for interim and annual reporting periods beginning after December 15, 2018, with early adoption permitted. Management is currently evaluating the impact of this update on its Consolidated Financial Statements.

#### NOTE 2 – FAIR VALUE OF FINANCIAL INSTRUMENTS

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

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

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

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

The following is a description of the Company's valuation methodologies used to measure and disclose the fair values of its financial assets and liabilities on a recurring or nonrecurring basis:

**Securities:** The fair values for securities are determined by quoted market prices, if available (Level 1). For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3). During times when trading is more liquid, broker quotes are used (if available) to validate the model. Rating agency and industry research reports as well as defaults and deferrals on individual securities are reviewed and incorporated into the calculations.

**Impaired Loans:** At the time a loan is considered impaired, it is valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the allowance for loan losses. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

**Other Real Estate Owned:** Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the

income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

Appraisals for both collateral-dependent impaired loans and other real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Company. Once received, a member of management reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with management's own assumptions of fair value based on factors that include recent market data or industry-wide statistics. On an as-needed basis, the Company reviews the fair value of collateral, taking into consideration current market data, as well as all selling costs that typically approximate 10%.

#### Assets and Liabilities Measured on a Recurring Basis

Assets and liabilities measured at fair value on a recurring basis are summarized below:

|  | Fair Value Measurements at March 31, 2016 Using                |   |   |
|--|--|---|---|
|  | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Assets:  |  |   |   |
| U.S. Government sponsored entity securities    | ----   | \$7,994                                       | ----                                      |
| Agency mortgage-backed securities, residential | ----   | 79,985  | ----                                      |

|  | Fair Value Measurements at December 31, 2015 Using             |   |   |
|--|--|---|---|
|  | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Assets:  |  |   |   |
| U.S. Government sponsored entity securities    | ----   | \$8,965                                       | ----                                      |
| Agency mortgage-backed securities, residential | ----   | 82,686  | ----                                      |

There were no transfers between Level 1 and Level 2 during 2016 or 2015.

#### Assets and Liabilities Measured on a Nonrecurring Basis

Assets and liabilities measured at fair value on a nonrecurring basis are summarized below:

|  | Fair Value Measurements at March 31, 2016, Using |                              |                                 |
|--|--|------------------------------|---------------------------------|
|  | Quoted Prices in Active                          | Significant Other Observable | Significant Unobservable Inputs |

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|                           | Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Inputs<br>(Level 2) | (Level 3) |
|---------------------------|--|---------------------|-----------|
| Assets:                   |  |                     |           |
| Impaired loans:           |  |                     |           |
| Commercial real estate:   |  |                     |           |
| Nonowner-occupied         | ----   | ----                | \$ 2,375  |
| Commercial and industrial | ----   | ----                | 3,905     |
| Other real estate owned:  |  |                     |           |
| Commercial real estate:   |  |                     |           |
| Construction              | ----   | ----                | 1,147     |



|                           | Fair Value Measurements at December 31, 2015, Using            |   |   |
|---------------------------|--|---|---|
|                           | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Assets:                   |  |   |   |
| Impaired loans:           |  |   |   |
| Commercial real estate:   |  |   |   |
| Nonowner-occupied         | ----   | ----  | \$ 2,473                                  |
| Commercial and industrial | ----   | ----  | 3,779                                     |
| Other real estate owned:  |  |   |   |
| Commercial real estate:   |  |   |   |
| Construction              | ----   | ----  | 1,147                                     |

At March 31, 2016, the recorded investment of impaired loans measured for impairment using the fair value of collateral for collateral-dependent loans totaled \$7,928, with a corresponding valuation allowance of \$1,648, resulting in an increase of \$89 in provision expense during the three months ended March 31, 2016, with no additional charge-offs recognized. This is compared to an increase of \$150 in provision expense during the three months ended March 31, 2015. At December 31, 2015, the recorded investment of impaired loans measured for impairment using the fair value of collateral for collateral-dependent loans totaled \$7,811, with a corresponding valuation allowance of \$1,559, resulting in an increase of \$741 in provision expense during the year ended December 31, 2015, with \$1,422 in additional charge-offs recognized.

Other real estate owned that was measured at fair value less costs to sell at March 31, 2016 and December 31, 2015 had a net carrying amount of \$1,147, which is made up of the outstanding balance of \$2,217, net of a valuation allowance of \$1,070 at December 31, 2015. There were no corresponding write downs during the three months ended March 31, 2016 and 2015.

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at March 31, 2016 and December 31, 2015:

| March 31, 2016            | Fair Value | Valuation Technique(s) | Unobservable Input(s)     | Range       | (Weighted Average) |
|---------------------------|------------|------------------------|---------------------------|-------------|--------------------|
| Impaired loans:           |            |                        |                           |             |                    |
| Commercial real estate:   |            |                        |                           |             |                    |
| Nonowner-occupied         | \$2,375    | Sales approach         | Adjustment to comparables | 0% to 12.5% | 5.7%               |
| Commercial and industrial | 3,905      | Sales approach         | Adjustment to comparables | 0.9% to 30% | 14.4%              |
| Other real estate owned:  |            |                        |                           |             |                    |

| Commercial real estate:                     |            |                        |                           |             |                    |
|---|------------|------------------------|---------------------------|-------------|--------------------|
| December 31, 2015                           | Fair Value | Valuation Technique(s) | Unobservable Input(s)     | Range       | (Weighted Average) |
| Impaired loans:                             |            |                        |                           |             |                    |
| Commercial real estate:                     |            |                        |                           |             |                    |
| Construction                                | 1,147      | Sales approach         | Adjustment to comparables | 5% to 35%   | 18%                |
| Other real estate owned:                    |            |                        |                           |             |                    |
| Commercial real estate:                     |            |                        |                           |             |                    |
| Nonowner-occupied Commercial and industrial | \$2,473    | Sales approach         | Adjustment to comparables | 0% to 12.5% | 5.7%               |
| Commercial and industrial                   | 3,779      | Sales approach         | Adjustment to comparables | 0.9% to 30% | 14.3%              |
| Other real estate owned:                    |            |                        |                           |             |                    |
| Commercial real estate:                     |            |                        |                           |             |                    |
| Construction                                | 1,147      | Sales approach         | Adjustment to comparables | 0% to 35%   | 15.2%              |

The carrying amounts and estimated fair values of financial instruments at March 31, 2016 and December 31, 2015 are as follows:

|   | Carrying<br>Value | Fair Value Measurements at March 31, 2016 Using: |         |         |            |
|---|-------------------|--|---------|---------|------------|
|   |                   | Level 1  | Level 2 | Level 3 | Total      |
| <b>Financial Assets:</b>                              |                   |  |         |         |            |
| Cash and cash equivalents                             | \$ 139,304        | \$ 139,304                                       | \$----  | \$----  | \$ 139,304 |
| Certificates of deposit in financial institutions     | 1,470             | ----   | 1,470   | ----    | 1,470      |
| Securities available for sale                         | 87,979            | ----   | 87,979  | ----    | 87,979     |
| Securities held to maturity                           | 19,506            | ----   | 9,822   | 10,705  | 20,527     |
| Federal Home Loan Bank and Federal Reserve Bank stock | 6,576             | N/A  | N/A     | N/A     | N/A        |
| Loans, net  | 578,899           | ----   | ----    | 583,867 | 583,867    |
| Accrued interest receivable                           | 1,778             | ----   | 327     | 1,451   | 1,778      |
| <b>Financial liabilities:</b>                         |                   |  |         |         |            |
| Deposits  | 741,005           | 240,642  | 500,856 | ----    | 741,498    |
| Other borrowed funds                                  | 28,133            | ----   | 27,952  | ----    | 27,952     |
| Subordinated debentures                               | 8,500             | ----   | 5,388   | ----    | 5,388      |
| Accrued interest payable                              | 470               | 3  | 467     | ----    | 470        |

|   | Carrying<br>Value | Fair Value Measurements at December 31, 2015<br>Using: |         |         |          |
|---|-------------------|--|---------|---------|----------|
|   |                   | Level 1  | Level 2 | Level 3 | Total    |
| <b>Financial Assets:</b>                              |                   |  |         |         |          |
| Cash and cash equivalents                             | \$45,530          | \$45,530   | \$----  | \$----  | \$45,530 |
| Certificates of deposit in financial institutions     | 1,715             | ----   | 1,715   | ----    | 1,715    |
| Securities available for sale                         | 91,651            | ----   | 91,651  | ----    | 91,651   |
| Securities held to maturity                           | 19,903            | ----   | 9,814   | 10,976  | 20,790   |
| Federal Home Loan Bank and Federal Reserve Bank stock | 6,576             | N/A  | N/A     | N/A     | N/A      |
| Loans, net  | 579,104           | ----   | ----    | 582,427 | 582,427  |
| Accrued interest receivable                           | 1,819             | ----   | 224     | 1,595   | 1,819    |
| <b>Financial liabilities:</b>                         |                   |  |         |         |          |
| Deposits  | 660,746           | 176,499  | 484,636 | ----    | 661,135  |
| Other borrowed funds                                  | 23,946            | ----   | 23,672  | ----    | 23,672   |
| Subordinated debentures                               | 8,500             | ----   | 5,368   | ----    | 5,368    |
| Accrued interest payable                              | 449               | 4  | 445     | ----    | 449      |

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

**Cash and Cash Equivalents:** The carrying amounts of cash and short-term instruments approximate fair values and are classified as Level 1.

**Certificates of Deposit in Financial Institutions:** The carrying amounts of certificates of deposit in financial institutions approximate fair values and are classified as Level 2.

**Securities Held to Maturity:** The fair values for securities held to maturity are determined in the same manner as securities held for sale and discussed earlier in this note. Level 3 securities consist of nonrated municipal bonds and tax credit (“QZAB”) bonds.

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

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

**Deposit Liabilities:** The fair values disclosed for noninterest-bearing deposits are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amount) resulting in a Level 1 classification. The carrying amounts of variable rate, fixed-term money market accounts and certificates of deposit approximate their fair values at the reporting date resulting in a Level 2 classification. Fair values for fixed rate certificates of deposit are estimated using a discounted cash flows calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits resulting in a Level 2 classification.

Other Borrowed Funds: The carrying values of the Company's short-term borrowings, generally maturing within ninety days, approximate their fair values resulting in a Level 2 classification. The fair values of the Company's long-term borrowings are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 2 classification.

Subordinated Debentures: The fair values of the Company's Subordinated Debentures are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 2 classification.

Accrued Interest Receivable and Payable: The carrying amount of accrued interest approximates fair value, resulting in a classification that is consistent with the earning assets and interest-bearing liabilities with which it is associated.

Off-balance Sheet Instruments: Fair values for off-balance sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value of commitments is not material.

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

### NOTE 3 – SECURITIES

The following table summarizes the amortized cost and fair value of securities available for sale and securities held to maturity at March 31, 2016 and December 31, 2015 and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) and gross unrecognized gains and losses:

|  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair Value |
|--|-------------------|------------------------------|-------------------------------|-------------------------|
| <b>Securities Available for Sale</b>             |                   |                              |                               |                         |
| <b>March 31, 2016</b>                            |                   |                              |                               |                         |
| U.S. Government sponsored entity securities      | \$ 8,009          | \$ ----                      | \$ (15 )                      | \$ 7,994                |
| Agency mortgage-backed securities, residential   | 78,569            | 1,445                        | (29 )                         | 79,985                  |
| Total securities                                 | \$ 86,578         | \$ 1,445                     | \$ (44 )                      | \$ 87,979               |
| <b>December 31, 2015</b>                         |                   |                              |                               |                         |
| U.S. Government sponsored entity securities      | \$ 9,011          | \$ ----                      | \$ (46 )                      | \$ 8,965                |
| Agency mortgage-backed securities, residential   | 82,178            | 981                          | (473 )                        | 82,686                  |
| Total securities                                 | \$ 91,189         | \$ 981                       | \$ (519 )                     | \$ 91,651               |
| <b>Securities Held to Maturity</b>               |                   |                              |                               |                         |
| <b>March 31, 2016</b>                            |                   |                              |                               |                         |
| Obligations of states and political subdivisions | \$19,501          | \$ 1,021                     | \$ ----                       | \$20,522                |
| Agency mortgage-backed securities, residential   | 5                 | ---                          | ---                           | 5                       |

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|  |          |          |         |          |
|--|----------|----------|---------|----------|
| Total securities                                 | \$19,506 | \$ 1,021 | ----    | \$20,527 |
| December 31, 2015                                |          |          |         |          |
| Obligations of states and political subdivisions | \$19,898 | \$ 892   | \$ (5 ) | \$20,785 |
| Agency mortgage-backed securities, residential   | 5        | ----     | ----    | 5        |
| Total securities                                 | \$19,903 | \$ 892   | \$ (5 ) | \$20,790 |

The amortized cost and estimated fair value of debt securities at March 31, 2016, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because certain issuers may have the right to call or prepay the debt obligations prior to their contractual maturities. Securities not due at a single maturity are shown separately.

| Debt Securities:                               | Available for Sale |                      | Held to Maturity |                      |
|--|--------------------|----------------------|------------------|----------------------|
|  | Amortized Cost     | Estimated Fair Value | Amortized Cost   | Estimated Fair Value |
| Due in one year or less                        | \$----             | \$----               | \$261            | \$268                |
| Due in over one to five years                  | 8,009              | 7,994                | 6,565            | 6,907                |
| Due in over five to ten years                  | ----               | ----                 | 10,593           | 11,243               |
| Due after ten years                            | ----               | ----                 | 2,082            | 2,104                |
| Agency mortgage-backed securities, residential | 78,569             | 79,985               | 5                | 5                    |
| Total debt securities                          | \$86,578           | \$87,979             | \$19,506         | \$20,527             |

The following table summarizes securities with unrealized losses at March 31, 2016 and December 31, 2015, aggregated by major security type and length of time in a continuous unrealized loss position:

| March 31, 2016<br>Securities Available for Sale | Less Than 12 Months |                 | 12 Months or More |                 | Total      |                 |
|---|---------------------|-----------------|-------------------|-----------------|------------|-----------------|
|   | Fair Value          | Unrealized Loss | Fair Value        | Unrealized Loss | Fair Value | Unrealized Loss |
| U.S. Government sponsored entity securities     | \$ 7,994            | \$ (15 )        | \$ ----           | \$ ----         | \$ 7,994   | \$ (15 )        |
| Agency mortgage-backed securities, residential  | 15,583              | (29 )           | ----              | ----            | 15,583     | (29 )           |
| Total available for sale                        | \$ 23,577           | \$ (44 )        | \$ ----           | \$ ----         | \$ 23,577  | \$ (44 )        |

| December 31, 2015<br>Securities Available for Sale | Less Than 12 Months |                 | 12 Months or More |                 | Total      |                 |
|--|---------------------|-----------------|-------------------|-----------------|------------|-----------------|
|  | Fair Value          | Unrealized Loss | Fair Value        | Unrealized Loss | Fair Value | Unrealized Loss |
| U.S. Government sponsored entity securities        | \$ 7,964            | \$ (46 )        | \$ ----           | \$ ----         | \$ 7,964   | \$ (46 )        |
| Agency mortgage-backed securities, residential     | 42,112              | (407 )          | 3,645             | (66)            | 45,757     | (473 )          |
| Total available for sale                           | \$ 50,076           | \$ (453 )       | \$ 3,645          | \$ (66)         | \$ 53,721  | \$ (519 )       |

|  | Less Than 12 Months |                   | 12 Months or More |                   | Total      |                   |
|--|---------------------|-------------------|-------------------|-------------------|------------|-------------------|
|  | Fair Value          | Unrecognized Loss | Fair Value        | Unrecognized Loss | Fair Value | Unrecognized Loss |

## Securities Held to

## Maturity

## Obligations of states and

|                        |        |         |         |         |        |         |
|------------------------|--------|---------|---------|---------|--------|---------|
| political subdivisions | \$ 995 | \$ (5 ) | \$ ---- | \$ ---- | \$ 995 | \$ (5 ) |
| Total held to maturity | \$ 995 | \$ (5 ) | \$ ---- | \$ ---- | \$ 995 | \$ (5 ) |

Unrealized losses on the Company's debt securities have not been recognized into income because the issuers' securities are of high credit quality as of March 31, 2016, and management does not intend to sell and it is likely that management will not be required to sell the securities prior to their anticipated recovery. Management does not believe any individual unrealized loss at March 31, 2016 and December 31, 2015 represents an other-than-temporary impairment.



## NOTE 4 – LOANS AND ALLOWANCE FOR LOAN LOSSES

| Loans are comprised of the following: | March 31,<br>2016 | December<br>31,<br>2015 |
|---------------------------------------|-------------------|-------------------------|
| Residential real estate               | \$227,026         | \$223,875               |
| Commercial real estate:               |                   |                         |
| Owner-occupied                        | 71,117            | 73,458                  |
| Nonowner-occupied                     | 71,731            | 72,002                  |
| Construction                          | 26,512            | 23,852                  |
| Commercial and industrial             | 81,034            | 81,936                  |
| Consumer:                             |                   |                         |
| Automobile                            | 44,952            | 44,566                  |
| Home equity                           | 19,558            | 20,841                  |
| Other                                 | 43,915            | 45,222                  |
|                                       | 585,845           | 585,752                 |
| Less: Allowance for loan losses       | 6,946             | 6,648                   |
| Loans, net                            | \$578,899         | \$579,104               |

The following table presents the activity in the allowance for loan losses by portfolio segment for the three months ended March 31, 2016 and 2015:

| March 31, 2016                 | Residential<br>Real Estate | Commercial<br>Real Estate | Commercial<br>and<br>Industrial | Consumer | Total   |
|--------------------------------|----------------------------|---------------------------|---------------------------------|----------|---------|
| Allowance for loan losses:     |                            |                           |                                 |          |         |
| Beginning balance              | \$1,087                    | \$1,959                   | \$2,589                         | \$1,013  | \$6,648 |
| Provision for loan losses      | 40                         | 17                        | 82                              | 340      | 479     |
| Loans charged off              | (104 )                     | ----                      | ----                            | (483 )   | (587 )  |
| Recoveries                     | 162                        | 19                        | 1                               | 224      | 406     |
| Total ending allowance balance | \$1,185                    | \$1,995                   | \$2,672                         | \$1,094  | \$6,946 |

| March 31, 2015                 | Residential<br>Real Estate | Commercial<br>Real Estate | Commercial<br>and<br>Industrial | Consumer | Total   |
|--------------------------------|----------------------------|---------------------------|---------------------------------|----------|---------|
| Allowance for loan losses:     |                            |                           |                                 |          |         |
| Beginning balance              | \$1,426                    | \$4,195                   | \$1,602                         | \$1,111  | \$8,334 |
| Provision for loan losses      | 31                         | 6                         | 14                              | (129 )   | (78 )   |
| Loans charged-off              | (97 )                      | (8 )                      | (2 )                            | (261 )   | (368 )  |
| Recoveries                     | 105                        | 17                        | 124                             | 186      | 432     |
| Total ending allowance balance | \$1,465                    | \$4,210                   | \$1,738                         | \$907    | \$8,320 |

The following table presents the balance in the allowance for loan losses and the recorded investment of loans by portfolio segment and based on impairment method as of March 31, 2016 and December 31, 2015:

| March 31, 2016 | Residential<br>Real Estate | Commercial<br>Real Estate | Commercial | Consumer | Total |
|----------------|----------------------------|---------------------------|------------|----------|-------|
|----------------|----------------------------|---------------------------|------------|----------|-------|

and  
Industrial

Allowance for loan losses:

Ending allowance balance attributable to  
loans:

|                                       |         |          |          |         |         |
|---------------------------------------|---------|----------|----------|---------|---------|
| Individually evaluated for impairment | \$----  | \$ 309   | \$ 1,900 | \$3     | \$2,212 |
| Collectively evaluated for impairment | 1,185   | 1,686    | 772      | 1,091   | 4,734   |
| Total ending allowance balance        | \$1,185 | \$ 1,995 | \$ 2,672 | \$1,094 | \$6,946 |

Loans:

|   |           |            |           |           |           |
|---|-----------|------------|-----------|-----------|-----------|
| Loans individually evaluated for impairment | \$730     | \$ 8,022   | \$ 8,869  | \$218     | \$17,839  |
| Loans collectively evaluated for impairment | 226,296   | 161,338    | 72,165    | 108,207   | 568,006   |
| Total ending loans balance                  | \$227,026 | \$ 169,360 | \$ 81,034 | \$108,425 | \$585,845 |

| December 31, 2015                               | Residential<br>Real Estate | Commercial<br>Real Estate | Commercial<br>and<br>Industrial | Consumer | Total    |
|---|----------------------------|---------------------------|---------------------------------|----------|----------|
| Allowance for loan losses:                      |                            |                           |                                 |          |          |
| Ending allowance balance attributable to loans: |                            |                           |                                 |          |          |
| Individually evaluated for impairment           | \$----                     | \$ 311                    | \$ 1,850                        | \$ 3     | \$ 2,164 |
| Collectively evaluated for impairment           | 1,087                      | 1,648                     | 739                             | 1,010    | 4,484    |
| Total ending allowance balance                  | \$ 1,087                   | \$ 1,959                  | \$ 2,589                        | \$ 1,013 | \$ 6,648 |

| Loans:                                      |            |            |           |            |            |
|---|------------|------------|-----------|------------|------------|
| Loans individually evaluated for impairment | \$ 1,001   | \$ 7,318   | \$ 8,691  | \$ 218     | \$ 17,228  |
| Loans collectively evaluated for impairment | 222,874    | 161,994    | 73,245    | 110,411    | 568,524    |
| Total ending loans balance                  | \$ 223,875 | \$ 169,312 | \$ 81,936 | \$ 110,629 | \$ 585,752 |

The following tables present information related to loans individually evaluated for impairment by class of loans as of March 31, 2016 and December 31, 2015:

| March 31, 2016                      | Unpaid<br>Principal<br>Balance | Recorded<br>Investment | Allowance<br>for Loan<br>Losses<br>Allocated |
|-------------------------------------|--------------------------------|------------------------|--|
| With an allowance recorded:         |                                |                        |  |
| Commercial real estate:             |                                |                        |  |
| Owner-occupied                      | \$ 204                         | \$ 204                 | \$ 204                                       |
| Nonowner-occupied                   | 393                            | 393                    | 105  |
| Commercial and industrial           | 4,524                          | 4,524                  | 1,900  |
| Consumer:                           |                                |                        |  |
| Home equity                         | 218                            | 218                    | 3  |
| With no related allowance recorded: |                                |                        |  |
| Residential real estate             | 730                            | 730                    | ----   |
| Commercial real estate:             |                                |                        |  |
| Owner-occupied                      | 3,797                          | 3,250                  | ----   |
| Nonowner-occupied                   | 5,896                          | 3,495                  | ----   |
| Construction                        | 680                            | 680                    | ----   |
| Commercial and industrial           | 4,345                          | 4,345                  | ----   |
| Total                               | \$ 20,787                      | \$ 17,839              | \$ 2,212                                     |

| December 31, 2015           | Unpaid<br>Principal<br>Balance | Recorded<br>Investment | Allowance<br>for Loan<br>Losses<br>Allocated |
|-----------------------------|--------------------------------|------------------------|--|
| With an allowance recorded: |                                |                        |  |
| Commercial real estate:     |                                |                        |  |
| Owner-occupied              | \$ 204                         | \$ 204                 | \$ 204                                       |
| Nonowner-occupied           | 396                            | 396                    | 107  |
| Commercial and industrial   | 4,355                          | 4,355                  | 1,850  |
| Consumer:                   |                                |                        |  |

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|                                     |          |          |         |
|-------------------------------------|----------|----------|---------|
| Home equity                         | 218      | 218      | 3       |
| With no related allowance recorded: |          |          |         |
| Residential real estate             | 1,001    | 1,001    | ----    |
| Commercial real estate:             |          |          |         |
| Owner-occupied                      | 3,812    | 3,265    | ----    |
| Nonowner-occupied                   | 5,178    | 2,773    | ----    |
| Construction                        | 680      | 680      | ----    |
| Commercial and industrial           | 4,336    | 4,336    | ----    |
| Total                               | \$20,180 | \$17,228 | \$2,164 |

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The following tables present information related to loans individually evaluated for impairment by class of loans for the three months ended March 31, 2016 and 2015:

|                                     | Three months ended March 31, 2016 |                            |                                |
|-------------------------------------|-----------------------------------|----------------------------|--------------------------------|
|                                     | Average Impaired Loans            | Interest Income Recognized | Cash Basis Interest Recognized |
| With an allowance recorded:         |                                   |                            |                                |
| Commercial real estate:             |                                   |                            |                                |
| Owner-occupied                      | \$204                             | \$ 4                       | \$ 4                           |
| Nonowner-occupied                   | 395                               | 5                          | 5                              |
| Commercial and industrial           | 4,439                             | 41                         | 41                             |
| Consumer:                           |                                   |                            |                                |
| Home equity                         | 219                               | 2                          | 2                              |
| With no related allowance recorded: |                                   |                            |                                |
| Residential real estate             | 731                               | 9                          | 9                              |
| Commercial real estate:             |                                   |                            |                                |
| Owner-occupied                      | 3,257                             | 43                         | 43                             |
| Nonowner-occupied                   | 3,134                             | 13                         | 13                             |
| Construction                        | 680                               | ----                       | ----                           |
| Commercial and industrial           | 4,341                             | 51                         | 51                             |
| Total                               | \$17,400                          | \$ 168                     | \$ 168                         |

|                                     | Three months ended March 31, 2015 |                            |                                |
|-------------------------------------|-----------------------------------|----------------------------|--------------------------------|
|                                     | Average Impaired Loans            | Interest Income Recognized | Cash Basis Interest Recognized |
| With an allowance recorded:         |                                   |                            |                                |
| Commercial real estate:             |                                   |                            |                                |
| Owner-occupied                      | \$827                             | \$ ----                    | \$ ----                        |
| Nonowner-occupied                   | 7,618                             | 16                         | 16                             |
| Commercial and industrial           | 2,701                             | 25                         | 25                             |
| Consumer:                           |                                   |                            |                                |
| Home equity                         | 219                               | 3                          | 3                              |
| With no related allowance recorded: |                                   |                            |                                |
| Residential real estate             | 1,412                             | 9                          | 9                              |
| Commercial real estate:             |                                   |                            |                                |
| Owner-occupied                      | 2,566                             | 30                         | 30                             |
| Nonowner-occupied                   | 300                               | 12                         | 12                             |
| Construction                        | 340                               | ----                       | ----                           |
| Commercial and industrial           | 4,390                             | 55                         | 55                             |
| Total                               | \$20,373                          | \$ 150                     | \$ 150                         |

The recorded investment of a loan is its carrying value excluding accrued interest and deferred loan fees.

Nonaccrual loans and loans past due 90 days or more and still accruing include both smaller balance homogenous loans that are collectively evaluated for impairment and individually classified as impaired loans.

The Company transfers loans to other real estate owned, at fair value less cost to sell, in the period the Company obtains physical possession of the property (through legal title or through a deed in lieu). As of March 31, 2016 and December 31, 2015, other real estate owned secured by residential real estate totaled \$951 and \$1,131, respectively. In addition, nonaccrual residential mortgage loans that are in the process of foreclosure had a recorded investment of \$1,114 and \$988 as of March 31, 2016 and December 31, 2015, respectively.

The following table presents the recorded investment of nonaccrual loans and loans past due 90 days or more and still accruing by class of loans as of March 31, 2016 and December 31, 2015:

| March 31, 2016            | Loans Past Due 90 Days And Still Accruing |  | Nonaccrual |
|---------------------------|---|--|------------|
|                           |   |  |            |
| Residential real estate   | \$90                                      |  | \$2,103    |
| Commercial real estate:   |   |  |            |
| Owner-occupied            | ----                                      |  | 367        |
| Nonowner-occupied         | ----                                      |  | 2,635      |
| Construction              | ----                                      |  | 769        |
| Commercial and industrial | ----                                      |  | 1,185      |
| Consumer:                 |   |  |            |
| Automobile                | 47  |  | 15         |
| Home equity               | ----                                      |  | 63         |
| Other                     | 4   |  | 5          |
| Total                     | \$141                                     |  | \$7,142    |

| December 31, 2015         | Loans Past Due 90 Days And Still Accruing |  | Nonaccrual |
|---------------------------|---|--|------------|
|                           |   |  |            |
| Residential real estate   | \$20                                      |  | \$2,048    |
| Commercial real estate:   |   |  |            |
| Owner-occupied            | ----                                      |  | 404        |
| Nonowner-occupied         | ----                                      |  | 2,737      |
| Construction              | ----                                      |  | 769        |
| Commercial and industrial | ----                                      |  | 1,152      |
| Consumer:                 |   |  |            |
| Automobile                | 18  |  | 27         |
| Home equity               | ----                                      |  | 96         |
| Other                     | 1   |  | 3          |
| Total                     | \$39                                      |  | \$7,236    |

The following table presents the aging of the recorded investment of past due loans by class of loans as of March 31, 2016 and December 31, 2015:

| March 31, 2016 | 30-59 Days Past Due     | 60-89 Days Past Due | 90 Days Or More Past Due | Total Past Due | Loans Not Past Due | Total     |
|----------------|-------------------------|---------------------|--------------------------|----------------|--------------------|-----------|
|                | Residential real estate | \$3,116             | \$755                    | \$1,919        | \$5,790            | \$221,236 |

## Commercial real estate:

|                           |      |       |       |       |        |        |
|---------------------------|------|-------|-------|-------|--------|--------|
| Owner-occupied            | 412  | 1,038 | 231   | 1,681 | 69,436 | 71,117 |
| Nonowner-occupied         | ---- | 239   | 2,635 | 2,874 | 68,857 | 71,731 |
| Construction              | ---- | ----  | 769   | 769   | 25,743 | 26,512 |
| Commercial and industrial | 71   | 75    | 1,077 | 1,223 | 79,811 | 81,034 |

## Consumer:

|             |         |         |         |          |           |           |
|-------------|---------|---------|---------|----------|-----------|-----------|
| Automobile  | 552     | 198     | 62      | 812      | 44,140    | 44,952    |
| Home equity | 35      | 15      | 45      | 95       | 19,463    | 19,558    |
| Other       | 324     | 73      | 4       | 401      | 43,514    | 43,915    |
| Total       | \$4,510 | \$2,393 | \$6,742 | \$13,645 | \$572,200 | \$585,845 |



| December 31, 2015         | 30-59<br>Days<br>Past Due | 60-89<br>Days<br>Past Due | 90 Days<br>Or More<br>Past Due | Total<br>Past Due | Loans Not<br>Past Due | Total     |
|---------------------------|---------------------------|---------------------------|--------------------------------|-------------------|-----------------------|-----------|
| Residential real estate   | \$2,564                   | \$1,484                   | \$1,708                        | \$5,756           | \$218,119             | \$223,875 |
| Commercial real estate:   |                           |                           |                                |                   |                       |           |
| Owner-occupied            | 141                       | 33                        | 371                            | 545               | 72,913                | 73,458    |
| Nonowner-occupied         | 35                        | 334                       | 2,737                          | 3,106             | 68,896                | 72,002    |
| Construction              | ----                      | 2                         | 769                            | 771               | 23,081                | 23,852    |
| Commercial and industrial | 31                        | 88                        | 1,077                          | 1,196             | 80,740                | 81,936    |
| Consumer:                 |                           |                           |                                |                   |                       |           |
| Automobile                | 727                       | 197                       | 36                             | 960               | 43,606                | 44,566    |
| Home equity               | 75                        | ----                      | 76                             | 151               | 20,690                | 20,841    |
| Other                     | 420                       | 104                       | 4                              | 528               | 44,694                | 45,222    |
| Total                     | \$3,993                   | \$2,242                   | \$6,778                        | \$13,013          | \$572,739             | \$585,752 |

#### Troubled Debt Restructurings:

A troubled debt restructuring (“TDR”) occurs when the Company has agreed to a loan modification in the form of a concession for a borrower who is experiencing financial difficulty. All TDR’s are considered to be impaired. The modification of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; a reduction in the contractual principal and interest payments of the loan; or short-term interest-only payment terms.

The Company has allocated reserves for a portion of its TDR’s to reflect the fair values of the underlying collateral or the present value of the concessionary terms granted to the customer.

The following table presents the types of TDR loan modifications by class of loans as of March 31, 2016 and December 31, 2015:

| March 31, 2016   | TDR’s<br>Performing<br>to Modified<br>Terms | TDR’s Not<br>Performing<br>to Modified<br>Terms | Total<br>TDR’s |
|--|---|---|----------------|
| Residential real estate                                  |   |   |                |
| Interest only payments                                   | \$730                                       | \$----  | \$730          |
| Commercial real estate:                                  |   |   |                |
| Owner-occupied   |   |   |                |
| Interest only payments                                   | 456   | ----  | 456            |
| Rate reduction   | ----  | 232   | 232            |
| Reduction of principal and interest payments             | 598   | ----  | 598            |
| Maturity extension at lower stated rate than market rate | 1,964                                       | ----  | 1,964          |
| Credit extension at lower stated rate than market rate   | 204   | ----  | 204            |
| Nonowner-occupied  |   |   |                |
| Interest only payments                                   | 539   | 2,375   | 2,914          |
| Rate reduction   | 393   | ----  | 393            |
| Credit extension at lower stated rate than market rate   | 581   | ----  | 581            |

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|  |          |         |          |
|--|----------|---------|----------|
| <b>Commercial and industrial</b>                         |          |         |          |
| Interest only payments                                   | 7,544    | ----    | 7,544    |
| Credit extension at lower stated rate than market rate   | 439      | 391     | 830      |
| <b>Consumer:</b>   |          |         |          |
| <b>Home equity</b>                                       |          |         |          |
| Maturity extension at lower stated rate than market rate | 218      | ----    | 218      |
| Total TDR's  | \$13,666 | \$2,998 | \$16,664 |

|  | TDR's<br>Performing<br>to Modified<br>Terms | TDR's Not<br>Performing<br>to Modified<br>Terms | Total<br>TDR's   |
|--|---|---|------------------|
| December 31, 2015  |   |   |                  |
| Residential real estate                                  |   |   |                  |
| Interest only payments                                   | \$ 1,001                                    | \$----  | \$ 1,001         |
| Commercial real estate:                                  |   |   |                  |
| Owner-occupied   |   |   |                  |
| Interest only payments                                   | 433   | ----  | 433              |
| Rate reduction   | ----  | 232   | 232              |
| Reduction of principal and interest payments             | 604   | ----  | 604              |
| Maturity extension at lower stated rate than market rate | 1,996                                       | ----  | 1,996            |
| Credit extension at lower stated rate than market rate   | 204   | ----  | 204              |
| Nonowner-occupied  |   |   |                  |
| Interest only payments                                   | 300   | 2,473   | 2,773            |
| Rate reduction   | 396   | ----  | 396              |
| Commercial and industrial                                |   |   |                  |
| Interest only payments                                   | 7,579                                       | ----  | 7,579            |
| Credit extension at lower stated rate than market rate   | 226   | 391   | 617              |
| Consumer:  |   |   |                  |
| Home equity  |   |   |                  |
| Maturity extension at lower stated rate than market rate | 218   | ----  | 218              |
| <b>Total TDR's</b>                                       | <b>\$ 12,957</b>                            | <b>\$ 3,096</b>                                 | <b>\$ 16,053</b> |

During the three months ended March 31, 2016, the TDR's described above increased the provision expense and the allowance for loan losses by \$48 with no corresponding charge-offs. During the year ended December 31, 2015, the TDR's described above increased the allowance for loan losses and provision expense by \$93 with corresponding charge-offs of \$1,422. The charge-offs of \$1,422 during 2015 included \$1,304 that were related to specific reserves that had already been provided for during 2014, and, as a result, did not impact provision expense during 2015.

At March 31, 2016, the balance in TDR loans increased \$611, or 3.8%, from year-end 2015. The increase was largely due to concessions granted on two commercial real estate nonowner-occupied loans during the first quarter of 2016. The Company had 82% of its TDR's performing according to their modified terms at March 31, 2016, as compared to 81% at December 31, 2015. The Company's specific allocations in reserves to customers whose loan terms have been modified in TDR's totaled \$1,717 at March 31, 2016, as compared to \$1,669 in reserves at December 31, 2015. At March 31, 2016, the Company had \$823 in commitments to lend additional amounts to customers with outstanding loans that are classified as TDR's, as compared to \$995 at December 31, 2015.

The following table presents the pre- and post-modification balances of TDR loan modifications by class of loans that occurred during the three months ended March 31, 2016:

|                                   | TDR's<br>Performing to Modified<br>Terms   |   | TDR's Not<br>Performing to Modified<br>Terms |   |
|-----------------------------------|--|---|--|---|
|                                   | Pre-Modification<br>Recorded<br>Investment | Post-Modification<br>Recorded<br>Investment | Pre-Modification<br>Recorded<br>Investment   | Post-Modification<br>Recorded<br>Investment |
| Three months ended March 31, 2016 |  |   |  |   |

Commercial real estate:

Nonowner-occupied

|  |       |        |        |         |
|--|-------|--------|--------|---------|
| Interest only payments                                 | \$238 | \$ 238 | \$---- | \$ ---- |
| Credit extension at lower stated rate than market rate | 581   | 581    | ----   | ----    |
| Total TDR's  | \$819 | \$ 819 | \$---- | \$ ---- |

All of the Company's loans that were restructured during the three months ended March 31, 2016 were performing in accordance with their modified terms. Furthermore, there were no TDR's described above at March 31, 2016 that experienced any payment defaults within twelve months following their loan modification. A default is considered to have occurred once the TDR is past due 90 days or more or it has been placed on nonaccrual. TDR 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 loans modified during the three months ended March 31, 2016 had no impact on the provision expense or the allowance for loan losses. As of March 31, 2016, the Company had no allocation of reserves to customers whose loan terms were modified during the first three months of 2016.

There were no TDR loan modifications that occurred during the three months ended March 31, 2015.

#### Credit Quality Indicators:

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, among other factors. These risk categories are represented by a loan grading scale from 1 through 10. The Company analyzes loans individually with a higher credit risk rating and groups these loans into categories called "criticized" and "classified" assets. The Company considers its criticized assets to be loans that are graded 8 and its classified assets to be loans that are graded 9 through 10. The Company's risk categories are reviewed at least annually on loans that have aggregate borrowing amounts that meet or exceed \$500.

The Company uses the following definitions for its criticized loan risk ratings:

**Special Mention (Loan Grade 8).** Loans classified as special mention indicate considerable risk due to deterioration of repayment (in the earliest stages) due to potential weak primary repayment source, or payment delinquency. These loans will be under constant supervision, are not classified and do not expose the institution to sufficient risks to warrant classification. These deficiencies should be correctable within the normal course of business, although significant changes in company structure or policy may be necessary to correct the deficiencies. These loans are considered bankable assets with no apparent loss of principal or interest envisioned. The perceived risk in continued lending is considered to have increased beyond the level where such loans would normally be granted. Credits that are defined as a troubled debt restructuring should be graded no higher than special mention until they have been reported as performing over one year after restructuring.

The Company uses the following definitions for its classified loan risk ratings:

**Substandard (Loan Grade 9).** Loans classified as substandard represent very high risk, serious delinquency, nonaccrual, or unacceptable credit. Repayment through the primary source of repayment is in jeopardy due to the existence of one or more well defined weaknesses and the collateral pledged may inadequately protect collection of the loans. Loss of principal is not likely if weaknesses are corrected, although financial statements normally reveal significant weakness. Loans are still considered collectible, although loss of principal is more likely than with special mention loan grade 8 loans. Collateral liquidation considered likely to satisfy debt.

**Doubtful (Loan Grade 10).** Loans classified as doubtful display a high probability of loss, although the amount of actual loss at the time of classification is undetermined. This should be a temporary category until such time that actual loss can be identified, or improvements made to reduce the seriousness of the classification. These loans exhibit all substandard characteristics with the addition that weaknesses make collection or liquidation in full highly questionable and improbable. This classification consists of loans

where the possibility of loss is high after collateral liquidation based upon existing facts, market conditions, and value. Loss is deferred until certain important and reasonable specific pending factors which may strengthen the credit can be more accurately determined. These factors may include proposed acquisitions, liquidation procedures, capital injection, receipt of additional collateral, mergers, or refinancing plans. A doubtful classification for an entire credit should be avoided when collection of a specific portion appears highly probable with the adequately secured portion graded substandard.

Criticized and classified loans will mostly consist of commercial and industrial and commercial real estate loans. The Company considers its loans that do not meet the criteria for a criticized and classified asset rating as pass rated loans, which will include loans graded from 1 (Prime) to 7 (Watch). All commercial loans are categorized into a risk category either at the time of origination or reevaluation date. As of March 31, 2016 and December 31, 2015, and based on the most recent analysis performed, the risk category of commercial loans by class of loans was as follows:

| March 31, 2016            | Pass      | Criticized | Classified | Total     |
|---------------------------|-----------|------------|------------|-----------|
| Commercial real estate:   |           |            |            |           |
| Owner-occupied            | \$61,731  | \$5,548    | \$3,838    | \$71,117  |
| Nonowner-occupied         | 61,968    | 1,775      | 7,988      | 71,731    |
| Construction              | 25,375    | ----       | 1,137      | 26,512    |
| Commercial and industrial | 69,708    | 4,809      | 6,517      | 81,034    |
| Total                     | \$218,782 | \$12,132   | \$19,480   | \$250,394 |

| December 31, 2015         | Pass      | Criticized | Classified | Total     |
|---------------------------|-----------|------------|------------|-----------|
| Commercial real estate:   |           |            |            |           |
| Owner-occupied            | \$62,287  | \$6,738    | \$4,433    | \$73,458  |
| Nonowner-occupied         | 61,577    | 6,305      | 4,120      | 72,002    |
| Construction              | 23,080    | ----       | 772        | 23,852    |
| Commercial and industrial | 70,852    | 5,232      | 5,852      | 81,936    |
| Total                     | \$217,796 | \$18,275   | \$15,177   | \$251,248 |

The Company also obtains the credit scores of its borrowers upon origination (if available by the credit bureau), but the scores are not updated. The Company focuses mostly on the performance and repayment ability of the borrower as an indicator of credit risk and does not consider a borrower's credit score to be a significant influence in the determination of a loan's credit risk grading.

For residential and 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 recorded investment of residential and consumer loans by class of loans based on repayment activity as of March 31, 2016 and December 31, 2015:

| March 31, 2016 | Automobile | Consumer Home Equity | Other    | Residential Real Estate | Total     |
|----------------|------------|----------------------|----------|-------------------------|-----------|
| Performing     | \$44,890   | \$19,495             | \$43,906 | \$224,833               | \$333,124 |
| Nonperforming  | 62         | 63                   | 9        | 2,193                   | 2,327     |
| Total          | \$44,952   | \$19,558             | \$43,915 | \$227,026               | \$335,451 |

| December 31, 2015 | Automobile | Consumer Home Equity | Other     | Residential Real Estate | Total      |
|-------------------|------------|----------------------|-----------|-------------------------|------------|
| Performing        | \$ 44,521  | \$ 20,745            | \$ 45,218 | \$ 221,807              | \$ 332,291 |
| Nonperforming     | 45         | 96                   | 4         | 2,068                   | 2,213      |
| Total             | \$ 44,566  | \$ 20,841            | \$ 45,222 | \$ 223,875              | \$ 334,504 |

The Company, through its subsidiaries, originates residential, consumer, and commercial loans to customers located primarily in the southeastern areas of Ohio as well as the western counties of West Virginia. Approximately 6.09% of total loans were unsecured at March 31, 2015, up from 6.06% at December 31, 2015.

#### NOTE 5 - FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit and financial guarantees. The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit, and financial guarantees written, is represented by the contractual amount of those instruments. The contract amounts of these instruments are not included in the consolidated financial statements. At March 31, 2016, the contract amounts of these instruments totaled approximately \$64,405, compared to \$62,415 at December 31, 2015. The Bank uses the same credit policies in making commitments and conditional obligations as it does for instruments recorded on the balance sheet. Since many of these instruments are expected to expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements.



## NOTE 6 - OTHER BORROWED FUNDS

Other borrowed funds at March 31, 2016 and December 31, 2015 are comprised of advances from the Federal Home Loan Bank (“FHLB”) of Cincinnati and promissory notes. At March 31, 2016 and December 31, 2015, FHLB Borrowings included \$106 and \$117 in capitalized lease obligations, respectively.

|                   | FHLB<br>Borrowings | Promissory<br>Notes | Totals   |
|-------------------|--------------------|---------------------|----------|
| March 31, 2016    | \$ 24,215          | \$3,918             | \$28,133 |
| December 31, 2015 | \$ 20,028          | \$3,918             | \$23,946 |

Pursuant to collateral agreements with the FHLB, advances were secured by \$218,299 in qualifying mortgage loans, \$80,271 in commercial loans and \$5,081 in FHLB stock at March 31, 2016. Fixed-rate FHLB advances of \$24,109 mature through 2042 and have interest rates ranging from 1.34% to 3.31% and a year-to-date weighted average cost of 2.09%. There were no variable-rate FHLB borrowings at March 31, 2016.

At March 31, 2016, the Company had a cash management line of credit enabling it to borrow up to \$75,000 from the FHLB. All cash management advances have an original maturity of 90 days. The line of credit must be renewed on an annual basis. There was \$75,000 available on this line of credit at March 31, 2016.

Based on the Company's current FHLB stock ownership, total assets and pledgeable loans, the Company had the ability to obtain borrowings from the FHLB up to a maximum of \$176,455 at March 31, 2016. Of this maximum borrowing capacity, the Company had \$109,346 available to use as additional borrowings, of which \$75,000 could be used for short-term, cash management advances, as mentioned above.

Promissory notes, issued primarily by Ohio Valley, are due at various dates through a final maturity date of December 4, 2017, and have fixed rates ranging from 1.25% to 1.50% and a year-to-date weighted average cost of 1.44% at March 31, 2016, as compared to 1.38% at December 31, 2015. Promissory notes payable by Ohio Valley to related parties totaled \$360 at March 31, 2016.

Letters of credit issued on the Bank's behalf by the FHLB to collateralize certain public unit deposits as required by law totaled \$43,000 at March 31, 2016 and \$34,800 at December 31, 2015.

Scheduled principal payments as of March 31, 2016:

|            | FHLB<br>Borrowings | Promissory<br>Notes | Totals   |
|------------|--------------------|---------------------|----------|
| 2016       | \$1,638            | \$2,416             | \$4,054  |
| 2017       | 4,866              | 1,502               | 6,368    |
| 2018       | 1,807              | ----                | 1,807    |
| 2019       | 1,744              | ----                | 1,744    |
| 2020       | 1,650              | ----                | 1,650    |
| Thereafter | 12,510             | ----                | 12,510   |
|            | \$24,215           | \$3,918             | \$28,133 |

## NOTE 7 – SEGMENT INFORMATION

The reportable segments are determined by the products and services offered, primarily distinguished between banking and consumer finance. They are also distinguished by the level of information provided to the chief operating decision maker, who uses such information to review performance of various components of the business, which are then aggregated if operating performance, products/services, and customers are similar. Loans, investments, and deposits provide the majority of the net revenues from the banking operation, while loans provide the majority of the net revenues for the consumer finance segment. All Company segments are domestic.

Total revenues from the banking segment, which accounted for the majority of the Company's total revenues, totaled 85.7% and 85.9% of total consolidated revenues for the quarters ended March 31, 2016 and 2015, respectively.

The accounting policies used for the Company's reportable segments are the same as those described in Note 1 - Summary of Significant Accounting Policies. Income taxes are allocated based on income before tax expense.

|                     | Three Months Ended March 31, 2016 |                  |               |
|---------------------|-----------------------------------|------------------|---------------|
|                     | Banking                           | Consumer Finance | Total Company |
| Net interest income | \$7,671                           | \$1,429          | \$9,100       |
| Provision expense   | 375                               | 104              | 479           |
| Noninterest income  | 2,832                             | 403              | 3,235         |
| Noninterest expense | 7,194                             | 775              | 7,969         |
| Tax expense         | 731                               | 324              | 1,055         |
| Net income          | 2,202                             | 630              | 2,832         |
| Assets              | 871,819                           | 11,698           | 883,517       |

|                     | Three Months Ended March 31, 2015 |                  |               |
|---------------------|-----------------------------------|------------------|---------------|
|                     | Banking                           | Consumer Finance | Total Company |
| Net interest income | \$ 7,561                          | \$ 1,369         | \$ 8,930      |
| Provision expense   | (175 )                            | 97               | (78 )         |
| Noninterest income  | 3,043                             | 446              | 3,489         |
| Noninterest expense | 6,707                             | 720              | 7,427         |
| Tax expense         | 1,107                             | 339              | 1,446         |
| Net income          | 2,965                             | 659              | 3,624         |
| Assets              | 855,500                           | 12,485           | 867,985       |

#### NOTE 8 – MERGERS AND ACQUISITIONS

On January 7, 2016, Ohio Valley and Milton Bancorp, Inc. (“Milton Bancorp”), entered into an Agreement and Plan of Merger (“Merger Agreement”). The Merger Agreement provides for a business combination whereby Milton Bancorp will merge with and into Ohio Valley and Milton Bancorp’s banking subsidiary, The Milton Banking Company, will merge with and into the Bank. At the effective time and as a result of the Merger, each of the 400 Milton Bancorp common shares issued and outstanding shall be converted into the right to receive, at the election of the holder thereof, the following: (i) 1,636 of Ohio Valley’s common shares; (ii) cash in the amount of \$37,219; or (iii) a combination of cash and Ohio Valley common shares. The form of consideration to be received by each Milton Bancorp shareholder is subject to reallocation in order to ensure that 20% of the outstanding Milton Bancorp shares are exchanged for cash and 80% of the outstanding Milton Bancorp shares are exchanged for Ohio Valley common shares. Each of the 1,237 Milton Bancorp preferred shares issued and outstanding shall be converted into the right to receive a cash payment in the amount of \$3,600 per Milton Bancorp preferred share. Ohio Valley intends to finance all or part of the cash portion of the purchase price through borrowed funds. Milton Bancorp operates five branches with assets of \$141 million, loans of \$110 million and deposits of \$126 million. After the merger, the Company's total assets will exceed \$900 million and branches will increase to 19 locations. The merger consideration was valued at \$20 million at the time of signing the merger agreement. The transaction is subject to certain conditions, including the approval of regulatory authorities and the shareholders of Milton Bancorp. The merger is expected to be completed by the third quarter of 2016.



## ITEM 2.MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(dollars in thousands, except share and per share data)

### Forward Looking Statements

Except for the historical statements and discussions contained herein, statements contained in this report constitute "forward looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Act of 1934 and as defined in the Private Securities Litigation Reform Act of 1995. Such statements are often, but not always, identified by the use of such words as "believes," "anticipates," "expects," and similar expressions. Such statements involve various important assumptions, risks, uncertainties, and other factors, many of which are beyond our control and which could cause actual results to differ materially from those expressed in such forward looking statements. These factors include, but are not limited to: changes in political, economic or other factors, such as inflation rates, recessionary or expansive trends, taxes, the effects of implementation of legislation and the continuing economic uncertainty in various parts of the world; competitive pressures; fluctuations in interest rates; the level of defaults and prepayment on loans made by the Company; unanticipated litigation, claims, or assessments; fluctuations in the cost of obtaining funds to make loans; and regulatory changes. Additional detailed information concerning a number of important factors which could cause actual results to differ materially from the forward-looking statements contained in management’s discussion and analysis is available in the Company’s filings with the Securities and Exchange Commission, under the Securities Exchange Act of 1934, including the disclosure under the heading “Item 1A. Risk Factors” of Part 1 of the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2015. Readers are cautioned not to place undue reliance on such forward looking statements, which speak only as of the date hereof. The Company undertakes no obligation and disclaims any intention to republish revised or updated forward looking statements, whether as a result of new information, unanticipated future events or otherwise.

### Financial Overview

The Company is primarily engaged in commercial and retail banking, offering a blend of commercial and consumer banking services within southeastern Ohio as well as western West Virginia. The banking services offered by the Bank include the acceptance of deposits in checking, savings, time and money market accounts; the making and servicing of personal, commercial, floor plan and student loans; the making of construction and real estate loans; and credit card services. The Bank also offers individual retirement accounts, safe deposit boxes, wire transfers and other standard banking products and services. In addition, the Bank is one of a limited number of financial institutions that facilitates the payment of tax refunds through a third-party tax refund product provider. The Bank has facilitated the payment of these tax refunds through electronic refund check/deposit (“ERC/ERD”) transactions. ERC/ERD transactions involve the payment of a tax refund to the taxpayer after the Bank has received the refund from the federal/state government. ERC/ERD transactions occur primarily during the tax refund season, typically during the first quarter of each year. Loan Central also provides refund anticipation loans (“RALs”) to its customers. RALs are short-term cash advances against a customer’s anticipated income tax refund.

Net income totaled \$2,832 during the first quarter of 2016, a decrease of \$792, or 21.9%, compared to \$3,624 during the first quarter of 2015. Earnings per share for the first quarter of 2016 also decreased by \$.19, or 78.4%, compared to the first quarter of 2015, to finish at \$.69 per share. The decrease in earnings compared to the first quarter of 2015 was largely due to increases in provision for loan loss and merger related expenses combined with lower ERC/ERD processing fees. The annualized net income to average asset ratio, or return on assets (“ROA”), decreased to 1.29% at March 31, 2016, compared to 1.67% at March 31, 2015. The Company’s net income to average equity ratio, or return

on equity (“ROE”), also decreased to 12.50% at March 31, 2016, compared to 16.94% at March 31, 2015.

Net interest income for the three months ended March 31, 2016 increased \$170, or 1.9%, over the first quarter of 2015. The increase was primarily due to higher interest revenue recorded from the Company’s interest-bearing Federal Reserve clearing account. During the first quarter of 2016, average interest-bearing balances maintained at the Federal Reserve grew 4.7% over the first quarter of 2015, impacted by seasonal tax processing activity. With the Federal Reserve increasing short-term interest rates in December 2015 by 25 basis points, the interest earned on the heightened liquidity maintained during the first quarter contributed an additional \$97 to interest income for 2016. Furthermore, the higher rate on balances maintained at the Federal Reserve contributed to an increase in the net interest margin, which finished at 4.50% during the first quarter 2016, as compared to 4.45% during the first quarter of 2015. Margin improvement was also enhanced by lower deposit expenses, as rates continued to adjust downward during 2015. As a result, the average cost of interest-bearing deposit liabilities finished at 0.41% during the first quarter of 2016, as compared to 0.44% during the same period in 2015. Partially offsetting net interest margin growth was a \$1,718 decline in average earning assets during the first quarter of 2016. Comparing the first quarter of 2016 to the first quarter of 2015, average loan balances decreased \$11,531, or 1.9%, which was partially offset by growth in average investments and Federal Reserve balances. The decrease in average loan balances was primarily related to a decrease in average participation loans of \$12,804 due to an increase in payoffs.

In 2016, provision expense increased \$557 over the prior year's first quarter. The increase in provision expense was partly due to an increase in net charge-offs. For the three months ended March 31, 2016, net charge-offs totaled \$181, an increase of \$245 from the net recoveries of \$64 for the three months ended March 31, 2015. Furthermore, the general reserve for loan losses increased due to certain economic risk factors, such as the balance of classified loans, which was partially offset by the improvement in lower historical loan loss factors. The allowance for loan losses was 1.19 percent of total loans at March 31, 2016, compared to 1.13 percent at December 31, 2015 and 1.40 percent at March 31, 2015.

Total noninterest income was \$3,235 for the quarter ended March 31, 2016, which was \$254 lower than the prior year's first quarter. Year-over-year decreases were largely due to lower tax processing fees through ERC/ERD transactions. Although the volume of tax refunds processed increased during the first quarter of 2016, the per item fees received by the Company were lower under the new contract with the third-party tax refund product provider. Tax refund processing fees totaled \$1,754, a decrease of \$341 from the same period during 2015. The remaining noninterest categories increased \$87, or 6.2%, led by service charges on deposit accounts, earnings from tax-free bank owned life insurance ("BOLI") investments and interchange fees earned on debit and credit card transactions.

Total noninterest expense was \$7,969 for the quarter ended March 31, 2016, an increase of 7.3% from the prior year's first quarter. The increase was primarily related to merger expenses related to the announced merger with Milton Bancorp, Inc. ("Milton Bancorp"), as well as increases in salaries and employee benefit costs due to annual merit increases and higher health insurance costs.

At March 31, 2016, total assets were \$883,517, compared to \$796,285 at year-end 2015, with the increase due mostly to temporary interest-bearing deposits into the Company's Federal Reserve clearing account that were generated from seasonal tax clearing activities during the first quarter of 2016. Gross loan balances of \$585,845 at March 31, 2016 were relatively the same when compared to year-end 2015, increasing just \$93. Total investment securities decreased 3.6% to \$107,485 at March 31, 2016, compared to \$111,554 at year-end 2015, mostly from monthly principal repayments of mortgage-backed securities.

Total liabilities were \$789,886 at March 31, 2016, up \$84,071 since December 31, 2015. Total deposit balances experienced continued growth during 2016, increasing \$80,259 compared to year-end 2015. Noninterest-bearing deposits accounted for \$64,143 of the increase and were the result of normal seasonal increases in tax refund processing activities and municipal public fund deposit balances.

At March 31, 2016, total shareholders' equity was \$93,631, up \$3,161 since December 31, 2015. Regulatory capital ratios remained significantly higher than the "well capitalized" minimums.

Comparison of  
Financial Condition  
at March 31, 2016 and December 31, 2015

The following discussion focuses, in more detail, on the consolidated financial condition of the Company at March 31, 2016 compared to December 31, 2015. This discussion should be read in conjunction with the interim consolidated financial statements and the footnotes included in this Form 10-Q.

Cash and Cash Equivalents

At March 31, 2016, cash and cash equivalents increased \$93,774, to finish at \$139,304, compared to \$45,530 at December 31, 2015. The increase in cash and cash equivalents was largely due to deposit liability growth from

year-end 2015, mostly from seasonal increases in ERC/ERD transactions. The Company continues to utilize its interest-bearing Federal Reserve Bank clearing account to maintain these excess funds, which are expected to decrease during the remainder of 2016. The interest rate paid on both the required and excess reserve balances is based on the targeted federal funds rate established by the Federal Open Market Committee, which currently is 0.50%. In December 2015, short-term interest rates were increased by 25 basis points, which had a corresponding effect to the interest revenue growth experienced during the first quarter of 2016 on Federal Reserve Bank clearing account balances. This interest rate is higher than what the Company would have received from its investments in federal funds sold, currently in a range of less than 0.50%. Furthermore, Federal Reserve Bank balances are 100% secured.



As liquidity levels vary continuously based on consumer activities, amounts of cash and cash equivalents can vary widely at any given point in time. The Company's focus will be to invest excess funds into longer-term, higher-yielding assets, primarily loans, when the opportunities arise.

#### Certificates of deposit

At March 31, 2016, the Company had \$1,470 in certificates of deposit owned by the Captive. This represented a decrease of \$245, or 14.3%, from year-end 2015. During the first quarter of 2016, the Captive experienced one certificate maturity of \$245. The deposits on hand at March 31, 2016 consist of six certificates with maturity terms ranging from 1.5 to 3 years.

#### Securities

The balance of total securities decreased \$4,069, or 3.6%, compared to year-end 2015. The decrease came mostly from U.S. Government agency ("Agency") mortgage-backed securities, which decreased \$2,701, or 3.3%, from year-end 2015. The Company's investment securities portfolio is made up mostly of agency mortgage-backed securities, representing 74.4% of total investments at March 31, 2016. During the first quarter of 2016, the Company received principal repayments of \$3,539, which has been the primary advantage of Agency mortgage-backed securities as compared to other types of investment securities, which deliver proceeds upon maturity or call date.

#### Loans

The loan portfolio represents the Company's largest asset category and is its most significant source of interest income. Gross loan balances were consistent with year-end, totaling \$585,845 at March 31, 2016, as compared to \$585,752 at December 31, 2015. Loan balances were positively impacted by growth in residential real estate balances, partially offset by decreases in commercial and consumer loans.

The commercial lending segment decreased \$854, or 0.3%, from year-end 2015, which came partly from the commercial and industrial loan portfolio, which decreased \$902, or 1.1%, from year-end 2015. Commercial and industrial loans consist of loans to corporate borrowers primarily in small to mid-sized industrial and commercial companies that include service, retail and wholesale merchants. Collateral securing these loans includes equipment, inventory, and stock. The commercial real estate loan segment comprises the largest portion of the Company's total commercial loan portfolio, representing 67.6% at March 31, 2016, with net loan balances remaining relatively unchanged from year-end 2015. Loan volume contributed to construction loans being up \$2,660, or 11.2%, from year-end 2015, while larger payoffs caused owner-occupied loans to decrease \$2,341, or 3.2%, from year-end 2015. While management believes lending opportunities exist in the Company's markets, future commercial lending activities will depend upon economic and related conditions, such as general demand for loans in the Company's primary markets, interest rates offered by the Company, the effects of competitive pressure and normal underwriting considerations. Management will continue to place emphasis on its commercial lending, which generally yields a higher return on investment as compared to other types of loans.

Consumer loan balances decreased \$2,204, or 2.0%, from year-end 2015. This decrease was impacted most by a 2.9% decrease in other consumer loan balances that include mobile homes, recreational vehicles, consumer real estate and unsecured loans. Furthermore, consumer home equity lines were down \$1,283, or 6.2%, from year-end 2015. These decreases were partially offset by a 0.9% increase in automobile loans. Automobile loans represent the Company's largest consumer loan segment at 41.5% of total consumer loans. The Company will continue to monitor its auto lending segment while maintaining strict loan underwriting processes to limit future loss exposure.

The residential real estate loan segment comprises the largest portion of the Company's loan portfolio at 38.8% and consists primarily of one- to four-family residential mortgages and carries many of the same customer and industry risks as the commercial loan portfolio. Residential real estate loan balances during the first quarter of 2016 increased \$3,151, or 1.4%, from year-end 2015. Movement within the real estate portfolio consists of increasing short-term adjustable-rate mortgages partially offset by decreasing long-term fixed-rate mortgages. As part of management's interest rate risk strategy, the Company continues to sell most of its long-term fixed-rate residential mortgages to the Federal Home Loan Mortgage Corporation, while maintaining the servicing rights for those mortgages. A customer that does not qualify for a long-term, secondary market loan may choose from one of the Company's other adjustable-rate mortgage products, which contributed to higher balances of adjustable-rate mortgages from year-end 2015.

## Allowance for Loan Losses

The Company established a \$6,946 allowance for loan losses at March 31, 2016, which was up from the \$6,648 allowance at year-end 2015. The allowance reserves were impacted by higher general allocations from year-end 2015 impacted by the economic risk factors within the calculation of the allowance for loan losses. As part of the Company's quarterly analysis of the allowance for loan losses, management reviewed various factors that directly impact the general allocation need of the allowance, which include: historical loan losses, loan delinquency levels, local economic conditions and unemployment rates, criticized/classified asset coverage levels and loan loss recoveries. During the first quarter of 2016, the Company experienced an increase in its classified assets from year-end 2015, which contributed to most of the general allocation increases within all segments of the loan portfolio. These allocation increases were partially offset by the positive effects of lower criticized assets and a decreasing historical loss factor from year-end 2015. The changes in both classified and criticized assets from year-end 2015 came primarily from nonowner-occupied commercial real estate loans. As a result, the general allocation component of the allowance for loan losses increased \$250, or 5.6%, from year-end 2015.

Specific allocations of the allowance for loan losses identify loan impairment by measuring fair value of the underlying collateral and the present value of estimated future cash flows. When re-evaluating the impaired loan balances to their corresponding collateral values at March 31, 2016, a specific allocation of \$2,212 was needed to fund the allowance for loan losses, representing an increase of \$48, or 2.2%, from year-end 2015. This higher reserve allocation was impacted mostly by one commercial and industrial loan relationship.

The Company experienced no change in its troubled assets, with nonperforming loans to total loans finishing at 1.24% at March 31, 2016 and December 31, 2015. The Company's nonperforming assets to total assets finished at 1.07% at March 31, 2016, a decrease of 14 basis points from year-end 2015. Impaired loans at March 31, 2016 increased \$611, or 3.6%, from year-end 2015, largely from the debt restructures of two nonowner-occupied commercial real estate loans during the first quarter of 2016.

The Company maintained its allowance for loan losses to total loans ratio at 1.19% at March 31, 2016 and 1.13% at year-end 2015. Management believes that the allowance for loan losses at March 31, 2016 was adequate and reflected probable incurred losses in the loan portfolio. There can be no assurance, however, that adjustments to the allowance for loan losses will not be required in the future. Changes in the circumstances of particular borrowers, as well as adverse developments in the economy, are factors that could change and make adjustments to the allowance for loan losses necessary. Asset quality will continue to remain a key focus, as management continues to stress not just loan growth, but quality in loan underwriting, as well.

## Deposits

Deposits continue to be the most significant source of funds used by the Company to meet obligations for depositor withdrawals, to fund the borrowing needs of loan customers, and to fund ongoing operations. Total deposits at March 31, 2016 increased \$80,259, or 12.1%, from year-end 2015. This deposit growth came primarily from noninterest-bearing deposit balances. During the first quarter of 2016, the Company experienced a significant increase in its business checking account balances, which increased \$65,898, or 66.7%, from year-end 2015. This increase was largely the result of ERC/ERD tax refund items processed during the first quarter of 2016. During 2016, the Company benefited from the successful volume increase in ERC/ERD transactions. As a result of the tax processing activity being seasonal, the elevated first quarter balances within the Company's business checking accounts should decrease during the remainder of 2016.

Deposit growth also came from interest-bearing NOW account balances, which increased \$18,935, or 15.2%, during the first three months of 2016 as compared to year-end 2015. This increase was largely driven by growth in municipal

NOW products due to seasonality of tax collections received, which typically decrease in the second quarter.

During the first quarter of 2016, time deposits decreased \$4,323, or 2.7%, from year-end 2015. As CD market rates continue to adjust downward, the spread between a short-term CD rate and a statement savings rate has become small enough that many customers choose to invest balances into a more liquid product, perhaps hoping for rising rates in the near future. This change in time deposits from year-end 2015 fits within management's strategy of focusing on more "core" deposit balances that include interest-bearing demand, savings, money market and noninterest-bearing deposit balances.

While facing increased competition for deposits in its market areas, the Company will continue to emphasize growth and retention in its core deposit relationships during the remainder of 2016, reflecting the Company's efforts to reduce its reliance on higher cost funding and improving net interest income.

#### Other Borrowed Funds

Other borrowed funds were \$28,133 at March 31, 2016, an increase of \$4,187, or 17.5%, from year-end 2015. The increase was related to management's decision to fund a specific fixed-rate loan with like-term FHLB advances during the first quarter of 2016. While deposits continue to be the primary source of funding for growth in earning assets, management will continue to utilize Federal Home Loan Bank advances and promissory notes to help manage interest rate sensitivity and liquidity.

#### Shareholders' Equity

The Company maintains a capital level that exceeds regulatory requirements as a margin of safety for its depositors. At March 31, 2016, the Bank's capital exceeded the minimum requirements to be deemed "well capitalized" under applicable prompt corrective action regulations. Total shareholders' equity at March 31, 2016 of \$93,631 increased \$3,161, or 3.5%, as compared to \$90,470 at December 31, 2015. Contributing most to this increase was year-to-date net income of \$2,832, partially offset by cash dividends paid of \$865, or \$.21 per share.

#### Comparison of Results of Operations for the Three Months Ended March 31, 2016 and 2015

The following discussion focuses, in more detail, on the consolidated results of operations of the Company for the three months ended March 31, 2016 compared to the same period in 2015. This discussion should be read in conjunction with the interim consolidated financial statements and the footnotes included in this Form 10-Q.

#### Net Interest Income

The most significant portion of the Company's revenue, net interest income, results from properly managing the spread between interest income on earning assets and interest expense incurred on interest-bearing liabilities. During the first quarter of 2016, net interest income increased \$170, or 1.9%, as compared to the first quarter of 2015. The improvement came primarily from higher interest income on interest-bearing deposits with banks and consumer loan balances, while also benefiting from lower premium expenses on investment securities and a reduction in deposit expenses.

Total interest and fee income recognized on the Company's earning assets increased \$143, or 1.5%, during the first quarter of 2016, as compared to the same period in 2015, mostly impacted by other interest income sources. During the first quarter of 2016, total other interest income totaled \$167, an increase of \$101, or 153.0%, from the first quarter of 2015. The increase was primarily due to higher interest revenue recorded from the Company's interest-bearing Federal Reserve clearing account. The Company continues to utilize its Federal Reserve clearing account to manage

seasonal tax refund deposits and fund earning asset growth. This interest-bearing account carried an interest rate of 0.25% during most of 2015. In December 2015, the Federal Reserve increased short-term rates by 25 basis points, which increased the Federal Reserve clearing account's interest rate from 0.25% to 0.50%. The timing of this rate adjustment benefited the Company, as it entered into the first quarter experiencing significant levels of excess funds impacted by the large volume of ERC/ERD transactions that were maintained within the Federal Reserve clearing account. This contributed to a \$97, or 150.8%, increase to interest income during the first quarter of 2016.

Total interest and fees on loans also increased \$28, or 0.3%, during the first quarter of 2016, as compared to the same period in 2015. The improvement came mostly from the average balance growth in both consumer and residential real estate loan portfolios, which contributed to a \$130, or 2.3%, increase in interest and fees during the first three months of 2016, as compared to the first three months of 2015. Partially offsetting this increase was a \$102, or 3.2%, decrease in commercial interest and fee income during the first three months of 2016, as compared to the first three months of 2015. This decrease was mostly the result of the significant payoffs of various commercial loan participations over the past 12 months.

The Company further benefited from increased earnings within investment securities, which increased \$14, or 2.4%, during the first quarter of 2016, as compared to the same period in 2015, coming primarily from Agency mortgage-backed securities. The investment prices for Agency mortgage-backed securities continue to adjust closer to their par values, resulting in less monthly premium expense and higher return yields.

Yields on the Company's earning assets were positively impacted by the Federal Reserve's 25 basis point increase in short-term interest rates from December 2015. The effect of this rate adjustment was felt mostly in the higher average balances associated with the Federal Reserve clearing account. As a result, the earning asset yield at March 31, 2016 was 4.83%, compared to 4.79% at March 31, 2015.

Total interest expense incurred on the Company's interest-bearing liabilities during the first quarter of 2016 decreased \$37, or 6.9%, from the same period in 2015. The decrease was primarily due to a sustained low-rate environment that impacted the repricings of various Bank deposit products, including certain interest-bearing demand accounts. This contributed to a lower weighted average cost of the Company's core deposits, which finished at 0.23% at March 31, 2016, as compared to 0.27% at March 31, 2015. The Company continues to utilize more of its lower cost, core deposit funding sources to further reduce interest expense. As a result, the Company's average interest- and non-interest bearing core deposits increased \$15,541, or 2.7%, while the higher costing, average time deposit balances decreased \$16,378, or 9.5%, during the first three months of 2016, as compared to the same period in 2015. The decreases in average market interest rates and the continued emphasis on utilizing lower costing deposit balances have caused the Company's total weighted average costs on interest-bearing deposits to decrease by 3 basis points from 0.44% at March 31, 2015 to 0.41% at March 31, 2016.

During 2016, the Company has benefited from both an increase in asset yields and a decline in funding costs. As a result, the Company's net interest margin improved 5 basis points to 4.50% during the first quarter of 2016, as compared to the same period in 2015. While the Company benefited in the first quarter of 2016 from a heightened level of excess funds within its Federal Reserve clearing account, the focus will be on re-deploying the retained portion of these funds to higher yielding assets as opportunities arise. The Company will continue to face pressure on its net interest income and margin improvement unless loan balances continue to expand and remain a larger component of overall earning assets.

#### Provision for Loan Losses

During the first quarter of 2016, the Company experienced provision expense charges of \$479, as compared to negative provision expense of \$78 during the first quarter of 2015. Provision expense during 2016 was impacted by net charge-offs, which totaled \$181 and came mostly from consumer loans. Negative provision expense during 2015 was impacted by higher net recoveries of previously charged-off loans. Furthermore, the Company experienced a higher general allocation need within the allowance for loan losses in 2016, caused by increases in classified asset balances. Classified assets totaled \$26,402 at March 31, 2016, which were up from \$22,566 in classified assets at year-end 2015. The higher classified numbers contributed to an upward adjustment to the Company's economic risk factor from 0.32% at year-end 2015 to 0.41% at March 31, 2016.

Future provisions to the allowance for loan losses will continue to be based on management's quarterly in-depth evaluation that is discussed in further detail under the caption "Critical Accounting Policies - Allowance for Loan Losses" within this Management's Discussion and Analysis.

#### Noninterest Income

Noninterest income for the three months ended March 31, 2016 was \$3,235, a decrease of \$254, or 7.3%, from the three months ended March 31, 2015. Lower noninterest income during 2016 was largely affected by the Company's

seasonal ERC/ERD fees, which decreased \$341, or 16.3%, from the prior year. In October 2014, the Bank entered into a new agreement with the third-party tax refund product provider, which lowered the per transaction fee associated with each refund facilitated. As a result, even though the Company experienced an increase in the number of ERC/ERD transactions that were facilitated, the lower fee structure caused tax processing revenues to be lower than the year before. As a result of ERC/ERD fee activity being mostly seasonal, the majority of income will be recorded during the first half of 2016, with only minimal income expected during the second half of 2016.



The Company's remaining noninterest income categories were collectively up \$87, or 6.2%, during the first quarter of 2016, when compared to the same period in 2015. These changes were primarily due to increases in service charges on deposit accounts, earnings from tax-free BOLI investments and interchange fees earned on debit and credit card transactions.

#### Noninterest Expense

Noninterest expense during the first quarter of 2016 increased \$542, or 7.3%, from the first quarter in 2015. Contributing to the increase in net overhead expense were merger related expenses and higher salaries and employee benefits.

The Company's largest noninterest expense item, salaries and employee benefits, increased \$170, or 3.9%, during the three months ended March 31, 2016, when compared to the same period in 2015. The increase was largely due to annual merit increases and higher health insurance costs.

In January 2016, the Company entered into a merger agreement with Milton Bancorp, which will result in the business combination of both holding companies and their respective bank subsidiaries. In preparation for the merger, both the Company and the Bank have experienced various merger related expenses totaling \$227. The merger is expected to be completed in the third quarter of 2016, and as a result, the Company anticipates merger expenses to increase throughout the remainder of the year.

The net change in remaining noninterest expense categories during the first quarter of 2016 increased \$145, or 4.8%, as compared to the same period in 2015.

The Company's efficiency ratio is defined as noninterest expense as a percentage of fully tax-equivalent net interest income plus noninterest income. The effects from provision expense are excluded from the efficiency ratio. Management continues to place emphasis on managing its balance sheet mix and interest rate sensitivity as well as developing more innovative ways to generate noninterest revenue. During the first quarter of 2016, the Company was successful in generating more net interest income primarily due to higher interest-bearing deposits with banks while reducing funding costs by 3.9%. However, a 16.3% decline in tax processing fees combined with higher personnel and merger costs caused overhead expense to outpace net revenue levels during 2016. As a result, the first quarter 2016 efficiency ratio regressed to 63.8%, as compared to a stronger 59.0% efficiency ratio during the first quarter of 2015.

#### Capital Resources

Banks and bank holding companies are subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Company and the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Under the final rules, minimum requirements increased for both the quantity and quality of capital held by the Company and the Bank. The rules include a new common equity tier 1 capital to risk-weighted assets ratio of 4.5% and a capital conservation buffer of 2.5% of risk-weighted assets. The capital conservation buffer began to phase in on January 1, 2016 at 0.625%, and will be phased in over a four-year period, increasing by the same amount on each subsequent January 1, until fully phased-in on January 1, 2019. Further, Basel III rules increased the minimum ratio of tier 1 capital to risk-weighted assets increased from 4.0% to 6.0% and all

banks are now subject to a 4.0% minimum leverage ratio. The required total risk-based capital ratio was unchanged. Failure to maintain the required common equity tier 1 capital conservation buffer will result in potential restrictions on a bank's ability to pay dividends, repurchase stock and/or pay discretionary compensation to its employees.

Effective May 15, 2015, the Federal Reserve Board amended the Small Bank Holding Company Policy ("the Policy") that increased from \$500 million to \$1 billion the asset threshold for a bank to qualify under the Policy. The Company qualifies for treatment under the Policy and, at March 31, 2016 and year-end 2015, is no longer subject to the consolidated capital rules at the bank holding company level. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital. Management believes that as of March 31, 2016 and year-end 2015, the Bank met all capital adequacy requirements to which it was subject. Furthermore, when compared to the regulatory minimum, the Bank's tier 1, common equity tier 1, and total risk-based capital ratios exceeded the new capital conservation buffer of 0.625% at March 31, 2016.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At March 31, 2016 and year-end 2015, the Bank met the capital requirements to be deemed well capitalized under the regulatory framework for prompt corrective action.

The following table summarizes the capital ratios of the Company and Bank and the minimum regulatory requirements:

|   | 3/31/16 | 12/31/15 | Regulatory Minimum |
|---|---------|----------|--------------------|
| Common equity tier 1 risk-based capital ratio |         |          |                    |
| Company                                       | 16.1%   | 15.6%    | N/A                |
| Bank  | 15.5%   | 15.1%    | 4.5%               |
| Tier 1 risk-based capital ratio               |         |          |                    |
| Company                                       | 17.6%   | 17.1%    | N/A                |
| Bank  | 15.5%   | 15.1%    | 6.0%               |
| Total risk-based capital ratio                |         |          |                    |
| Company                                       | 18.8%   | 18.2%    | N/A                |
| Bank  | 16.7%   | 16.3%    | 8.0%               |
| Leverage ratio                                |         |          |                    |
| Company                                       | 11.4%   | 12.2%    | N/A                |
| Bank  | 10.0%   | 10.8%    | 4.0%               |

Cash dividends paid by the Company were \$865 during the first three months of both 2016 and 2015. The year-to-date dividend rate was \$0.21 per share for both 2016 and 2015.

#### Liquidity

Liquidity relates to the Company's ability to meet the cash demands and credit needs of its customers and is provided by the ability to readily convert assets to cash and raise funds in the market place. Total cash and cash equivalents, held to maturity securities maturing within one year and available for sale securities, totaling \$227,544, represented 25.8% of total assets at March 31, 2016. In addition, the FHLB offers advances to the Bank, which further enhances the Bank's ability to meet liquidity demands. At March 31, 2016, the Bank could borrow an additional \$109,346 from the FHLB, of which \$75,000 could be used for short-term, cash management advances. Furthermore, the Bank has established a borrowing line with the Federal Reserve. At March 31, 2016, this line had total availability of \$41,499. Lastly, the Bank also has the ability to purchase federal funds from a correspondent bank.

#### Off-Balance Sheet Arrangements

As discussed in Note 5 – Financial Instruments with Off-Balance Sheet Risk, the Company engages in certain off-balance sheet credit-related activities, including commitments to extend credit and standby letters of credit, which could require the Company to make cash payments in the event that specified future events occur. Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of

a fee. Standby letters of credit are conditional commitments to guarantee the performance of a customer to a third party. While these commitments are necessary to meet the financing needs of the Company's customers, many of these commitments are expected to expire without being drawn upon. Therefore, the total amount of commitments does not necessarily represent future cash requirements.

#### Critical Accounting Policies

The most significant accounting policies followed by the Company are presented in Note A to the financial statements in the Company's 2015 Annual Report to Shareholders. These policies, along with the disclosures presented in the other financial statement notes, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Management views critical accounting policies to be those which are highly dependent on subjective or complex judgments, estimates and assumptions, and where changes in those estimates and assumptions could have a significant impact on the financial statements. Management currently views the adequacy of the allowance for loan losses to be a critical accounting policy.

The allowance for loan losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other 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.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired. 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. Impaired loans generally consist of loans with balances of \$200 or more on nonaccrual status or nonperforming in nature. Loans for which the terms have been modified, 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 and reasons for the delay, the borrower's prior payment record, and the amount of shortfall in relation to the principal and interest owed.

Commercial and commercial real estate loans are individually evaluated for impairment. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Smaller balance homogeneous loans, such as consumer and most residential real estate, are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosure. Troubled debt restructurings are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a troubled debt restructuring is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. For troubled debt restructurings that subsequently default, the Company determines the amount of reserve in accordance with the accounting policy for the allowance for loan losses.

The general component covers non-impaired loans and impaired loans that are not individually reviewed for impairment and is based on historical loss experience adjusted for current factors. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the most recent 3 years for the consumer and real estate portfolio segment and 5 years for the commercial portfolio segment. The total loan portfolio's actual loss experience is supplemented with other economic factors based on the risks present for each portfolio segment. These economic factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; and effects of changes in credit concentrations. The following portfolio segments have been identified: Commercial Real Estate, Commercial and Industrial, Residential Real Estate, and Consumer.

Commercial and industrial loans consist of borrowings for commercial purposes by individuals, corporations, partnerships, sole proprietorships, and other business enterprises. Commercial and industrial loans are generally secured by business assets such as equipment, accounts receivable, inventory, or any other asset excluding real estate and generally made to finance capital expenditures or operations. The Company's risk exposure is related to deterioration in the value of collateral securing the loan should foreclosure become necessary. Generally, business

assets used or produced in operations do not maintain their value upon foreclosure, which may require the Company to write down the value significantly to sell.

Commercial real estate consists of nonfarm, nonresidential loans secured by owner-occupied and nonowner-occupied commercial real estate as well as commercial construction loans. An owner-occupied loan relates to a borrower purchased building or space for which the repayment of principal is dependent upon cash flows from the ongoing business operations conducted by the party, or an affiliate of the party, who owns the property. Owner-occupied loans that are dependent on cash flows from operations can be adversely affected by current market conditions for their product or service. A nonowner-occupied loan is a property loan for which the repayment of principal is dependent upon rental income associated with the property or the subsequent sale of the property. Nonowner-occupied loans that are dependent upon rental income are primarily impacted by local economic conditions which dictate occupancy rates and the amount of rent charged. Commercial construction loans consist of borrowings to purchase and develop raw land into one- to four-family residential properties. Construction loans are extended to individuals as well as corporations for the construction of an individual or multiple properties and are secured by raw land and the subsequent improvements. Repayment of the loans to real estate developers is dependent upon the sale of properties to third parties in a timely fashion upon completion. Should there be delays in construction or a downturn in the market for those properties, there may be significant erosion in value which may be absorbed by the Company.

Residential real estate loans consist of loans to individuals for the purchase of one- to four-family primary residences with repayment primarily through wage or other income sources of the individual borrower. The Company's loss exposure to these loans is dependent on local market conditions for residential properties as loan amounts are determined, in part, by the fair value of the property at origination.

Consumer loans are comprised of loans to individuals secured by automobiles, open-end home equity loans and other loans to individuals for household, family, and other personal expenditures, both secured and unsecured. These loans typically have maturities of 6 years or less with repayment dependent on individual wages and income. The risk of loss on consumer loans is elevated as the collateral securing these loans, if any, rapidly depreciate in value or may be worthless and/or difficult to locate if repossession is necessary. During the last several years, one of the most significant portions of the Company's net loan charge-offs have been from consumer loans. Nevertheless, the Company has allocated the highest percentage of its allowance for loan losses as a percentage of loans to the other identified loan portfolio segments due to the larger dollar balances associated with such portfolios.

#### Concentration of Credit Risk

The Company maintains a diversified credit portfolio, with residential real estate loans currently comprising the most significant portion. Credit risk is primarily subject to loans made to businesses and individuals in southeastern Ohio and western West Virginia. Management believes this risk to be general in nature, as there are no material concentrations of loans to any industry or consumer group. To the extent possible, the Company diversifies its loan portfolio to limit credit risk by avoiding industry concentrations.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's goal for interest rate sensitivity management is to maintain a balance between steady net interest income growth and the risks associated with interest rate fluctuations. Interest rate risk ("IRR") is the exposure of the Company's financial condition to adverse movements in interest rates. Accepting this risk can be an important source of profitability, but excessive levels of IRR can threaten the Company's earnings and capital.

The Company evaluates IRR through the use of an earnings simulation model to analyze net interest income sensitivity to changing interest rates. The modeling process starts with a base case simulation, which assumes a static balance sheet and flat interest rates. The base case scenario is compared to rising and falling interest rate scenarios assuming a parallel shift in all interest rates. Comparisons of net interest income and net income fluctuations from the flat rate scenario illustrate the risks associated with the current balance sheet structure.

The Company's Asset/Liability Committee monitors and manages IRR within Board approved policy limits. The current IRR policy limits anticipated changes in net interest income to an instantaneous increase or decrease in market interest rates over a 12 month horizon to +/- 5% for a 100 basis point rate shock, +/- 7.5% for a 200 basis point rate shock and +/- 10% for a 300 basis point rate shock. Based on the level of interest rates, management did not test interest rates down 200 or 300 basis points.



The following table presents the Company's estimated net interest income sensitivity:

| Change in Interest Rates<br>in Basis Points | March 31, 2016<br>Percentage Change in<br>Net Interest Income | December 31, 2015<br>Percentage Change in<br>Net Interest Income |
|---|---|--|
| +300  | 6.99%   | (.03%)   |
| +200  | 4.84%   | .18%   |
| +100  | 2.53%   | .19%   |
| -100  | (3.49%)   | (2.48%)  |

The estimated percentage change in net interest income due to a change in interest rates was within the policy guidelines established by the Board. With the historical low interest rate environment, management generally has been focused on limiting the duration of assets, while trying to extend the duration of our funding sources to the extent customer preferences will permit the Company to do so. At March 31, 2016, the interest rate risk profile reflects an asset sensitive position, which produces higher net interest income due to an increase in interest rates. Contributing to the change in interest rate risk profile from December 31, 2015, was the significant increase in liquidity due to tax refund processing. The additional liquidity is maintained in an interest-bearing account at the Federal Reserve and the interest rate is highly correlated to any rate change implemented by the Federal Reserve as part of its monetary policy. Since the deposit balance associated with tax refund processing is seasonal, management expects a portion of the balance maintained at the Federal Reserve to decline in subsequent quarters, which will reduce or eliminate our asset sensitive position. In a declining rate environment, net interest income is impacted by the interest rate on many deposit accounts not being able to adjust downward. With interest rates so low, deposit accounts are perceived to be at or near an interest rate floor. As a result, net interest income decreases in a declining interest rate environment. Overall, management is comfortable with the current interest rate risk profile, which reflects minimal exposure to interest rate changes.

#### ITEM 4. CONTROLS AND PROCEDURES

##### Evaluation of Disclosure Controls and Procedures

With the participation of the Chief Executive Officer (the principal executive officer) and the Vice President and Chief Financial Officer (the principal financial officer) of Ohio Valley, Ohio Valley's management has evaluated the effectiveness of Ohio Valley's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the quarterly period covered by this Quarterly Report on Form 10-Q. Based on that evaluation, Ohio Valley's Chief Executive Officer and Vice President and Chief Financial Officer have concluded that Ohio Valley's disclosure controls and procedures are effective as of the end of the quarterly period covered by this Quarterly Report on Form 10-Q to ensure that information required to be disclosed by Ohio Valley in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by Ohio Valley in the reports that it files or submits under the Exchange Act is accumulated and communicated to Ohio Valley's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

##### Changes in Internal Control over Financial Reporting

There was no change in Ohio Valley's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during Ohio Valley's fiscal quarter ended March 31, 2016, that has materially affected, or is reasonably likely to materially affect, Ohio Valley's internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Not applicable.

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## ITEM 1A. RISK FACTORS

Completion of the merger contemplated by the agreement between Ohio Valley and Milton Bancorp is subject to many conditions, and if these conditions are not satisfied or waived, the merger will not be completed.

The obligations of Ohio Valley and Milton Bancorp to complete the merger contemplated by their Agreement and Plan of Merger dated January 7, 2016, as amended, are subject to the fulfillment or written waiver of many conditions, including approval by the banking regulators, the required vote of the Milton Bancorp shareholders, the absence of orders prohibiting completion of the merger, the continued accuracy of the representations and warranties of both parties, and the performance by both parties of their respective covenants and agreements. These conditions may not be fulfilled and, accordingly, the merger may not be completed. In addition, if the merger is not completed by August 6, 2016, either Ohio Valley or Milton Bancorp may have the opportunity to terminate the agreement, and Ohio Valley and Milton Bancorp can mutually agree to terminate the agreement at any time, before or after the approval by the Milton Bancorp shareholders.

In addition to the above risk factor, you should carefully consider the risk factors discussed in Part I, "Item 1A. Risk Factors" in Ohio Valley's Annual Report on Form 10-K for the year ended December 31, 2015, as filed with the Securities and Exchange Commission on March 15, 2016 and available at [www.sec.gov](http://www.sec.gov). These risk factors could materially affect the Company's business, financial condition or future results. The risk factors described in the Annual Report on Form 10-K are not the only risks facing the Company. Additional risks and uncertainties not currently known to the Company or that management currently deems to be immaterial also may materially adversely affect the Company's business, financial condition and/or operating results. Moreover, the Company undertakes no obligation and disclaims any intention to publish revised information or updates to forward looking statements contained in such risk factors or in any other statement made at any time by any director, officer, employee or other representative of the Company unless and until any such revisions or updates are expressly required to be disclosed by applicable securities laws or regulations.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

On February 24, 2016, Ohio Valley sold 24,572 of its common shares, without par value, to the Ohio Valley Banc Corp. Employee Stock Ownership Plan (the "ESOP") for an aggregate of \$575. No underwriters were involved, and no underwriting discount or commissions were paid. The sale was exempt from registration under Section 4(2) of the Securities Act of 1933 as a transaction by the issuer not involving any public offering, made only to the ESOP, with respect to which The Ohio Valley Bank Company serves as the Trustee.

Ohio Valley did not purchase any of its shares during the three months ended March 31, 2016.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

## ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

## ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS

(a) Exhibits:

Reference is made to the Exhibit Index set forth immediately following the signature page of this Form 10-Q.

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SIGNATURES

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

OHIO VALLEY BANC CORP.

Date: May 10, 2016

By: /s/Thomas E. Wiseman  
Thomas E. Wiseman  
President and Chief Executive Officer

Date: May 10, 2016

By: /s/Scott W. Shockey  
Scott W. Shockey  
Senior Vice President and Chief Financial  
Officer

EXHIBIT INDEX

The following exhibits are included in this Form 10-Q or are incorporated by reference as noted in the following table:

| Exhibit Number | Exhibit Description   |
|----------------|---|
| 2(a)           | Agreement and Plan of Merger between Ohio Valley Banc Corp. and Milton Bancorp, Inc., dated January 7, 2016: Incorporated herein by reference to Exhibit 2.1 to Ohio Valley's Current Report on Form 8-K filed on January 7, 2016 (SEC File No. 0-20914).   |
| 2(b)           | Amendment to Agreement and Plan of Merger by and between Ohio Valley Banc Corp. and Milton Bancorp, Inc., effective April 20, 2016: Incorporated herein by reference to Exhibit 2.1 to Ohio Valley's Current Report on Form 8-K filed on April 21, 2016 (SEC File No. 0-20914).   |
| 3(a)           | Amended Articles of Incorporation of Ohio Valley (reflects amendments through April 7, 1999) [for SEC reporting compliance only - - not filed with the Ohio Secretary of State]. Incorporated herein by reference to Exhibit 3(a) to Ohio Valley's Annual Report on Form 10-K for fiscal year ended December 31, 2007 (SEC File No. 0-20914). |
| 3(b)           | Code of Regulations of Ohio Valley (as amended by the shareholders on May 12, 2010): Incorporated herein by reference to Exhibit 3(b) to Ohio Valley's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2010 (SEC File No. 0-20914).   |
| 4              | Agreement to furnish instruments and agreements defining rights of holders of long-term debt: Filed herewith.   |
| 10.1*          | The Ohio Valley Bank Company Executive Deferred Compensation Agreement, dated January 26, 2016, between Larry E. Miller and The Ohio Valley Bank Company: Incorporated herein by reference to Exhibit 10.1 to Ohio Valley's Current Report on Form 8-K filed on January 26, 2016 (SEC File No. 0-20914).                                      |
| 10.2*          | The form of First Amendment to The Ohio Valley Bank Company Executive Deferred Compensation Agreement, dated January 26, 2016: Incorporated herein by reference to Exhibit 10.2 to Ohio Valley's Current Report on Form 8-K filed on January 26, 2016 (SEC File No. 0-20914).   |
| 10.3*          | Schedule A to Exhibit 10.2 identifying the named executive officers of OVBC who have executed with the Bank the First   |

Amendment to The Ohio Valley Bank Company Executive Deferred Compensation Agreement: Incorporated herein by reference to Exhibit 10.3 to Ohio Valley's Current Report on Form 8-K filed on January 26, 2016 (SEC File No. 0-20914).

10.4\*

The Ohio Valley Bank Company Salary Continuation Agreement, dated January 26, 2016, by and between Larry E. Miller and The Ohio Valley Bank Company: Incorporated herein by reference to Exhibit 10.4 to Ohio Valley's Current Report on Form 8-K filed on January 26, 2016 (SEC File No. 0-20914).

| Exhibit Number | Exhibit Description   |
|----------------|---|
| 31.1           | Rule 13a-14(a)/15d-14(a) Certification (Principal Executive Officer): Filed herewith.                       |
| 31.2           | Rule 13a-14(a)/15d-14(a) Certification (Principal Financial Officer): Filed herewith.                       |
| 32             | Section 1350 Certifications (Principal Executive Officer and Principal Accounting Officer): Filed herewith. |
| 101.INS #      | XBRL Instance Document: Filed herewith. #   |
| 101.SCH #      | XBRL Taxonomy Extension Schema: Filed herewith. #   |
| 101.CAL #      | XBRL Taxonomy Extension Calculation Linkbase: Filed herewith. #   |
| 101.DEF #      | XBRL Taxonomy Extension Definition Linkbase: Filed herewith. #  |
| 101.LAB #      | XBRL Taxonomy Extension Label Linkbase: Filed herewith. #   |
| 101.PRE #      | XBRL Taxonomy Extension Presentation Linkbase: Filed herewith. #  |

\* Compensatory plan or arrangement.

# Attached as Exhibit 101 are the following documents formatted in XBRL (eXtensive Business Reporting Language): (i) Unaudited Consolidated Balance Sheets; (ii) Unaudited Condensed Consolidated Statements of Income; (iii) Unaudited Consolidated Statements of Comprehensive Income; (iv) Unaudited Condensed Consolidated Statements of Changes in Stockholders' Equity; (v) Unaudited Condensed Consolidated Statements of Cash Flows; and (vi) Notes to the Consolidated Financial Statements.