

2011
ANNUAL
REPORT



MAKING A DIFFERENCE, ONE CUSTOMER AT A TIME



William P. Hayes,
Chairman, President, and
Chief Executive Officer

Several years ago, the theme for our annual report to shareholders was titled "The Test of Time." I couldn't help but be reminded of that theme recently when the Comptroller of the Currency presented Kish Bank with a large embossed certificate on the occasion of the 100th anniversary of the Bank's national charter. Kish's charter was originally granted to the Farmers National Bank of Belleville in 1912. Over the years, it is a charter that has stood the test of challenging economic periods and difficult regulatory conditions, perhaps never more so than the past few years. Today, we can say with pride that this milestone, like all those before it, was made possible by a sustained focus on the fundamentals of our business and a tradition of delivering on our promises to our customers and communities. So that now, as we review the results for Kish Bancorp in 2011, we can do so with a deep sense of pride in the tradition of performance that has brought Kish to this point in our history; a tradition of "Making a Difference, One Customer at a Time."

The economic recovery that many were predicting and hoping for failed to gain much traction; therefore, headwinds facing many of our small business borrowers continued. The challenging regulatory climate and heightened scrutiny of community banks, previously focused on other regions of the country, began to impact Pennsylvania's community banks as well. In February of 2011, Kish Bank voluntarily entered into an agreement with its primary regulator to address certain concerns arising from a 2009 examination regarding criticized loans and IT infrastructure. Despite this unexpected development, we maintained our focus on serving our customers and communities while moving swiftly to address these regulatory issues. Although the resources dedicated to addressing this situation were significant, Kish Bank remained profitable, well capitalized and growing. We continued to add new customers and new members to the team. We also remained supportive of our existing borrowers, most of whom had been customers for years and had never stopped performing or paying as agreed. Today we can point with pride to the metrics of loan quality and financial performance that were sustained at high levels throughout 2011. We can also report that the actions necessary to address the agreement are essentially completed, except for the period of time required to validate our capacity to sustain this performance.

A discussion of Kish Bancorp's performance in 2011 begins with an acknowledgement of the political, economic and regulatory climate that provided the backdrop for the year. A famous politician once said, "All politics is local." That statement is true for banking as well. Sooner or later, the forces at work on the national stage, from which we often feel removed, come home to impact us locally. That was the case for Kish in 2011. The Dodd-Frank Act, which had passed in 2010 with the stated intent of addressing the excesses that caused the financial crisis, had already rewritten the rules under which banks operate. Bank bashing remained in vogue in Washington, despite the fact that few banks, and certainly few community banks, had contributed to the crisis.

As you review our results for 2011, I would also ask you to bear in mind that the financial and internal resources committed to responding to the environment, while considerable, in reality represent the commitment of resources necessary to build the platform for the future. Our 2011 performance continued to advance Kish's strategic vision of "Building to a Billion"

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in assets. The balance sheet was strengthened. We invested in internal processes, systems, and infrastructure. Kish Bank expanded its market share in the region and our capacity to manage growth was fortified by a number of key additions to the Kish team. We are better positioned to pursue the growth opportunities that we are confident await us as the economic recovery begins to take hold. It is this solid foundation, built on the discipline of performance and team commitment, that permits us to proudly present this Annual Report.

Net income for 2011 grew to \$3.631 million, an increase of 2.1 percent over 2010. Earnings per share, at \$6.74, also exceeded 2010 performance. Return on average shareholder's equity remained strong at 9.82 percent, significantly exceeding the current industry average. It was this critical measure of shareholder performance that ranked Kish Bancorp among the top 200 Community Banks in the U.S. in 2011 for the third consecutive year, based on a ranking by *U.S. Banker* magazine.

The key driver of the growth in net income was a stable net interest margin coupled with growth in earning assets. Most importantly, the core banking business remained strong. Kish achieved a 1.5 percent increase in net interest income compared to 2010, despite weak market demand for commercial loans that contributed to a nominal decline of 1 percent in the loan portfolio. Net interest income during 2011 was

\$17.243 million, an increase of \$255 thousand compared to 2010.

Earnings were also aided during 2011 by strengthening loan quality metrics. There was a \$1.05 million decrease in the contribution to the reserve for loan losses, as \$800 thousand was set aside in 2011 compared to \$1.850 million in 2010. Because of a significant decline in actual losses, the reserve for loan losses, the Bank's buffer against possible future loan charge-offs, increased 12.8 percent to \$7.043 million at December 31, 2011 from \$6.245 million at December 31, 2010. While the Corporation's provision expenses declined, the reserve ratio increased substantially to 1.91 percent of total loans as of December 31, 2011 from 1.67 percent at December 31, 2010.

As noted above, loan quality indicators began the year on positive footing and grew stronger as 2011 progressed. The increased stability of our loan portfolio reflected continued efforts to work with our borrowers to resolve loan problems. Most notably, net loan losses were near zero during 2011, loan delinquencies were near historic lows, and criticized assets had begun to decrease substantially. When compared to our national peer group of banks between \$300 million and \$1 billion in assets at year end, Kish Bank's ratio of loan losses to total loans ranked in the top 3 percent of those banks; our earnings coverage of net losses ranked in the top 1 percent, and loans on non-accrual as a percentage of loans ranked in the top 60 percent. Over the past five years,

and in stark contrast to our national peer group, the sustained quality of these metrics have been important contributors to Kish Bancorp's overall performance. They also reflect our capacity to support local borrowers who have endured this very difficult economic period.

Noninterest income increased \$1.574 million, or 24.6 percent, to \$7.982 million for 2011 from \$6.408 million in 2010. This includes full-year business property income from a foreclosed business loan on the property, which was sold during the fourth quarter. Offsetting this \$1.9 million increase in noninterest revenues was a decline in investment securities gains, as well as lower gains on sales of residential mortgage loans originated for the secondary market.

Noninterest expense was \$20.355 million during 2011, an increase of \$2.835 million, or 16.2 percent, over the same period in 2010. This was driven in large part by the costs related to operating the business property discussed above. Excluding the impact of these expenses, core noninterest expenses grew by \$1.288 million, or 7.5 percent, in 2011 due to increases in FDIC insurance premiums, consulting fees, and salaries and benefits. Although a number of these expenses were nonrecurring, the rising cost of regulatory compliance in this environment must be a concern and underscores the need for prudent and profitable growth if we are to continue to achieve historical performance thresholds.

In addition to our sustained earnings performance, 2011 also witnessed the improvement of other key indicators of financial strength and durability. Capital ratios were continuously bolstered during the past year through retained earnings and a private offering of common stock of just over \$3 million. These activities served to augment Kish Bancorp's already strong capital base and equip the Corporation for the next period of expansion. Capital ratios at the holding company for December 31, 2011 versus the previous year were as follows: Tier 1 Leverage – 8.26 percent up from 7.24 percent; and Total Risk Based Capital – 13.85 percent up from 11.67 percent. We were pleased with the ready acceptance given to the private offering during what is still a difficult environment for banks in the capital markets. We were also gratified that the issuance had little impact on the market value of Kish Bancorp stock. As was true with previous forms of government provided capital (TARP), Kish did not raise capital through the U.S. Treasury's Small Business Lending Fund.

During 2011, the Bank implemented further enhancements to information security protocols, technology infrastructure, and information management systems that, along with other actions, have improved external and internal service capabilities across the organization. We will continue to place a high priority on investing in systems that protect information and deliver the most

efficient service possible to our customers.

To further strengthen our Build to a Billion initiatives and sharpen our focus on service to our customers, Kish also realigned the executive management team and made a number of strategic hires and appointments that are worthy of note in this report. In that process, we have strengthened our overall management focus, our sales focus and our sales teams.

In recognition of his leadership and strong performance since joining the Kish organization in 2009, Brad Scovill was promoted to the position of Senior Executive Vice President and Chief Operating Officer. In that capacity, he assumed full day-to-day operating responsibility for the Bank. He previously served in the dual role as Chief Operating Officer and CFO. Brad is also continuing his responsibilities as Chief Risk Officer for the Corporation.

There were also important additions to the Kish team this past year.

- John Arrington joined Kish early in 2011 as Regional Market Manager, Centre County, and was subsequently promoted to Executive Vice President for Sales and Retail Banking. John is passionate about community banking and customer service and, in addition to directing the sales efforts across all regions, is leading the Bank's efforts in product and service improvement.

- Carol Herrmann, a noted State College business leader, joined Kish as Vice President for Administration to provide executive-level direction, support and administrative oversight of such key functions as strategic planning, corporate communications, investor relations and marketing. She also facilitates the governance activities of the Bank and Corporation Boards of Directors and Regional Boards.

- Sangeeta Kishore, a seasoned bank financial executive, joined Kish Bank as Executive Vice President and Chief Financial Officer. She brought an extensive background and expertise in reporting requirements for banks above the \$1 billion asset threshold that will be invaluable as Kish continues to grow.

- Other key additions and appointments include Matt Raptosh, who joined the Bank as Assistant Vice President, Commercial Relationship Manager in Centre County, and John Keeler, as a Commercial Relationship Manager in Mifflin County. Several seasoned Kish bankers were promoted to new roles. In Mifflin County, John Cunningham was promoted to Regional Market Manager, Mifflin County and Allana Hartung was promoted to VP, Commercial Relationship Manager. Marsha Kuhns was appointed as VP of Branch Administration,

and Kayelene Sunderland was promoted to AVP and Trust Manager.

These enhancements to the team, among others, were part of an overall reorganization that aligned executive efforts in a number of key areas including sales, retail and business banking, finance, operations, and enterprise risk management.

An important component of Kish's Build to a Billion strategy is to develop the professional governance capabilities necessary to represent the interests of our shareholders, oversee and direct our activities, and set the strategic direction of the Company. Board members of Kish Bank and Kish Bancorp are charged with understanding the banking and diverse financial needs of our businesses and customers and possessing the technical and financial acumen important to the governance of the Bank and its various business units. They are also accountable for Kish's adherence to the regulatory structure under which we operate. Together, our Board members further strengthen the capacity of the Corporation to achieve its long-term goals and objectives. We are grateful for their extraordinary commitment to Kish and our mission of driving sustained shareholder value through an unwavering focus on service to our customers and communities.

In that regard, we were pleased to welcome Mr. Delmont R. Sunderland of Huntingdon to the Kish Bancorp Board in 2011. Recently, we were also pleased to announce the

appointment of William S. Lake to the Kish Bank and Kish Bancorp Boards of Directors. Mr. Lake is a long-time resident of Mifflin County and is the owner of the Lake Automobile Dealerships in Lewistown. He is respected for his community support and business acumen and brings an in-depth knowledge of the markets in which we operate. He will stand for election by the shareholders at the upcoming annual meeting in May.

We also want to acknowledge with gratitude the departure of a valued member of our Boards following the upcoming shareholders meeting in May. Alison B. Kurtz of State College has decided to conclude her service as a director of Kish Bank and Kish Bancorp at the end of her term. The demands imposed on our directors have increased dramatically in recent years and we are grateful to Alison for her contributions, commitment, and dedication during a challenging and demanding time.

In summary, Kish's sustained positive financial performance, strengthened balance sheet, loan quality, realignment of the management structure, additions to our governance teams, and focus on building a winning team, in combination with strategic investments in our technology infrastructure, focus on risk management, improvement in our internal processes, and refinements to our product development and support processes, reinforce Kish's ability to continue to advance the Corporation's long-term goals in the years ahead.

In reviewing the Corporation's achievements for 2011, we gratefully acknowledge the continued support and encouragement of you, our shareholders. You have supported Kish's special mission in the marketplace and its ambitious goals for the future. The Corporation has been fortunate to welcome a strong and local group of new investors this year. We extend to you a warm welcome to the Kish organization, one uniquely committed to making a difference in our community— one customer at a time.

As always, we encourage your inquiries regarding the Corporation's performance noted herein and throughout the coming year.

Sincerely,

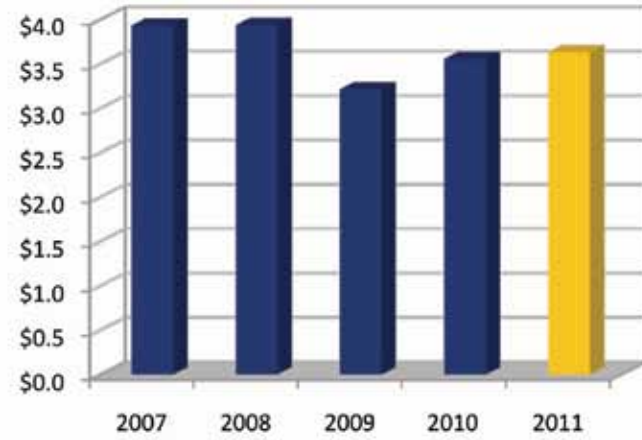


William P. Hayes
Chairman, President, and
Chief Executive Officer

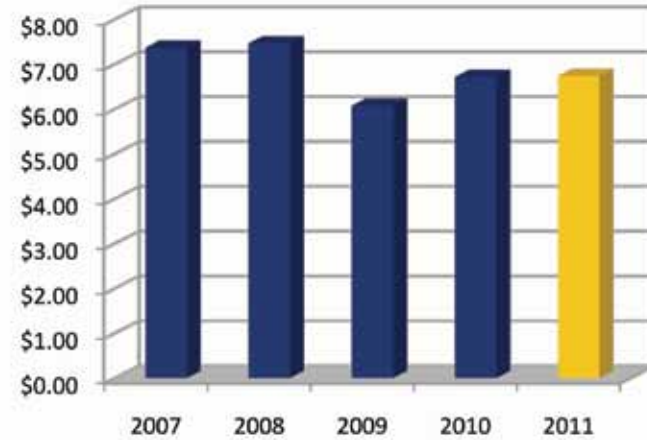
Five Year Summary

FOR THE YEAR	2011	2010	2009	2008	2007
Net Income	\$3,631,298	\$3,556,124	\$3,216,423	\$3,937,791	\$3,933,582
Net Income Before Taxes	4,070,114	4,026,669	3,586,370	4,817,481	4,826,174
Total Dividends Declared	1,760,493	1,739,714	1,721,575	1,713,474	1,629,120
AT YEAR END (IN 000's)					
Total Assets	\$560,069	\$556,623	\$527,396	\$476,263	\$454,092
Total Loans (Net)	362,163	367,306	367,824	333,434	305,729
Total Deposits	454,660	446,002	407,721	352,729	331,688
Stockholders' Equity	43,517	35,729	34,062	31,302	30,323
Loan Loss Reserve	7,043	6,245	5,397	3,305	3,001
Net Loan Losses (Recoveries)	3	1,001	252	(5)	140
RATIO ANALYSIS					
Return on Average Assets	0.65%	0.65%	0.64%	0.84%	0.92%
Return on Average Equity	9.82%	10.31%	9.73%	12.75%	13.32%
Dividend Declared/Net Income	48.48%	48.92%	53.57%	43.51%	41.42%
Loan/Deposits	79.66%	82.36%	90.21%	94.53%	92.17%
Primary Capital/Total Assets	9.03%	7.54%	7.48%	7.27%	7.34%
Total Capital/Risk Weighted Assets	13.85%	11.67%	11.26%	10.40%	10.41%
Loan Loss Reserve/Loans	1.91%	1.67%	1.44%	0.98%	0.97%
Net Loan Losses to Total Loans (Net)	0.00%	0.27%	0.07%	0.00%	0.05%
PER SHARE DATA					
Basic Earnings	\$6.74	\$6.72	\$6.08	\$7.47	\$7.37
Fully Diluted Earnings	6.72	6.68	6.07	7.47	7.35
Dividends Paid	3.24	3.24	3.24	3.24	3.03
Equity (Book Value)	72.95	66.54	63.61	59.04	57.50
Equity Plus Loan Loss Reserve	84.75	78.17	73.69	65.27	63.19
Average Shares Outstanding (#)	538,735	529,343	528,125	527,044	534,916

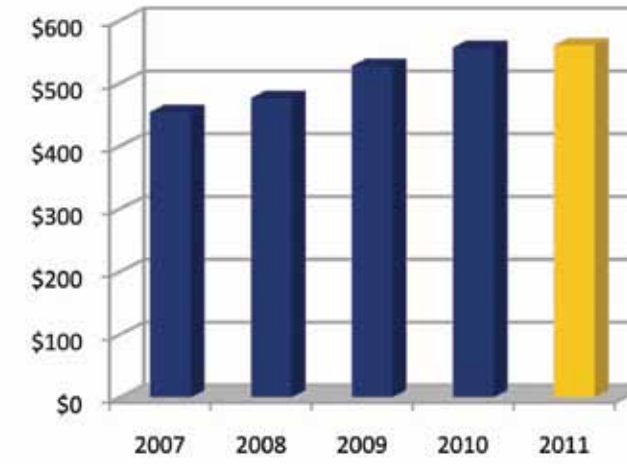
Net Income (in millions)



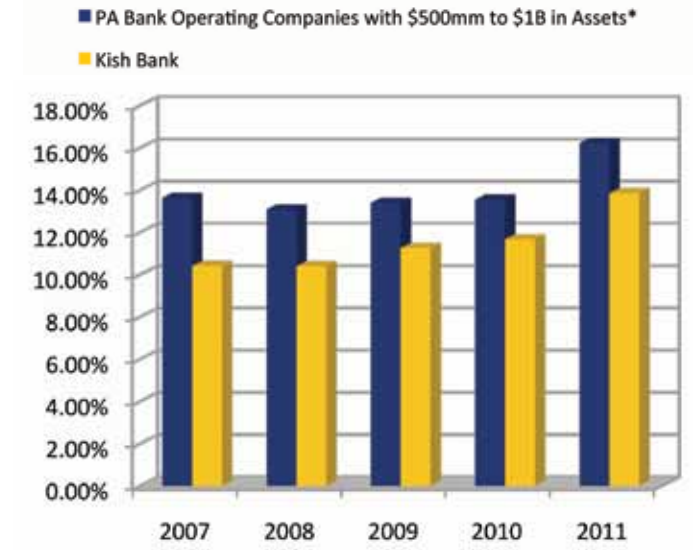
Basic Earnings Per Share



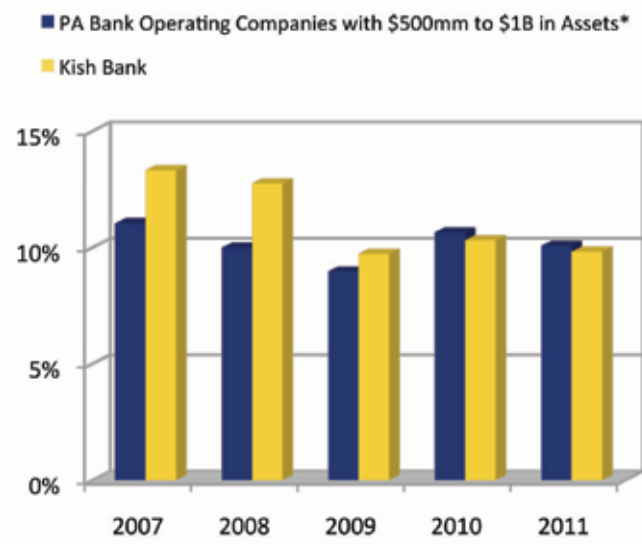
Total Assets (in millions)



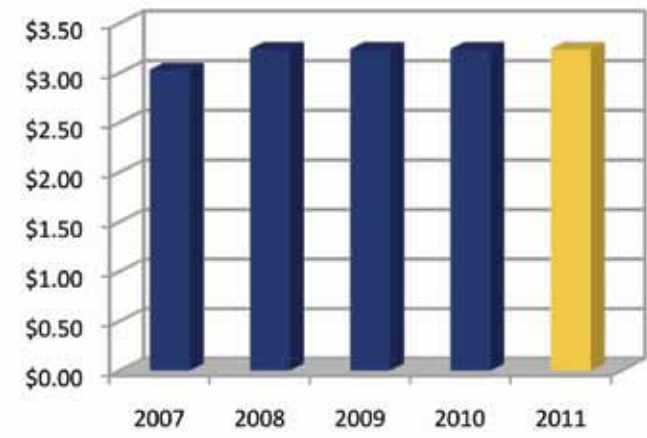
Total Capital/
Risk Weighted Assets



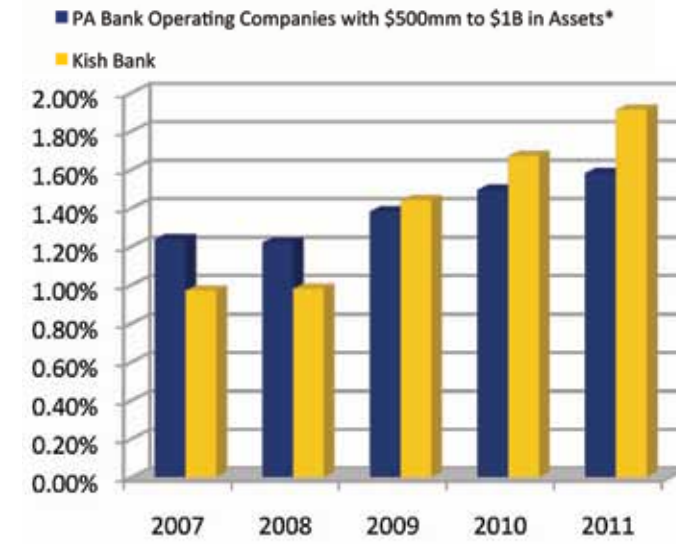
Return on Average Equity



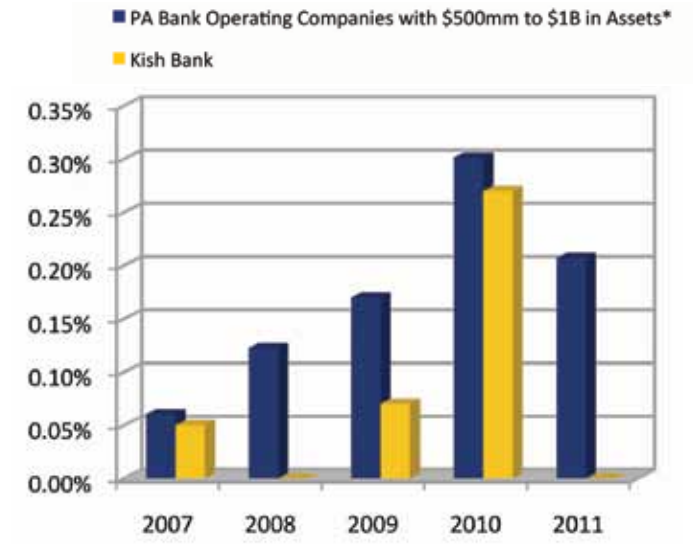
Dividends Per Share



Loan Loss Reserve/Loans



Net Loan Losses to
Total Loans (Net)



* Source – SNL Financial, median values

* Source – SNL Financial, median values

Making a Difference – One Customer at a Time



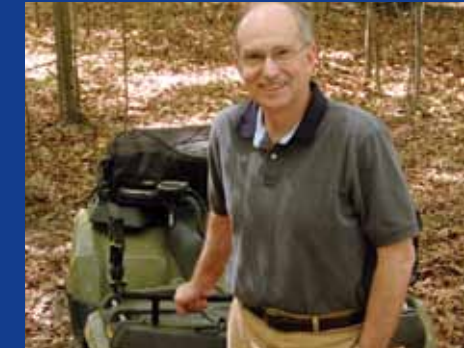
Ed Bridgens
Owner, Eastgate Feed & Grain
Kish Banking, Insurance, and Travel Customer



Suzy Glenn
Owner, Best Event Rental
Kish Bank Customer



Mark Mazur and Christina Calkins-Mazur
Owners, Calkins Automotive
Kish Bank Customers



Art DeCamp
Kish Insurance Customer



Paula Seguin
Owner, Boxer's Café
Kish Bank Customer

At Kish Bancorp, we never get confused about our reason for being in business. We're here to serve our customers by meeting their needs and helping them accomplish their goals, realize their dreams, and build brighter futures. To the extent we are successful in achieving that objective, then we can also focus on our goal of delivering long term performance and value to our shareholders and our communities.

Of course, the critical element of delivering value is strong financial performance. But it extends beyond that. By producing consistently strong financial performance, we not only achieve results for shareholders, we are also able to invest in our franchise, our employees and the organizations that serve our communities. As we reinvest in the infrastructure of the company, we strengthen our capacity to perform and compete. The same is true for our workforce. Investing in our people is the only means to elevate the professional capacity of our people and deliver great service. Solid profitability also enhances our ability to provide financial support to the organizations that help the most vulnerable and needy in our communities.

Most importantly of course, by touching so many aspects of our customers' lives with an expanding range of products and services, we make a difference in our community by helping to fuel business innovation and expansion, capital formation, and wealth generation.

All of this makes an investment in Kish a winning proposition on multiple levels. It's an investment not only in an organization committed to achieving outstanding financial results, but also dedicated to having a positive impact on the quality of life in our community. An investment in Kish is an investment that makes a difference.

So, one of the best ways to see how Kish makes a difference is to look first-hand at the experiences of our customers. Behind every Kish customer relationship is an individual story. As a community-based institution built on personal relationships, Kish has a unique opportunity to see our customers' stories unfold on a direct and personal level. The stories you will see in these pages provide just a few of many examples of how **Kish makes a difference—one customer at a time.**

With the long retail hours and financial complexities, running a successful car dealership doesn't allow for much down time. So it's important for Mark Mazur and Christina Calkins-Mazur to be able to ensure the achievement of their personal financial goals without a lot of hands-on administrative involvement. That's why they choose Kish Bank for their personal banking needs as well as their business banking. The peace of mind that comes with knowing that Kish is navigating their personal financial ship in the right direction makes a difference in their lives; plus it gives them more opportunities to enjoy life with their growing young family, including leisure time at the shore.

Art DeCamp has a variety of specialized relationships with the financial services team at Kish. From banking, to investment management to insurance, his experience is that Kish delivers customized and highly personalized solutions. He likes to discuss his insurance needs—some of which he wasn't even fully aware of before he met his Kish Insurance agent—as an example of how Kish differentiates itself. Previously, he had repeatedly experienced the frustration of working with insurance agents who

seemed a lot more interested in passing his questions along to assistants, instead of working with him directly. That's why Art has found that his experience with Kish Insurance makes such a difference. It has been like a breath of fresh air to have an insurance partner who takes the time to truly understand his needs and personally attend to the smallest details.

Ed Bridgens has experienced all facets of financial services delivery through his relationship with Kish: his business banking needs as a small business owner, personal banking, as well as his personal and business insurance and investment management needs have all been provided at levels that have helped him meet his financial goals; all while maintaining a quality of life in the local community that makes his hard work worthwhile. So when it comes to leisure time, Ed turns to a trusted source for managing his vacation trips as well. There are many options, online and offline, for planning a vacation. Finding competitive prices on fares and lodging can be time consuming and often challenging. It's even more daunting to try to make sure you don't run into the unexpected hassles and unpleasant surprises that can make a pleasure trip



“Kish caters to me.”

– John Pannizzo

Owner, Downtown OIP and Grille
Kish Financial Solutions Customer

much less pleasurable. If you lead the busy lifestyle of a business owner like Ed Bridgens, finding the time it takes to plan a vacation on your own can be difficult. That’s why Ed trusts the experts at Kish Travel, who make a difference in his leisure life by devoting the time and personal attention it takes to take care of the details and ensure that every trip, from a weekend getaway to a long, leisurely vacation package, is an exceptional and memorable experience.

The restaurant business is fast-paced—that’s a given. But that doesn’t bother John Pannizzo, who you’re likely to see out for a run if he’s not at his restaurant multi-tasking to make sure everything, from the kitchen to the dining room to the restrooms, is running in a way that ensures his customers an experience that meets his high standards. John also has high standards when it comes to choosing a financial services partner. With a life outside of work that’s often just as fast-paced as his business, he doesn’t want to spend a lot of time managing the details of keeping his long-term financial goals on track. So it makes a big difference for John that he can trust Kish Financial Solutions to manage the details of retirement, children’s college funding, and

more—giving him more time to lace up the sneakers and make tracks.

We think these customer stories speak volumes. Since our management team and associates share our communities with our customers and shareholders, we can see the positive difference that our performance, products and services make in our neighbors’ lives: from helping their personal and business finances thrive... to helping them provide for their children’s education and attaining financial security for retirement; from providing peace of mind with insurance products to protecting what matters most to them... to enhancing their ability to enjoy downtime with unique travel and leisure experiences.

The Kish Experience is a story about our customers’ success. It is a sum of the stories of all of our customers. It is what makes our alignment with our customers so strong and our shareholders’ investment so important to the health and well-being of our communities.

**Kish Bancorp, Inc.
Consolidated Audited Financial Statements
December 31, 2011**

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Market and Dividend Information for 2011

During 2011, Kish Bancorp, Inc. paid four quarterly dividends totaling \$3.24. \$0.81 per share was paid on January 31, April 30, July 31 and October 31. These dividends were paid to shareholders of record as of January 1, April 1, July 1 and October 1.

Stock in Kish Bancorp, Inc. is not actively traded on a national securities exchange. During 2011, trades occurred in the over the counter (OTC) market. To management’s knowledge, sale prices ranged from \$63.00 to \$56.00 per share. At year-end, an average bid price of \$58.00 was posted.

On December 31, 2011, there were 438 shareholders of record. The following firms are market makers in the Corporation’s stock:

Boenning & Scattergood, Inc.
4 Tower Bridge, 200 Barr Harbor Drive, Suite 300
West Conshohocken, PA 19428
(610) 862-5368

Raymond James and Associates, Inc.
222 South Riverside Plaza, 7th Floor
Chicago, IL 60606
(312) 655-2975

Registrar and Transfer Company serves as the Corporation’s transfer agent and record keeper. Founded in 1899, Registrar and Transfer Company is the nation’s oldest, most widely respected specialist in the stock transfer business. Thousands of banks and public companies, trading on all U.S. exchanges, utilize R&T to provide efficient and comprehensive shareholder services.

Their contact information is as follows:

Registrar and Transfer Company
10 Commerce Drive
Cranford, NJ 07016
(800) 368-5948
info@rtco.com

**Report of Independent Auditors
Board of Directors and Stockholders,
Kish Bancorp, Inc.**

We have audited the accompanying consolidated balance sheet of Kish Bancorp, Inc. and subsidiaries as of December 31, 2011 and 2010, and the related consolidated statements of income, changes in stockholders’ equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Kish Bancorp, Inc. and subsidiaries as of December 31, 2011 and 2010, and the results of their operations and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

J. A. Amodeo, A.C.

Wexford, Pennsylvania
March 14, 2012

Consolidated Balance Sheet

	December 31,	
	2011	2010
ASSETS		
Cash and due from banks	\$ 9,592,946	\$ 9,338,767
Interest-bearing deposits with other institutions	31,588,825	10,544,564
Cash and cash equivalents	41,181,771	19,883,331
Certificates of deposit in other financial institutions	1,619,833	2,734,094
Investment securities available for sale	114,170,492	120,862,285
Loans held for sale	1,401,376	918,342
Loans	369,205,842	373,551,450
Less allowance for loan losses	7,042,911	6,245,441
Net loans	362,162,931	367,306,009
Premises and equipment	14,211,627	13,633,292
Goodwill	1,668,699	1,668,699
Regulatory stock	4,042,400	4,161,800
Bank-owned life insurance	12,097,673	11,684,697
Accrued interest and other assets	7,512,072	13,770,102
TOTAL ASSETS	\$ 560,068,874	\$ 556,622,651
LIABILITIES		
Deposits:		
Noninterest-bearing	\$ 54,985,004	\$ 45,225,548
Interest-bearing demand	8,021,861	8,233,339
Savings	40,358,678	36,303,525
Money market	177,667,176	177,084,834
Time	173,627,594	179,154,740
Total deposits	454,660,313	446,001,986
Short-term borrowings	5,696,162	7,608,645
Other borrowings	52,049,918	62,871,140
Accrued interest and other liabilities	4,145,495	4,411,628
TOTAL LIABILITIES	516,551,888	520,893,399
STOCKHOLDERS' EQUITY		
Preferred stock, \$.50 par value; 500,000 shares authorized, no shares issued and outstanding	-	-
Common stock, \$.50 par value; 2,000,000 shares authorized, 663,791 and 610,000 shares issued	331,896	305,000
Additional paid-in capital	2,979,269	114,999
Retained earnings	43,654,117	41,783,312
Accumulated other comprehensive income	2,466,659	24,409
Treasury stock, at cost (67,237 and 73,046 shares)	(5,914,955)	(6,498,468)
TOTAL STOCKHOLDERS' EQUITY	43,516,986	35,729,252
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 560,068,874	\$ 556,622,651

See accompanying notes to consolidated financial statements.

Consolidated Statement of Income

	Year Ended December 31,	
	2011	2010
INTEREST AND DIVIDEND INCOME		
Interest and fees on loans:		
Taxable	\$ 19,773,794	\$ 20,716,935
Exempt from federal income tax	1,030,427	1,087,627
Interest and dividends on investment securities:		
Taxable	1,832,161	1,891,681
Exempt from federal income tax	1,336,001	1,322,196
Interest-bearing deposits with other institutions	83,224	108,819
Other dividend income	63,870	88,104
Total interest and dividend income	24,119,477	25,215,362
INTEREST EXPENSE		
Deposits	4,266,998	4,861,254
Short-term borrowings	203,640	121,890
Other borrowings	2,406,192	3,244,235
Total interest expense	6,876,830	8,227,379
NET INTEREST INCOME	17,242,647	16,987,983
Provision for loan losses	800,000	1,850,000
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	16,442,647	15,137,983
NONINTEREST INCOME		
Service fees on deposit accounts	1,483,286	1,423,464
Investment securities gains, net	840,576	1,050,999
Investment securities impairment loss	(8,728)	(28,167)
Gain on sale of loans, net	797,914	1,045,435
Earnings on bank-owned life insurance	416,069	399,688
Insurance commissions	886,733	852,732
Travel agency commissions	236,580	230,688
Business property income	2,059,377	168,008
Other	1,270,226	1,265,390
Total noninterest income	7,982,033	6,408,237
NONINTEREST EXPENSE		
Salaries and employee benefits	9,969,960	8,751,543
Occupancy and equipment	2,847,007	2,207,718
Data processing	1,574,312	1,537,774
Professional fees	356,458	254,195
Advertising	436,651	377,299
Federal deposit insurance	1,074,877	646,016
Prepayment penalty on extinguishment of debt	-	548,896
Loss on sale of other assets	353,018	-
Other	3,742,283	3,196,110
Total noninterest expense	20,354,566	17,519,551
Income before income taxes	4,070,114	4,026,669
Income taxes	438,816	470,545
NET INCOME	\$ 3,631,298	\$ 3,556,124
EARNINGS PER SHARE		
Basic	\$ 6.74	\$ 6.72
Diluted	6.72	6.68

See accompanying notes to the consolidated financial statements.

Consolidated Statement of Changes In Stockholders' Equity

	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity	Comprehensive Income (Loss)
Balance, December 31, 2009	\$ 305,000	\$ 273,712	\$ 39,966,902	\$ 246,582	\$ (6,730,489)	\$ 34,061,707	
Net income			3,556,124			3,556,124	3,556,124
Other comprehensive loss:							
Unrealized loss on available-for-sale securities, net of reclassification adjustment, net of tax benefit of \$114,453				(222,173)		(222,173)	(222,173)
Comprehensive income							3,333,951
Stock option compensation expense		29,676				29,676	
Purchase of shares by RSP		(320,120)			320,120	-	
Forfeiture of shares by RSP		17,328			(17,328)	-	
Amortization of unearned RSP shares		154,896				154,896	
Cash dividends (\$3.24 per share)			(1,739,714)		(197,150)	(1,739,714)	
Purchase of treasury stock (2,973 shares)					126,379	85,886	
Sale of treasury stock (1,341 shares)							
Balance, December 31, 2010	305,000	114,999	41,783,312	24,409	(6,498,468)	35,729,252	
Net income			3,631,298			3,631,298	3,631,298
Other comprehensive income:							
Unrealized gain on available-for-sale securities, net of reclassification adjustment, net of taxes of \$1,270,706				2,442,250		2,442,250	2,442,250
Comprehensive income							6,073,548
Stock option compensation expense		42,100				42,100	
Purchase of shares by RSP		(498,911)			498,911	-	
Forfeiture of shares by RSP		27,405			(27,405)	-	
Amortization of unearned RSP shares		193,319				193,319	
Cash dividends (\$3.24 per share)			(1,760,493)			(1,760,493)	
Sale of new issue common stock (53,791 shares)		3,150,001				3,150,001	
Purchase of treasury stock (383 shares)	26,896				(23,227)	(23,227)	
Sale of treasury stock (1,411 shares)		(49,644)			135,234	85,590	
Balance, December 31, 2011	\$ 331,896	\$ 2,979,269	\$ 43,654,117	\$ 2,466,659	\$ (5,914,955)	\$ 43,516,986	
			2011			2010	
Components of other comprehensive income (loss):							
Change in net unrealized gain on investments available for sale							
Realized gains included in net income, net of tax of \$285,796 and \$357,340			\$ 2,991,270			\$ 452,896	
Impairment losses included in net income, net of tax benefit of \$2,968 and \$9,577			(554,780)			(693,659)	
Total			5,760			18,590	
			\$ 2,442,250			\$ (222,173)	

See accompanying notes to consolidated financial statements.

Consolidated Statement of Cash Flows

	Year Ended December 31,	
	2011	2010
OPERATING ACTIVITIES		
Net income	\$ 3,631,298	\$ 3,556,124
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	800,000	1,850,000
Investment securities gains, net	(840,576)	(1,050,999)
Investment securities impairment loss	8,728	28,167
Proceeds from sale of loans held for sale	24,715,642	36,312,273
Origination of loans held for sale	(24,400,762)	(35,611,190)
Gain on sales of loans, net	(797,914)	(1,045,435)
Depreciation, amortization and accretion	1,557,325	2,696,173
Deferred income taxes	(104,051)	(428,312)
Increase (decrease) in accrued interest receivable	167,919	(163,160)
Decrease in accrued interest payable	(101,444)	(118,311)
Earnings on bank-owned life insurance	(416,069)	(399,688)
Decrease in prepaid federal deposit insurance	1,035,498	597,013
Loss on sale of other assets	353,018	-
Other, net	143,275	(180,986)
Net cash provided by operating activities	<u>5,751,887</u>	<u>6,041,669</u>
INVESTING ACTIVITIES		
Maturities of certificates of deposit	1,114,261	2,642,275
Purchase of certificates of deposit	-	(1,818,165)
Investment securities available for sale:		
Proceeds from sale of investments	53,533,950	45,120,669
Proceeds from repayments and maturities	21,467,880	16,851,299
Purchases	(64,388,175)	(105,916,061)
Decrease (increase) in loans, net	7,038,702	(5,070,085)
Purchase of regulatory stock	(213,000)	(17,500)
Redemption of regulatory stock	332,400	-
Purchase of premises and equipment	(1,516,320)	(1,144,384)
Proceeds from sale of premises and equipment	-	67,966
Purchase of bank-owned life insurance ("BOLI")	(16,000)	-
Proceeds from sale of other real estate owned	43,127	570,135
Proceeds from sale of other assets	746,339	-
Net cash provided by (used for) investing activities	<u>18,143,164</u>	<u>(48,713,851)</u>
FINANCING ACTIVITIES		
Increase in deposits, net	8,658,327	38,280,949
Increase (decrease) in short-term borrowings, net	(1,912,483)	2,980,743
Proceeds from other borrowings	2,712,000	10,050,000
Repayments of other borrowings	(13,533,222)	(24,102,662)
Proceeds from sale of common stock	3,176,897	-
Purchases of treasury stock	(23,227)	(197,150)
Proceeds from sale of treasury stock	85,590	85,886
Cash dividends	(1,760,493)	(1,739,714)
Net cash provided by (used for) financing activities	<u>(2,596,611)</u>	<u>25,358,052</u>
Increase (decrease) in cash and cash equivalents	21,298,440	(17,314,130)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>19,883,331</u>	<u>37,197,461</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 41,181,771</u>	<u>\$ 19,883,331</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid during the year for:		
Interest on deposits and borrowings	\$ 6,978,272	\$ 8,345,690
Income taxes	482,000	1,050,000
SUPPLEMENTAL DISCLOSURE OF NON-CASH CASH FLOW INFORMATION		
Real estate acquired in settlement of loans	\$ 54,841	\$ 3,737,599

See accompanying notes to consolidated financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting and reporting policies applied in the presentation of the accompanying consolidated financial statements follows:

Nature of Operations and Basis of Presentation

Kish Bancorp, Inc. (the "Company") is a diversified financial services organization whose principal activity is the ownership and management of its subsidiaries, Kishacoquillas Valley National Bank (the "Bank"), Kish Travel Services, Inc., and the Bank's subsidiaries, Kish Agency, Inc. and Tri Valley Properties, LLC. The Company generates commercial and agricultural, commercial mortgage, residential real estate, and consumer loans and deposit services to its customers located primarily in central Pennsylvania and the surrounding areas. The Bank operates under a national bank charter and provides full banking services. Deposits are insured by the Federal Deposit Insurance Corporation ("FDIC") to the extent provided by law. Kish Agency, Inc. provides insurance products and services. Kish Travel Services, Inc. is a Pennsylvania business established to provide travel services to its customers. Tri Valley properties, LLC is a limited liability company established to hold and manage real estate and other property acquired through debts previously contracted.

The consolidated financial statements include the accounts of Kish Bancorp, Inc., and its subsidiaries, Kishacoquillas Valley National Bank and Kish Travel Services, Inc., after elimination of all intercompany transactions.

The accounting principles followed by the Company and the methods of applying these principles conform to U.S. generally accepted accounting principles ("GAAP") and to general practice within the banking industry. Management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the Consolidated Balance Sheet date and revenues and expenses for that period. Actual results could differ from those estimates.

Investment Securities

Investment securities are classified at the time of purchase, based on management's intention and ability, as securities held to maturity, available for sale, or trading. Debt securities acquired with the intent and ability to hold to maturity are stated at cost, adjusted for amortization of premium and accretion of discount, which are computed using the interest method and recognized as adjustments of interest income. Debt securities which are held principally as a source of liquidity are classified as available for sale. Unrealized holding gains and losses for available-for-sale securities are reported as a separate component of stockholders' equity, net of tax, until realized. Realized security gains and losses are computed using the specific identification method for debt securities and the average cost method for marketable equity securities. Debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and reported at fair value, with unrealized gains and losses included in current earnings. Realized securities gains and losses are computed using the specific identification method. The Company does not have trading securities or securities held to maturity as of December 31, 2011 and 2010. Interest and dividends on investment securities are recognized as income when earned.

Securities are evaluated on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation to determine whether a decline in their value is other than temporary. For debt securities, management considers whether the present value of cash flows expected to be collected are less than the security's amortized cost basis (the difference defined as the credit loss), the magnitude and duration of the decline, the reasons underlying the decline and the Company's intent to sell the security or whether it is more likely than not that the Company would be required to sell the security before its anticipated recovery in market value, to determine whether the loss in value is other than temporary. Once a decline in value is determined to be other than temporary, if the investor does not intend to sell the security, and it is more likely than not that it will not be required to sell the security before recovery of the security's amortized cost basis, the charge to earnings is limited to the amount of credit loss. Any remaining difference between fair value and amortized cost (the difference

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**Investment Securities (Continued)**

defined as the non-credit portion) is recognized in other comprehensive income, net of applicable taxes. Otherwise, the entire difference between fair value and amortized cost is charged to earnings.

Common stock of the Federal Home Loan Bank ("FHLB") of Pittsburgh and Federal Reserve Bank represents ownership in institutions that are wholly owned by other financial institutions. These equity securities are accounted for at cost and are shown separately on the Consolidated Balance Sheet.

The Bank is a member of the FHLB and, as such, is required to maintain a minimum investment in stock of the FHLB that varies with the level of advances outstanding with the FHLB. The stock is bought from and sold to the FHLB based upon its \$100 par value. The stock does not have a readily determinable fair value and, as such, is classified as restricted stock, carried at cost and evaluated by management. The stock's value is determined by the ultimate recoverability of the par value rather than by recognizing temporary declines. The determination of whether the par value will ultimately be recovered is influenced by criteria such as the following: (a) the significance of the decline in net assets of the FHLB as compared with the capital stock amount and the length of time this situation has persisted; (b) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance; (c) the impact of legislative and regulatory changes on the customer base of the FHLB; and (d) the liquidity position of the FHLB.

The FHLB had incurred losses in 2009 and for parts of 2010 due primarily to other-than-temporary impairment credit losses on its private-label mortgage-backed securities portfolio. These securities were the most effected by the extreme economic conditions in place during the previous several years. As a result, the FHLB had suspended the payment of dividends and limited the amount of excess capital stock repurchases. The FHLB has reported net income for both the fourth quarter and the year ended December 31, 2011, and has declared a .10 percent annualized dividend to its shareholders effective February 23, 2012. While the FHLB has not committed to regular dividend payments or future limited repurchases of excess capital stock, it will continue to monitor the overall financial performance of the FHLB in order to determine the status of limited repurchases of excess capital stock or dividends in the future. Management evaluated the stock and concluded that the stock was not impaired for the periods presented herein. More consideration was given to the long-term prospects for the FHLB as opposed to the recent stress caused by the extreme economic conditions the world is facing. Management also considered that the FHLB maintains regulatory capital ratios in excess of all regulatory capital requirements, liquidity appears adequate, new shares of FHLB stock continue to change hands at the \$100 par value, and the resumption of dividends.

Loans

Loans are reported at their principal amount net of the allowance for loan losses and deferred origination fees or costs. Interest on loans is recognized as income when earned on the accrual method. Generally, the policy has been to stop accruing interest on loans when it is determined that a reasonable doubt exists as to the collectibility of additional interest. Interest previously accrued but deemed uncollectible is deducted from current interest income. Payments received on nonaccrual loans are recorded as income or applied against principal according to management's judgment as to the collectibility of such principal. Nonaccrual loans will generally be put back on accrual status after demonstrating six consecutive months of nondelinquency.

The allowance for loan losses is established through provisions for loan losses charged against income. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance.

Loan origination fees and certain direct loan origination costs are being deferred and the net amount amortized is accounted for as an adjustment of the related loan's yield. Management is amortizing these amounts over the contractual life of the related loans.

In general, fixed rate, permanent residential mortgage loans originated by the Bank are held for sale and are carried in the aggregate at the lower of cost or market. The Bank sells these loans to various other financial institutions. Currently, the Bank retains the servicing of those loans sold to the FHLB and releases the servicing of loans sold to all other institutions.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**Allowance for Loan Losses**

The allowance for loan losses represents the amount that management estimates is adequate to provide for probable losses inherent in its loan portfolio as of the Consolidated Balance Sheet date. The allowance method is used in providing for loan losses. Accordingly, all loan losses are charged to the allowance, and all recoveries are credited to it. The allowance for loan losses is established through a provision for loan losses charged to operations. The provision for loan losses is based on management's periodic evaluation of individual loans, economic factors, past loan loss experience, changes in the composition and volume of the portfolio, and other relevant factors. The estimates used in determining the adequacy of the allowance for loan losses, including the amounts and timing of future cash flows expected on impaired loans, are particularly susceptible to change in the near term.

Impaired loans are commercial and industrial, agricultural, state and political subdivisions, and commercial real estate loans for which it is probable the Company will not be able to collect all amounts due according to the contractual terms of the loan agreement. The Company individually evaluates such loans for impairment and does not aggregate loans by major risk classifications. The definition of "impaired loans" is not the same as the definition of "nonaccrual loans," although the two categories overlap. The Company may choose to place a loan on nonaccrual status due to payment delinquency or uncertain collectibility while not classifying the loan as impaired, provided the loan is not a commercial or commercial real estate classification. Factors considered by management in determining impairment include payment status and collateral value. The amount of impairment for these types of loans is determined by the difference between the present value of the expected cash flows related to the loan using the original interest rate and its recorded value, or as a practical expedient in the case of collateralized loans, the difference between the fair value of the collateral and the recorded amount of the loans. When foreclosure is probable, impairment is measured based on the fair value of the collateral.

Mortgage loans secured by one-to-four family properties and all consumer loans are large groups of smaller-balance homogenous loans and are measured for impairment collectively. Loans that experience insignificant payment delays, which are defined as 90 days or less, generally are not classified as impaired. Management determines the significance of payment delays on a case-by-case basis taking into consideration all circumstances concerning the loan, the creditworthiness and payment history of the borrower, the length of the payment delay, and the amount of shortfall in relation to the principal and interest owed.

In addition to the allowance for loan losses, the Company also estimates probable losses related to unfunded lending commitments, such as letters of credit, financial guarantees and unfunded loan commitments. Unfunded lending commitments are subject to individual reviews and are analyzed and segregated by risk according to the Company's internal risk rating scale. These risk classifications, in conjunction with an analysis of historical loss experience, current economic conditions, performance trends within specific portfolio segments and any other pertinent information, result in the estimation of the reserve for unfunded lending commitments. Provision for credit losses related to the loan portfolio and unfunded lending commitments are reported in the Consolidated Statement of Income.

Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost, less accumulated depreciation. Depreciation is principally computed on the straight-line method over the estimated useful lives of the related assets, which range from 3 to 7 years for furniture, fixtures, and equipment, and 31 to 39½ years for building premises and leasehold improvements. Expenditures for maintenance and repairs are charged against income as incurred. Costs of major additions and improvements are capitalized.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**Goodwill**

The Company accounts for goodwill using a two-step process for testing the impairment of goodwill on at least an annual basis. This approach could cause more volatility in the Company's reported net income because impairment losses, if any, could occur irregularly and in varying amounts.

Bank-Owned Life Insurance ("BOLI")

The Company purchased life insurance policies on certain key employees. BOLI is recorded at its cash surrender value, or the amount that can be realized.

Real Estate Owned

Real estate acquired by foreclosure is included with other assets on the Consolidated Balance Sheet at the lower of the recorded investment in the property or its fair value less estimated costs of sale. Prior to foreclosure, the value of the underlying collateral is written down by a charge to the allowance for loan losses if necessary. Any subsequent write-downs are charged against operating expenses. Operating expenses of such properties, net of related income and losses on their disposition, are included in other expense.

Treasury Stock

Treasury stock is carried at cost. Sales are determined by the first-in, first-out method.

Advertising Costs

Advertising costs are expensed as the costs are incurred. Advertising expense amounted to \$436,651 and \$377,299 for 2011 and 2010, respectively.

Income Taxes

The Company and its subsidiaries file a consolidated federal income tax return. Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

Earnings Per Share

The Company provides dual presentation of basic and diluted earnings per share. Basic earnings per share are calculated utilizing net income as reported in the numerator and average shares outstanding in the denominator. The computation of diluted earnings per share differs in that the dilutive effects of any stock options, warrants, and convertible securities are adjusted in the denominator.

Stock Options

As of December 31, 2011 and 2010, the Company recorded compensation expense of \$42,100 and \$29,676 related to share-based compensation awards. At December 31, 2011, there was approximately \$49,018 in unrecognized compensation cost related to unvested share-based compensation awards granted. That cost is expected to be recognized over the next two years.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Stock Options (Continued)

For purposes of computing stock compensation expense, the Company estimated the fair values of stock options using the Black-Scholes option-pricing model. The model requires the use of subjective assumptions that can materially affect fair value estimates. The fair value of each option is amortized into compensation expense on a straight-line basis between the grant date for the option and each vesting date. The fair value of each stock option granted was estimated using the following weighted-average assumptions:

Grant Year	Expected Dividend Yield	Risk-Free Interest Rate	Expected Volatility	Expected Life (in Years)
2011	5.79 %	3.27 %	17.71 %	10.00
2010	4.75 %	3.89 %	12.73 %	10.00
2009	6.20 %	2.31 %	15.53 %	6.30

The weighted-average fair value of each stock option granted for 2011 and 2010 was \$5.01 and \$5.28, respectively. There were no stock options exercised during the years ended December 31, 2011 and 2010.

Mortgage Servicing Rights (“MSRs”)

The Company has agreements for the express purpose of selling loans in the secondary market. The Company retains servicing rights for certain loans. Originated MSRs are recorded by allocating total costs incurred between the loan and servicing rights based on their relative fair values. MSRs are amortized in proportion to the estimated servicing income over the estimated life of the servicing portfolio. The Company performs an impairment review of the MSRs and recognizes impairment through a valuation account. MSRs are a component of accrued interest and other assets on the Consolidated Balance Sheet. Gains and losses on sales of loans are recognized at settlement dates and are determined by the difference between the sales proceeds and the carrying value of the loans. All sales are made with limited recourse. For the years ended December 31, 2011 and 2010, the Company recorded gross servicing rights of \$319,725 and \$324,141 with a reserve for impairment of \$150,322 and \$135,055, respectively.

Transfer of Assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when: (1) the assets have been isolated from the Company; (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets; and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Cash Flow Information

The Company has defined cash and cash equivalents as those amounts included in the balance sheet captions “Cash and due from banks” and “Interest-bearing deposits with other institutions” that have original maturities of less than 90 days.

Reclassification of Comparative Amounts

Certain items previously reported have been reclassified to conform to the current year’s format. Such reclassifications did not affect net income or stockholders’ equity.

2. EARNINGS PER SHARE

There are no convertible securities that would affect the numerator in calculating basic and diluted earnings per share; therefore, net income as presented on the Consolidated Statement of Income will be used as the numerator. The following table sets forth the composition of the weighted-average common shares (denominator) used in the basic and diluted earnings per share computation.

	2011	2010
Weighted-average common shares outstanding	616,925	610,000
Average treasury stock shares	(69,675)	(73,233)
Average unearned nonvested RSP shares	(8,515)	(7,424)
Weighted-average common shares and common stock equivalents used to calculate basic earnings per share	538,735	529,343
Additional common stock equivalents (nonvested stock) used to calculate diluted earnings per share	710	398
Additional common stock equivalents (stock options) used to calculate diluted earnings per share	1,291	2,231
Weighted-average common shares and common stock equivalents used to calculate diluted earnings per share	540,736	531,972

Options to purchase 48,620 and 65,760 shares of common stock at a price of \$68.25 to \$96.75, as of December 31, 2011 and 2010, and 4,956 and 5,293 shares of restricted stock ranging in price from \$59.50 to \$93.00, respectively, were not included in the computation of diluted earnings per share. To include these shares would have been antidilutive.

3. INVESTMENT SECURITIES AVAILABLE FOR SALE

The amortized cost and fair value of investment securities available for sale are as follows:

	2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government agency securities	\$ 23,682,923	\$ 688,742	\$ (50)	\$ 24,371,615
Obligations of states and political subdivisions	51,204,454	3,054,779	(36,077)	54,223,156
Corporate securities	3,365,045	-	(463,700)	2,901,345
Mortgage-backed securities in government-sponsored entities	31,861,904	451,776	(3,093)	32,310,587
Total debt securities	110,114,326	4,195,297	(502,920)	113,806,703
Equity securities in financial institutions	318,800	56,725	(11,736)	363,789
Total	\$ 110,433,126	\$ 4,252,022	\$ (514,656)	\$ 114,170,492

3. INVESTMENT SECURITIES AVAILABLE FOR SALE (Continued)

	2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. treasury securities	\$ 12,773,866	\$ 127,833	\$ -	\$ 12,901,699
U.S. government agency securities	37,053,379	182,459	(493,846)	36,741,992
Obligations of states and political subdivisions	57,664,105	912,020	(634,554)	57,941,571
Corporate securities	4,043,027	91,564	(374,811)	3,759,780
Mortgage-backed securities in government-sponsored entities	8,839,595	202,110	(37,592)	9,004,113
Total debt securities	120,373,972	1,515,986	(1,540,803)	120,349,155
Equity securities in financial institutions	460,298	73,124	(20,292)	513,130
Total	\$ 120,834,270	\$ 1,589,110	\$ (1,561,095)	\$ 120,862,285

The following tables show the Company's gross unrealized losses and fair value, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position, at December 31, 2011 and 2010.

	2011					
	Less than Twelve Months		Twelve Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. government agency securities	\$ 999,950	\$ (50)	\$ -	\$ -	\$ 999,950	\$ (50)
Obligations of states and political subdivisions	321,942	(82)	436,796	(35,995)	758,738	(36,077)
Corporate securities	2,315,813	(81,732)	585,532	(381,968)	2,901,345	(463,700)
Mortgage-backed securities in government-sponsored entities	6,745,746	(3,093)	-	-	6,745,746	(3,093)
Total debt securities	10,383,451	(84,957)	1,022,328	(417,963)	11,405,779	(502,920)
Equity securities in financial institutions	167,456	(11,736)	-	-	167,456	(11,736)
Total	\$ 10,550,907	\$ (96,693)	\$ 1,022,328	\$ (417,963)	\$ 11,573,235	\$ (514,656)

3. INVESTMENT SECURITIES AVAILABLE FOR SALE (Continued)

	2010					
	Less than Twelve Months		Twelve Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. government agency securities	\$ 22,169,080	\$ (493,846)	\$ -	\$ -	\$ 22,169,080	\$ (493,846)
Obligations of states and political subdivisions	24,938,008	(604,970)	443,059	(29,584)	25,381,067	(634,554)
Corporate securities	1,803,861	(21,666)	114,355	(353,145)	1,918,216	(374,811)
Mortgage-backed securities in government-sponsored entities	4,762,831	(37,592)	-	-	4,762,831	(37,592)
Total debt securities	53,673,780	(1,158,074)	557,414	(382,729)	54,231,194	(1,540,803)
Equity securities in financial institutions	-	-	79,590	(20,292)	79,590	(20,292)
Total	\$ 53,673,780	\$ (1,158,074)	\$ 637,004	\$ (403,021)	\$ 54,310,784	\$ (1,561,095)

U.S. Government agency securities. The unrealized loss on one investment in U.S. government obligations and direct obligations of U.S. government agencies was caused by interest rate increases. The contractual terms of these investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at December 31, 2011.

Obligations of states and political subdivisions. The Company's unrealized losses on two municipal bonds relates to investments within the governmental service sector. The unrealized losses are primarily caused by recent decreases in profitability and profit forecasts, in general, by industry analysts. The contractual terms of these investments do not permit the issuer to settle the security at a price less than the par value of the investment. The Company currently does not believe it is probable that it will be unable to collect all amounts due according to the contractual terms of the investments. Because the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their par value, which may be maturity, it does not consider these investments to be other-than-temporarily impaired at December 31, 2011.

Corporate securities. The Company had unrealized losses on investments in seven different debt securities with an aggregate fair value of \$2,901,345 at December 31, 2011. The unrealized losses on these debt securities amounted to \$463,700 at December 31, 2011. Due to dislocations in the credit markets broadly, and the lack of trading and new issuances, market price indications generally reflect the lack of liquidity in the market. Prices on debt securities were calculated by a third-party valuation company. The valuation methodology is based on the premise that the fair value of the security's collateral should approximate the fair value of its liabilities. Based on cash flow forecasts for the securities, the Company expects to recover the remaining amortized cost of these securities. Furthermore, the Company does not intend to sell these securities and it is not more likely than not that the Company will be required to sell these securities before recovery of their cost basis, which may be maturity. Therefore, it does not consider these investments to be other-than-temporarily impaired at December 31, 2011.

3. INVESTMENT SECURITIES AVAILABLE FOR SALE (Continued)

Mortgage-backed securities in government-sponsored entities. The unrealized losses on the Company's investment in three mortgage-backed securities were caused by interest rate increases. The Company purchased those investments at a premium relative to their face amount, and the contractual cash flows of those investments are guaranteed by an agency of the U.S. government. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost basis of the Company's investments. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at December 31, 2011.

Equity securities. The Company's investments in four marketable equity securities consist primarily of common stock of entities in the financial services industry. As of December 31, 2011, the Company recognized in earnings impairment charges of \$8,728 on one investment in common stock of a community bank, resulting from the duration and extent to which the market value has been less than the cost and the performance of the financial institution over the past two years. Based on the Company's analysis, and because the Company has the ability and intent to hold the investments until recovery of its cost basis, except for the investment mentioned above, the Company does not consider the remaining assets to be other-than-temporarily impaired at December 31, 2011.

The amortized cost and fair value of debt securities at December 31, 2011, by contractual maturity, are shown below. Expected maturities of mortgage-backed securities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available for Sale	
	Amortized Cost	Fair Value
Due in one year or less	\$ 2,004,333	\$ 2,016,193
Due after one year through five years	26,197,163	27,189,504
Due after five years through ten years	29,546,850	30,997,445
Due after ten years	52,365,980	53,603,561
Total	<u>\$ 110,114,326</u>	<u>\$ 113,806,703</u>

Investment securities with a carrying value of \$79,829,596 and \$90,418,896 at December 31, 2011 and 2010, respectively, were pledged to secure deposits and other purposes as required by law.

The following is a summary of proceeds received, gross gains, and gross losses realized on the sale of investment securities available for sale for the years ended December 31:

	2011	2010
Proceeds from sales	\$ 53,533,950	\$ 45,120,669
Gross gains	939,368	1,706,450
Gross losses	98,792	655,451
Other-than-temporary impairment loss	8,728	28,167

4. LOANS

Major classifications of loans are summarized as follows:

	2011	2010
Commercial real estate	\$ 120,270,997	\$ 126,325,616
Commercial and industrial	79,754,672	88,126,648
Agricultural	19,294,360	19,126,593
State and political subdivisions	25,125,149	23,936,034
Consumer	45,026,255	44,439,561
Residential real estate	79,734,409	71,596,998
	<u>369,205,842</u>	<u>373,551,450</u>
Less allowance for loan losses	7,042,911	6,245,441
Net loans	<u>\$ 362,162,931</u>	<u>\$ 367,306,009</u>

Mortgage loans serviced by the Company for others amounted to \$54,190,608 and \$54,939,124 at December 31, 2011 and 2010, respectively.

The Company grants residential, commercial, and consumer loans to customers throughout its trade area, which is concentrated in central Pennsylvania. Such loans are subject to, at origination, credit risk assessment by management following the Company's lending policy. Although the Company has a diversified loan portfolio at December 31, 2011 and 2010, a substantial portion of its debtors' ability to honor their loan agreements is dependent upon the economic stability of its immediate trade area.

In the normal course of business, loans are extended to directors, executive officers, and their associates. A summary of loan activity for those directors, executive officers, and their associates with loan balances in excess of \$60,000 for the year ended December 31, 2011 is as follows:

2010	Additions	Amounts Collected	Change in Executive Officer Status	2011
\$ 7,576,927	\$ 4,944,438	\$ 5,622,172	\$ (565,773)	\$ 6,333,420

5. ALLOWANCE FOR LOAN LOSSES

Changes in the allowance for loan losses for the years ended December 31 are as follows:

	2011	2010
Balance, January 1	\$ 6,245,441	\$ 5,396,553
Add:		
Provisions charged to operations	800,000	1,850,000
Recoveries	14,419	10,424
Less loans charged off	<u>(16,949)</u>	<u>(1,011,536)</u>
Balance, December 31	<u>\$ 7,042,911</u>	<u>\$ 6,245,441</u>

5. ALLOWANCE FOR LOAN LOSSES (Continued)

Management has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and losses inherent in the loan portfolio. For purposes of determining the allowance for loan losses, the Company has segmented certain loans in the portfolio by product type. Loans are segmented into the following pools: commercial real estate loans, commercial and industrial loans, agricultural loans, state and political subdivision loans, consumer loans, and residential real estate loans. Historical loss percentages for each risk category are calculated and used as the basis for calculating allowance allocations. These historical loss percentages are calculated over a two-year period for all portfolio segments. Certain qualitative factors are then added to the historical loss percentages to get the adjusted factor to be applied to nonclassified loans. The following qualitative factors are analyzed to determine allocations for nonclassified loans for each portfolio segment:

- Changes in lending policies and procedures
- Changes in economic and business conditions
- Changes in nature and volume of the loan portfolio
- Changes in lending staff experience and ability
- Changes in past-due loans, nonaccrual loans, and classified loans
- Changes in loan review
- Changes in underlying value of collateral-dependent loans
- Levels of credit concentrations
- Effects of external factors, such as legal and regulatory requirements

These qualitative factors are reviewed each quarter and adjusted based upon relevant changes within the Bank's operating environment. During 2011, the qualitative factors percentages for commercial real estate loans, commercial and industrial loans, state and political subdivision loans, and consumer loans all increased, while the qualitative factors for agricultural loans and residential real estate loans remained approximately the same. Changes in lending staff experience and ability, changes in the loan review process, and the effect of external factors all contributed to the increase in factor percentages for both commercial real estate loans and commercial and industrial loans. Changes in the underlying value of collateral-dependent loans also contributed to the factor percentage increase for commercial real estate loans. The increase in factor percentage for consumer loans was attributable to changes in economic and business conditions, along with changes in the loan review process and changes in external factors, while the increase in factor percentage for state and political subdivision loans was attributable solely to changes in the lending staff's experience and ability. The change in lending staff experience and ability factor percentage increased because of the retirement of some key lending personnel in 2011 combined with the addition of some new, less experienced lending personnel during the same time period. The changes in the loan review process factor percentage increased because of ongoing changes in the credit risk management process, while the effect of external factors' percentage increased due to a number of reasons, including the enactment of the Dodd-Frank Act. The changes in the underlying value of collateral-dependent loans increase in the commercial real estate category are attributable to the ongoing decline in market value of commercial real estate within the Bank's primary market area, while the changes in economic and business conditions' increase in the consumer loan category are attributable to the continued stagnant unemployment numbers in the Bank's market area.

We consider commercial real estate loans, commercial and industrial loans, agricultural loans and consumer loans to be riskier than one-to-four family residential mortgage loans. Commercial real estate loans entail significant additional credit risks compared to one-to-four family residential mortgage loans, as they involve large loan balances concentrated with single borrowers or groups of related borrowers. In addition, the payment experience on loans secured by income-producing properties typically depends on the successful operation of the related real estate project and/or business operation of the borrower who is also the primary occupant, and thus may be subject to a greater extent to adverse conditions in the real estate market and in the general economy. Commercial and industrial loans, along with agricultural loans, involve a higher risk of default than residential mortgage loans of like duration since their repayment is generally dependent on the successful operation of the borrower's business and the sufficiency of collateral, if any. The repayment of agricultural loans can also be impacted by commodity prices going up and down. Although a customer's ability to repay for both one-to-four family residential mortgage loans and consumer loans is highly dependent on the local economy, especially employment levels, consumer loans as a group generally present a higher degree of risk because of the nature of collateral, if any. State and political subdivision loans carry approximately the same risk as residential real estate loans as most state and

5. ALLOWANCE FOR LOAN LOSSES (Continued)

political subdivision loans are either backed by the full taxing authority of a municipality or the revenue of a municipal authority.

The following tables present, by portfolio segment, the changes in the allowance for loan losses and the recorded investment in loans as of and for the years ended December 31:

	2011							
	Commercial Real Estate	Commercial and Industrial	Agricultural	State and Political Subdivisions	Consumer	Residential Real Estate	Unallocated	Total
Allowance for loan losses:								
Beginning balance	\$ 3,023,441	\$ 1,854,554	\$ 255,190	\$ 105,893	\$ 403,463	\$ 455,083	\$ 147,817	\$ 6,245,441
Charge-offs	-	(6,258)	-	-	(10,691)	-	-	(16,949)
Recoveries	-	9,738	1,402	-	3,279	-	-	14,419
Provision	587,464	224,651	(54,072)	(4,342)	(84,848)	(93,476)	224,623	800,000
Ending balance	\$ 3,610,905	\$ 2,082,685	\$ 202,520	\$ 101,551	\$ 311,203	\$ 361,607	\$ 372,440	\$ 7,042,911
Ending balance individually evaluated for impairment	\$ 495,725	\$ 272,299	\$ -	\$ -	\$ 29,000	\$ 59,840	\$ -	\$ 856,864
Ending balance collectively evaluated for impairment	\$ 3,115,180	\$ 1,810,386	\$ 202,520	\$ 101,551	\$ 282,203	\$ 301,767	\$ 372,440	\$ 6,186,047
Loans:								
Individually evaluated for impairment	\$ 4,476,570	\$ 1,252,246	\$ 90,993	\$ -	\$ 104,289	\$ 269,806	\$ -	\$ 6,193,904
Collectively evaluated for impairment	115,794,427	78,502,426	19,203,367	25,125,149	44,921,966	79,464,603	-	363,011,938
Ending balance	\$ 120,270,997	\$ 79,754,672	\$ 19,294,360	\$ 25,125,149	\$ 45,026,255	\$ 79,734,409	\$ -	\$ 369,205,842
	2010							
	Commercial Real Estate	Commercial and Industrial	Agricultural	State and Political Subdivisions	Consumer	Residential Real Estate	Unallocated	Total
Allowance for loan losses:								
Beginning balance	\$ 2,837,773	\$ 1,242,249	\$ 240,231	\$ -	\$ 478,002	\$ 342,768	\$ 255,531	\$ 5,396,554
Charge-offs	(676,862)	(272,903)	-	(27,915)	(33,857)	-	-	(1,011,537)
Recoveries	-	4,729	1,955	-	3,740	-	-	10,424
Provision	862,530	880,479	13,004	133,808	(44,422)	112,315	(107,714)	1,850,000
Ending balance	\$ 3,023,441	\$ 1,854,554	\$ 255,190	\$ 105,893	\$ 403,463	\$ 455,083	\$ 147,817	\$ 6,245,441
Ending balance individually evaluated for impairment	\$ 97,347	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 97,347
Ending balance collectively evaluated for impairment	\$ 2,926,094	\$ 1,854,554	\$ 255,190	\$ 105,893	\$ 403,463	\$ 455,083	\$ 147,817	\$ 6,148,094
Loans:								
Individually evaluated for impairment	\$ 2,626,582	\$ 1,422,441	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 4,049,023
Collectively evaluated for impairment	123,699,034	86,704,207	19,126,593	23,936,034	44,439,561	71,596,998	-	369,502,427
Ending balance	\$ 126,325,616	\$ 88,126,648	\$ 19,126,593	\$ 23,936,034	\$ 44,439,561	\$ 71,596,998	\$ -	\$ 373,551,450

5. ALLOWANCE FOR LOAN LOSSES (Continued)

Credit Quality Information

The following tables represent the commercial credit exposures by internally-assigned grades for the years ended December 31, 2011 and 2010, respectively. The grading analysis estimates the capability of the borrower to repay the contractual obligations under the loan agreements as scheduled or at all. The Company's internal credit risk grading system is based on experiences with similarly graded loans.

The Company's internally-assigned grades are as follows:

Pass loans are loans which are protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral. Special Mention loans are loans where a potential weakness or risk exists, which could cause a more serious problem if not corrected. Substandard loans are loans that have a well-defined weakness based on objective evidence and are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Doubtful loans have all the weaknesses inherent in a substandard asset. In addition, these weaknesses make collection or liquidation in full highly questionable and improbable, based on existing circumstances. Finally, loans classified as Loss are considered uncollectible, or of such value that continuance as an asset is not warranted.

	2011				
	Commercial Real Estate	Commercial and Industrial	Agricultural	State and Political Subdivisions	Total
Pass	\$ 90,581,881	\$ 63,974,717	\$ 17,650,944	\$ 24,912,457	\$ 197,119,999
Special Mention	9,447,786	5,523,313	598,908	212,692	15,782,699
Substandard	17,856,862	9,731,488	1,044,508	-	28,632,858
Doubtful	2,384,468	525,154	-	-	2,909,622
Loss	-	-	-	-	-
Total	\$ 120,270,997	\$ 79,754,672	\$ 19,294,360	\$ 25,125,149	\$ 244,445,178

	2010				
	Commercial Real Estate	Commercial and Industrial	Agricultural	State and Political Subdivisions	Total
Pass	\$ 93,555,529	\$ 69,502,061	\$ 16,828,267	\$ 23,936,034	\$ 203,821,891
Special Mention	15,409,637	7,870,482	1,054,163	-	24,334,282
Substandard	14,733,868	10,709,323	1,244,163	-	26,687,354
Doubtful	2,626,582	44,782	-	-	2,671,364
Loss	-	-	-	-	-
Total	\$ 126,325,616	\$ 88,126,648	\$ 19,126,593	\$ 23,936,034	\$ 257,514,891

5. ALLOWANCE FOR LOAN LOSSES (Continued)

Credit Quality Information (Continued)

For consumer loans, the Company evaluates credit quality based on whether the loan is considered performing or nonperforming. The following table presents the balances of consumer loans by classes of loan portfolio based on payment performance as of December 31:

	2011		
	Consumer	Residential Real Estate	Total
Performing	\$ 44,872,546	\$ 79,066,061	\$ 123,938,607
Nonperforming	153,709	668,348	822,057
Total	\$ 45,026,255	\$ 79,734,409	\$ 124,760,664

	2010		
	Consumer	Residential Real Estate	Total
Performing	\$ 44,268,145	\$ 71,289,516	\$ 115,557,661
Nonperforming	171,416	307,482	478,898
Total	\$ 44,439,561	\$ 71,596,998	\$ 116,036,559

Age Analysis of Past-Due Loans by Class

The following are tables which show the aging analysis of past-due loans as of December 31:

	2011						
	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total Loans	Recorded Investment 90 Days and Accruing
	Commercial real estate	\$ 954,872	\$ 1,194,157	\$ 2,783,066	\$ 4,932,095	\$ 115,338,902	\$ 120,270,997
Commercial and industrial	480,256	-	729,903	1,210,159	78,544,513	79,754,672	-
Agricultural	257,928	-	90,993	348,921	18,945,439	19,294,360	-
State and political subdivisions	118,908	-	-	118,908	25,006,241	25,125,149	-
Consumer	189,895	45,219	153,709	388,823	44,637,432	45,026,255	49,420
Residential real estate	138,046	-	668,348	806,394	78,928,015	79,734,409	398,542
Total	\$2,139,905	\$ 1,239,376	\$ 4,426,019	\$ 7,805,300	\$ 361,400,542	\$ 369,205,842	\$ 447,962

	2010						
	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total Loans	Recorded Investment 90 Days and Accruing
	Commercial real estate	\$ -	\$ -	\$ 650,042	\$ 650,042	\$ 125,675,574	\$ 126,325,616
Commercial and industrial	631,679	96,955	20,503	749,137	87,377,511	88,126,648	-
Agricultural	-	-	-	-	19,126,593	19,126,593	-
State and political subdivisions	-	-	-	-	23,936,034	23,936,034	-
Consumer	113,404	64,365	171,416	349,185	44,090,376	44,439,561	171,416
Residential real estate	392,191	28,206	279,276	699,673	70,897,325	71,596,998	279,276
Total	\$1,137,274	\$ 189,526	\$ 1,121,237	\$ 2,448,037	\$ 371,103,413	\$ 373,551,450	\$ 450,692

5. ALLOWANCE FOR LOAN LOSSES (Continued)

Impaired Loans

Management considers commercial real estate loans, commercial and industrial loans, agricultural loans, and state and political subdivision loans which are 90 days or more past due to be impaired. After becoming 90 days or more past due, these categories of loans are measured for impairment. These loans are analyzed to determine if it is probable that all amounts will not be collected according to the contractual terms of the loan agreement. If management determines that the fair value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs, and unamortized premium or discount), impairment is recognized through a provision or through a charge to the allowance for loan losses.

The following tables include the recorded investment and unpaid principal balances for impaired loans with the associated allowance amount as of December 31:

	2011				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial real estate	\$ 2,561,616	\$ 2,561,616	\$ -	\$ 2,318,776	\$ 129,281
Commercial and industrial	287,539	287,539	-	1,236,654	59,394
Agricultural	90,993	90,993	-	173,373	3,893
State and political subdivisions	-	-	-	-	-
Consumer	57,083	57,083	-	94,985	8,351
Residential real estate	231,066	231,066	-	224,562	4,112
	<u>3,228,297</u>	<u>3,228,297</u>	<u>-</u>	<u>4,048,350</u>	<u>205,031</u>
With an allowance recorded:					
Commercial real estate	1,914,954	1,914,954	495,725	483,530	-
Commercial and industrial	964,707	964,707	272,299	147,859	-
Agricultural	-	-	-	-	-
State and political subdivisions	-	-	-	-	-
Consumer	47,206	47,206	29,000	11,801	-
Residential real estate	38,740	38,740	59,840	22,598	-
	<u>2,965,607</u>	<u>2,965,607</u>	<u>856,864</u>	<u>665,788</u>	<u>-</u>
Total:					
Commercial real estate	4,476,570	4,476,570	495,725	2,802,306	129,281
Commercial and industrial	1,252,246	1,252,246	272,299	1,384,513	59,394
Agricultural	90,993	90,993	-	173,373	3,893
State and political subdivisions	-	-	-	-	-
Consumer	104,289	104,289	29,000	106,786	8,351
Residential real estate	269,806	269,806	59,840	247,160	4,112
Total	<u>\$ 6,193,904</u>	<u>\$ 6,193,904</u>	<u>\$ 856,864</u>	<u>\$ 4,714,138</u>	<u>\$ 205,031</u>

5. ALLOWANCE FOR LOAN LOSSES (Continued)

Impaired Loans (Continued)

	2010				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial real estate	\$ 2,158,115	\$ 2,158,115	\$ -	\$ 2,186,997	\$ 145,898
Commercial and industrial	1,422,441	1,422,441	-	739,670	16,817
Agricultural	-	-	-	271,564	21,016
State and political subdivisions	-	-	-	-	-
Consumer	-	-	-	-	-
Residential real estate	-	-	-	-	-
	<u>3,580,556</u>	<u>3,580,556</u>	<u>-</u>	<u>3,198,231</u>	<u>183,731</u>
With an allowance recorded:					
Commercial real estate	468,467	468,467	97,347	4,261,352	-
Commercial and industrial	-	-	-	142,320	-
Agricultural	-	-	-	-	-
State and political subdivisions	-	-	-	-	-
Consumer	-	-	-	-	-
Residential real estate	-	-	-	-	-
	<u>468,467</u>	<u>468,467</u>	<u>97,347</u>	<u>4,403,672</u>	<u>-</u>
Total:					
Commercial real estate	2,626,582	2,626,582	97,347	6,448,349	145,898
Commercial and industrial	1,422,441	1,422,441	-	881,990	16,817
Agricultural	-	-	-	271,564	21,016
State and political subdivisions	-	-	-	-	-
Consumer	-	-	-	-	-
Residential real estate	-	-	-	-	-
Total	<u>\$ 4,049,023</u>	<u>\$ 4,049,023</u>	<u>\$ 97,347</u>	<u>\$ 7,601,903</u>	<u>\$ 183,731</u>

Nonaccrual Loans

Loans are considered nonaccrual upon reaching 90 days of delinquency even though the Company may be receiving partial payments of interest and partial repayments of principal on such loans. When a loan is placed on nonaccrual status, previously accrued but unpaid interest is deducted from interest income.

On the following table are the loan balances on nonaccrual status as of December 31:

	2011	2010
Commercial real estate	\$ 4,476,571	\$ 2,626,582
Commercial and industrial	1,102,246	1,422,441
Agricultural	90,993	-
State and political subdivisions	-	-
Consumer	104,289	-
Residential real estate	269,806	28,206
Total	<u>\$ 6,043,905</u>	<u>\$ 4,077,229</u>

5. ALLOWANCE FOR LOAN LOSSES (Continued)

Troubled Debt Restructuring

The Company's loan portfolio also includes certain loans that have been modified in a troubled debt restructuring ("TDR"), where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from the Company's loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance, or other actions. At December 31, 2011, the Company had four commercial real estate loans totaling \$2,134,564 that are TDRs and are classified as nonperforming and one commercial and industrial loan totaling \$48,802 that is a TDR that is classified nonperforming. At December 31, 2010, the Company did not have any TDRs.

When the Company modifies a loan, management evaluates any possible impairment based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan agreement, except when the sole remaining source of repayment for the loan is the operation or liquidation of the collateral. In these cases, management uses the current fair value of the collateral, less selling costs, instead of discounted cash flows. If management determines that the value of the modified loan is less than the recorded investment in the loan, impairment is recognized by segment of class of loan, as applicable, through a charge-off to the allowance. Segment and class status is determined by the loan's classification at origination. As of December 31, 2011 no specific reserves have been established against the TDRs. Also, as of December 31, 2011 no charge-offs for the TDRs were required.

Loan modifications that are considered "TDRs" completed during the year ending December 31, 2011 were as follows:

	2011		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled debt restructurings:			
Commercial real estate loans	4	\$ 2,148,060	\$ 2,148,060
Commercial and industrial	1	50,299	50,299
Agricultural	-	-	-
State and political subdivision	-	-	-
Consumer	-	-	-
Residential real estate	-	-	-
Total	5	\$ 2,198,359	\$ 2,198,359

As of December 31, 2011, none of the loan modifications classified as TDRs subsequently defaulted within one year of modification.

6. PREMISES AND EQUIPMENT

Major classifications of premises and equipment are summarized as follows:

	2011	2010
Land and land improvements	\$ 793,458	\$ 793,458
Building and leasehold improvements	15,535,165	14,955,760
Furniture, fixtures, and equipment	5,538,570	4,636,864
	21,867,193	20,386,082
Less accumulated depreciation	7,655,566	6,752,790
Total	\$ 14,211,627	\$ 13,633,292

Depreciation and amortization charged to operations was \$937,985 in 2011 and \$850,118 in 2010.

7. GOODWILL

As of each of the years ended December 31, 2011 and 2010, goodwill had a carrying amount of \$1,668,699. The gross carrying amount of goodwill was tested for impairment in the third quarter, after the annual forecasting process. There was no impairment for the years ended December 31, 2011 and 2010.

8. DEPOSITS

The scheduled maturities of time deposits approximate the following:

Year Ending December 31,	Amount
2012	\$ 89,285,908
2013	30,400,711
2014	19,237,752
2015	10,855,847
2016	4,314,089
Thereafter	19,533,287
	\$ 173,627,594

The aggregate of all time deposit accounts of \$100,000 or more amounted to \$62,843,237 and \$65,447,156 at December 31, 2011 and 2010, respectively.

9. SHORT-TERM BORROWINGS

Short-term borrowings include overnight repurchase agreements through the FHLB, Federal Funds Purchased, and repurchase agreements with customers. Short-term borrowings also include a \$5,000,000 unsecured line of credit with a commercial bank for the years ended December 31, 2011 and 2010, respectively. The line of credit agreement contains various covenants requiring the Company to maintain certain levels of financial performance. At December 31, 2011 and 2010, the Company was in compliance with all of its covenants. The outstanding balances and related information for short-term borrowings are summarized as follows:

	2011	2010
Balance at year-end	\$ 5,696,162	\$ 7,608,645
Average balance outstanding	10,577,428	8,699,070
Maximum month-end balance	16,028,082	14,254,009
Weighted-average rate at year-end	1.56%	2.66%
Weighted-average rate during the year	1.93%	1.40%

10. OTHER BORROWINGS

The following table sets forth information concerning other borrowings:

Description	Maturity Range		Weighted-Average Interest Rate	Stated Interest Rate Range		At December 31,	
	From	To		From	To	2011	2010
Convertible	08/22/12	08/22/12	4.44 %	4.44 %	4.44 %	\$ 5,000,000	\$ 10,000,000
Fixed rate	01/03/12	11/14/17	3.58	1.32	4.96	28,484,805	30,192,205
Fixed rate amortizing	07/17/13	06/26/18	3.43	1.95	6.53	4,629,113	6,442,935
Mid-term repos	07/08/13	07/08/13	1.53	1.53	1.53	3,000,000	6,000,000
Subordinated capital notes	03/23/19	12/28/20	7.83	3.88	8.50	4,750,000	4,050,000
Note payable	03/17/35	11/23/35	4.33	2.56	6.11	6,186,000	6,186,000
						<u>\$ 52,049,918</u>	<u>\$ 62,871,140</u>

Maturities of other borrowings at December 31, 2011 are summarized as follows:

Year Ending December 31,	Amount	Weighted-Average Rate
2012	\$ 11,329,200	4.41 %
2013	16,107,445	3.37
2014	4,217,600	3.19
2015	4,224,486	2.77
2016	2,012,000	1.34
2017 and after	14,159,187	5.39
	<u>\$ 52,049,918</u>	4.01 %

The terms of the convertible borrowings allow the FHLB to convert the interest rate to an adjustable rate based on the three-month London Interbank Offered Rate ("LIBOR") after two years from the original date of the advance. The fixed rate amortizing borrowings require monthly payments of principal and interest.

Borrowing capacity consists of credit arrangements with the FHLB. FHLB borrowings are subject to annual renewal, incur no service charges, and are secured by a blanket security agreement on certain investment and mortgage-backed securities, outstanding residential mortgages, and the Bank's investment in FHLB stock. As of December 31, 2011, the Bank's maximum borrowing capacity with the FHLB was approximately \$146 million.

The Company formed a special purpose entity ("Entity") to issue \$3,093,000 of fixed/floating rate subordinated debt securities with a stated maturity of March 17, 2035. The rate on these securities is determined quarterly and floats based on three-month LIBOR plus 2.00 percent. The Entity may redeem them, in whole or in part, at face value on or after March 17, 2010. The Company borrowed the proceeds from the Entity in the form of a \$3,093,000 note payable, which is included in the liabilities section of the Company's Consolidated Balance Sheet.

The Company formed an additional special purpose entity to issue \$3,093,000 of fixed/floating rate subordinated debt securities with a stated maturity of November 23, 2035. These securities bear a fixed rate of 6.11 percent until November 23, 2015, at which time the rate is determined quarterly and floats based on three-month LIBOR plus 1.50 percent. The Entity may redeem them, in whole or in part, at face value on or after November 23, 2010. The Company borrowed the proceeds from the Entity in the form of a \$3,093,000 note payable, which is included in the liabilities section of the Company's Consolidated Balance Sheet.

The Company's minority interests in these entities were recorded at the initial investment amount and is included in the accrued interest and other assets on the Consolidated Balance Sheet. These entities are not consolidated as part of the Company's consolidated financial statements.

10. OTHER BORROWINGS (Continued)

The Company issued \$3,000,000 of fixed rate subordinated debt securities with stated maturities of March 23, 2019 through June 26, 2019. These securities bear a fixed annual rate of 8.5 percent. The Company may redeem them, in whole or in part, at face value on or after March 23, 2014. These borrowings are included in the liabilities section of the Company's Consolidated Balance Sheet.

The Company issued \$1,700,000 of fixed rate subordinated debt securities with stated maturities of November 12, 2020 through February 10, 2021 and \$50,000 of adjustable rate subordinated debt securities with a stated maturity of March 2, 2021. The fixed securities bear an annual rate of 6.75 percent and the adjustable rate securities bear a rate of three-month LIBOR plus 3.50 percent and adjust quarterly. The Company may redeem them, in whole or in part, at face value on or after November 12, 2015. These borrowings are included in the liabilities section of the Company's Consolidated Balance Sheet.

11. INCOME TAXES

The provision for federal income taxes consists of:

	2011	2010
Current	\$ 542,867	\$ 898,857
Deferred	(104,051)	(428,312)
Total provision	<u>\$ 438,816</u>	<u>\$ 470,545</u>

The tax effects of deductible and taxable temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are as follows:

	2011	2010
Deferred tax assets:		
Allowance for loan losses	\$ 2,394,590	\$ 2,123,450
Deferred compensation	235,036	245,923
Core deposit intangible assets	32,759	41,861
Alternative minimum tax carryforward	479,512	474,550
Asset valuation allowances	313,102	326,381
Employee compensation accruals	266,212	187,438
Nonaccrual interest receivable	84,741	58,126
Capital loss carryforward	228,767	157,627
Deferred tax assets	<u>4,034,719</u>	<u>3,615,356</u>
Deferred tax liabilities:		
Premises and equipment	1,052,800	829,422
Goodwill	506,450	455,805
Deferred loan fees	141,356	138,219
Partnerships	168,844	130,692
Other	5,417	5,417
Unrealized gain on available-for-sale securities	1,270,707	9,525
Deferred tax liabilities	<u>3,145,574</u>	<u>1,569,080</u>
Net deferred tax assets	<u>\$ 889,145</u>	<u>\$ 2,046,276</u>

No valuation allowance was established at December 31, 2011 and 2010 in view of the Company's ability to carryback taxes paid in previous years and certain tax strategies, coupled with the anticipated future taxable income as evidenced by the Company's earnings potential.

11. INCOME TAXES (Continued)

The reconciliation between the federal statutory rate and the Company's effective consolidated income tax rate is as follows:

	2011		2010	
	Amount	% of Pretax Income	Amount	% of Pretax Income
Provision at statutory rate	\$ 1,385,395	34.0	% \$ 1,369,067	34.0
Tax-exempt interest	(804,586)	(19.7)	(819,340)	(20.3)
Life insurance income	(99,776)	(2.5)	(87,822)	(2.2)
Other	(42,217)	(1.0)	8,640	0.2
Actual tax expense and effective rate	\$ <u>438,816</u>	<u>10.8</u>	% \$ <u>470,545</u>	<u>11.7</u>

The Company prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Benefits from tax positions should be recognized in the financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority that would have full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be derecognized in the first subsequent financial reporting period in which that threshold is no longer met.

There is currently no liability for uncertain tax positions and no known unrecognized tax benefits. The Company recognizes, when applicable, interest and penalties related to unrecognized tax benefits in the provision for income taxes in the Consolidated Statement of Income. The Company's federal and state income tax returns for taxable years through 2007 have been closed for purposes of examination by the Internal Revenue Service and the Pennsylvania Department of Revenue.

12. EMPLOYEE BENEFITS

Savings Plan

The Bank maintains a qualified 401(k) salary reduction and profit sharing plan that covers substantially all employees. Under the plan, employees make voluntary, pretax contributions to their accounts, and the Bank contributions to the plan are at the discretion of the Board of Directors. Contributions by the Bank charged to operations were \$214,295 and \$204,465 for the years ended December 31, 2011 and 2010, respectively. The fair value of plan assets includes \$627,270 and \$604,632 pertaining to the value of the Company's common stock that is held by the plans as of December 31, 2011 and 2010, respectively.

Deferred Compensation Plan

The Company has a nonqualified deferred compensation plan that allows directors to defer fees. Outstanding balances under this arrangement for 2011 and 2010 were \$691,282 and \$723,302, respectively, and are reported as "Other liabilities" on the Consolidated Balance Sheet. Expenses related to this plan were \$1,616 and \$40,534 for December 31, 2011 and 2010, respectively.

12. EMPLOYEE BENEFITS (Continued)

Restricted Stock Plan

The Company maintains a Restricted Stock Plan (the "Plan"). Employees and non-employee corporate directors are eligible to receive awards of restricted stock based upon performance-related requirements. Awards granted under the Plan are in the form of the Company's common stock and are subject to certain vesting requirements including continuous employment or service with the Company. The Company has authorized 12,000 shares of the Company's common stock. The Plan assists the Company in attracting, retaining and motivating employees and non-employee directors to make substantial contributions to the success of the Company and to increase the emphasis on the use of equity as a key component of compensation. Compensation expense recognized related to the vesting of shares was \$193,319 and \$158,649 for the years ended December 31, 2011 and 2010, respectively.

The following is a summary of the status of the Company's restricted stock as of December 31, 2011, and changes therein during the year then ended:

	Number of Shares of Restricted Stock	Weighted-Average Grant Date Fair Value
Nonvested at January 1, 2011	7,310	\$ 66.15
Granted	5,208	59.47
Vested	(2,714)	65.08
Forfeited	(282)	63.13
Nonvested at December 31, 2011	<u>9,522</u>	\$ 62.89

Stock Option Plan

The Company has a fixed director and employee stock-based compensation plan. The plan has total options available to grant of 190,000 shares of common stock. The exercise price for the purchase of shares subject to a stock option may not be less than 100 percent of the fair market value of the shares covered by the option on the date of the grant. The term of stock options will not exceed ten years from the date of grant. Options granted are primarily vested evenly over a three-year period from the grant date.

The following table presents share data related to the outstanding options:

	Number of Options	Weighted-Average Exercise Price
Outstanding, January 1, 2011	71,983	\$ 80.21
Granted	13,000	59.52
Exercised	-	-
Forfeited	(6,746)	77.18
Outstanding, December 31, 2011	<u>78,237</u>	\$ 77.04
Exercisable at year-end	<u>55,141</u>	\$ 83.74

12. EMPLOYEE BENEFITS (Continued)

Stock Option Plan (Continued)

The following table summarizes the characteristics of stock options at December 31, 2011:

Grant Date	Exercise Price	Outstanding		Exercisable	
		Shares	Contractual Average Life	Shares	Average Exercise Price
01/24/02	\$ 90.00	5,012	0.06	5,012	\$ 90.00
02/21/02	91.00	8	0.14	8	91.00
02/27/03	90.00	4,059	0.15	4,059	90.00
09/02/03	90.00	2,222	0.67	2,222	90.00
12/29/03	91.25	3,168	2.00	3,168	91.25
03/16/04	91.25	3,450	2.20	3,450	91.25
05/26/04	94.00	734	2.40	734	94.00
06/30/04	96.75	2,618	2.49	2,618	96.75
01/05/05	93.00	8,127	3.01	8,127	93.00
02/03/05	93.00	380	3.09	380	93.00
02/09/05	93.00	26	3.11	26	93.00
02/10/05	95.00	100	3.11	100	95.00
02/24/05	96.00	42	3.15	42	96.00
03/29/05	96.00	3	3.24	3	96.00
04/26/05	96.00	441	3.32	441	96.00
07/08/05	96.00	333	3.52	333	96.00
12/08/05	95.00	1,401	3.93	1,401	95.00
12/10/05	95.25	3	3.94	3	95.25
12/16/05	95.00	150	3.96	150	95.00
12/22/05	95.00	4,440	3.97	4,440	95.00
01/25/07	88.00	545	5.07	545	88.00
02/23/07	90.00	525	5.15	525	90.00
01/31/08	76.35	6,750	5.08	6,750	76.35
03/26/09	51.00	9,800	7.23	6,521	51.00
10/27/09	70.00	1,000	7.82	666	70.00
04/01/10	68.25	10,300	8.25	3,417	68.25
04/28/11	59.50	11,800	9.24	-	59.50
10/11/11	62.00	500	9.77	-	62.00
12/22/11	56.00	300	9.98	-	56.00
		<u>78,237</u>		<u>55,141</u>	

13. COMMITMENTS

In the normal course of business, there are outstanding commitments and contingent liabilities such as commitments to extend credit, financial guarantees, and letters of credit that are not reflected in the accompanying consolidated financial statements. The Company does not anticipate any losses as a result of these transactions. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the Consolidated Balance Sheet. The contract or notional amounts of those instruments reflect the extent of involvement the Company has in the particular classes of financial instruments that consisted of the following:

	2011	2010
Commitments to extend credit	\$ 94,033,585	\$ 93,380,149
Standby letters of credit	<u>5,091,765</u>	<u>6,370,718</u>
Total	<u>\$ 99,125,350</u>	<u>\$ 99,750,867</u>

13. COMMITMENTS (Continued)

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. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Standby letters of credit represent conditional commitments issued by the Company to guarantee the performance of a customer to a third party. These instruments are issued primarily to support bid or performance-related contracts. The coverage period for these instruments is typically a one-year period with an annual renewal option subject to prior approval by management. Fees earned from the issuance of these letters are recognized upon expiration of the commitment period. For secured letters of credit, the collateral is typically Bank deposit instruments or real estate.

The Bank has committed to various operating leases for their branch and office facilities. Some of these leases include renewal options as well as specific provisions relating to rent increases. The minimum annual rental commitments under these leases outstanding at December 31, 2011 are as follows:

	Minimum Lease Payment
2012	\$ 274,972
2013	272,992
2014	269,032
2015	269,032
2016	235,363
Thereafter	<u>3,833,643</u>
Total	<u>\$ 5,155,034</u>

Rent expense under leases for each of the years ended December 31, 2011 and 2010 was \$285,923 and \$277,449, respectively.

Contingent Liabilities

The Company from time to time may be a party in various legal actions from the normal course of business activities. Management believes the liability, if any, arising from such actions will not have a material adverse effect on the Company's financial position.

14. REGULATORY RESTRICTIONS

Restriction on Cash and Due From Banks

The Bank is required to maintain reserve funds in cash or on deposit with the Federal Reserve Bank. The required reserve at December 31, 2011 and 2010, was \$1,513,000 and \$1,188,000, respectively.

Loans

Federal law prevents the Company from borrowing from the Bank unless the loans are secured by specific obligations. Further, such secured loans are limited in amount to 10 percent of the Bank's common stock and capital surplus.

Dividends

The approval of the Comptroller of the Currency is required before a national bank can pay any dividends up to the Company if the total of all dividends declared in any calendar year would exceed net profits, as defined for that year, combined with its retained net profits for the two preceding calendar years less any required transfers to surplus. Under this formula, the amount available for payment of dividends in 2012, without prior approval of the Comptroller, is approximately \$8.7 million plus net profits retained in 2012 up to the date of the dividend declaration.

14. REGULATORY RESTRICTIONS (Continued)

Dividends (Continued)

In order to manage capital and support safety and soundness of the Company and the Bank, management has decided to provide the banking regulators with written notice of any intention to pay dividends or make any capital distributions.

15. REGULATORY CAPITAL

Federal regulations require the Company and the Bank to maintain minimum amounts of capital. Specifically, each is required to maintain certain minimum dollar amounts and ratios of Total and Tier I capital to risk-weighted assets and of Tier I capital to average total assets.

In addition to the capital requirements, the Federal Deposit Insurance Corporation Improvement Act ("FDICIA") established five capital categories ranging from "well capitalized" to "critically undercapitalized." Should any institution fail to meet the requirements to be considered "adequately capitalized," it would become subject to a series of increasingly restrictive regulatory actions.

As of December 31, 2011 and 2010, the FDIC categorized the Company and the Bank as well capitalized under the regulatory framework for prompt corrective action. To be classified as a well capitalized financial institution, Total risk-based, Tier I risk-based, and Tier I leverage capital ratios must be at least 10 percent, 6 percent, and 5 percent, respectively.

The Company's actual capital ratios are presented in the following table that shows the Company met all regulatory capital requirements:

	2011		2010	
	Amount	Ratio	Amount	Ratio
Total Capital (to Risk-Weighted Assets)				
Actual	\$ 55,927,625	13.85 %	\$ 50,167,757	11.67 %
For Capital Adequacy Purposes To Be Well Capitalized	32,307,719	8.00	34,386,299	8.00
	40,384,648	10.00	1,004,609	10.00
Tier I Capital (to Risk-Weighted Assets)				
Actual	\$ 45,912,913	11.37 %	\$ 40,560,601	9.44 %
For Capital Adequacy Purposes To Be Well Capitalized	16,153,859	4.00	17,193,150	4.00
	24,230,789	6.00	25,789,724	6.00
Tier I Capital (to Average Assets)				
Actual	\$ 45,912,913	8.26 %	\$ 40,560,601	7.24 %
For Capital Adequacy Purposes To Be Well Capitalized	22,229,663	4.00	43,516,985	4.00
	27,787,078	5.00	28,016,617	5.00

15. REGULATORY CAPITAL (Continued)

The Bank's actual capital ratios are presented in the following table which shows the Bank met all regulatory capital requirements:

	2011		2010	
	Amount	Ratio	Amount	Ratio
Total Capital (to Risk-Weighted Assets)				
Actual	\$ 54,533,683	13.56 %	\$ 50,457,841	11.81 %
For Capital Adequacy Purposes To Be Well Capitalized	32,179,644	8.00	34,169,840	8.00
	40,224,655	10.00	42,712,300	10.00
Tier I Capital (to Risk-Weighted Assets)				
Actual	\$ 49,313,930	12.26 %	\$ 44,953,926	10.52 %
For Capital Adequacy Purposes To Be Well Capitalized	16,089,862	4.00	17,084,920	4.00
	24,134,793	6.00	25,627,380	6.00
Tier I Capital (to Average Assets)				
Actual	\$ 49,313,930	8.91 %	\$ 44,953,926	8.06 %
For Capital Adequacy Purposes To Be Well Capitalized	22,135,707	4.00	22,312,505	4.00
	27,669,634	5.00	27,890,631	5.00

16. FAIR VALUE MEASUREMENTS

The following disclosures show the hierarchal disclosure framework associated with the level of pricing observations utilized in measuring assets and liabilities at fair value. The three broad levels of pricing observations are as follows:

- Level I: Quoted prices are available in active markets for identical assets or liabilities as of the reported date.
- Level II: Pricing inputs are other than the quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these assets and liabilities includes items for which quoted prices are available but traded less frequently and items that are fair-valued using other financial instruments, the parameters of which can be directly observed.
- Level III: Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

This hierarchy requires the use of observable market data when available.

16. FAIR VALUE MEASUREMENTS (Continued)

The following tables present the assets reported on the Consolidated Balance Sheet at their fair value as of December 31, 2011 and 2010, by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

	December 31, 2011			
	Level I	Level II	Level III	Total
Assets:				
U.S. government agency securities	\$ -	\$ 24,371,615	\$ -	\$ 24,371,615
Obligations of states and political subdivisions	-	54,223,156	-	54,223,156
Corporate securities	-	2,801,028	100,317	2,901,345
Mortgage-backed securities in government-sponsored entities	-	32,310,587	-	32,310,587
Total debt securities	-	113,706,386	100,317	113,806,703
Equity securities	363,789	-	-	363,789
Total	\$ 363,789	\$ 113,706,386	\$ 100,317	\$ 114,170,492

	December 31, 2010			
	Level I	Level II	Level III	Total
Assets:				
U.S. treasury securities	\$ -	\$ 12,901,699	\$ -	\$ 12,901,699
U.S. government agency securities	-	36,741,992	-	36,741,992
Obligations of states and political subdivisions	-	57,941,571	-	57,941,571
Corporate securities	-	2,305,629	1,454,151	3,759,780
Mortgage-backed securities in government-sponsored entities	-	9,004,113	-	9,004,113
Total debt securities	-	118,895,004	1,454,151	120,349,155
Equity securities	513,130	-	-	513,130
Total	\$ 513,130	\$ 118,895,004	\$ 1,454,151	\$ 120,862,285

Financial instruments are considered Level III when their values are determined using pricing models, discounted cash flow methodologies or similar techniques, and at least one significant model assumption or input is unobservable. In addition to these unobservable inputs, the valuation models for Level III financial instruments typically also rely on a number of inputs that are readily observable either directly or indirectly. Level III financial instruments also include those for which the determination of fair value requires significant management judgment or estimation. The following table presents the changes in the Level III fair-value category for the years ended December 31, 2011 and 2010.

16. FAIR VALUE MEASUREMENTS (Continued)

	Corporate Securities
Balance, January 1, 2010	\$ 1,198,313
Transfers to Level III	267,165
Net change on unrealized gain on investment securities available for sale	<u>(11,327)</u>
Balance, January 1, 2011	1,454,151
Sales	(1,339,795)
Net change on unrealized gain on investment securities available for sale	<u>(14,039)</u>
Balance, December 31, 2011	<u>\$ 100,317</u>

The following tables present the assets measured on a nonrecurring basis on the Consolidated Balance Sheet at their fair value as of December 31, 2011 and 2010, by level within the fair value hierarchy. Impaired loans that are collateral dependent are written down to fair value through the establishment of specific reserves. Techniques used to value the collateral that secure the impaired loans include: quoted market prices for identical assets classified as Level I inputs and observable inputs employed by certified appraisers for similar assets classified as Level II inputs. In cases where valuation techniques included inputs that are unobservable and are based on estimates and assumptions developed by management based on the best information available under each circumstance, the asset valuation is classified as Level III input. Other real estate owned is measured at fair value, less cost to sell at the date of foreclosure. Valuations are periodically performed by management and the assets are carried at the lower of carrying amount, or fair value less cost to sell. The fair value for mortgage servicing rights is estimated by discounting contractual cashflows and adjusting for prepayment estimates. Discount rates are based upon rates generally charged for such loans with similar characteristics.

	December 31, 2011			
	Level I	Level II	Level III	Total
Assets:				
Impaired loans	\$ -	\$ -	\$ 5,337,040	\$ 5,337,040
Other real estate owned	-	370,173	-	370,173
Mortgage servicing rights	-	319,725	-	319,725

	December 31, 2010			
	Level I	Level II	Level III	Total
Assets:				
Impaired loans	\$ -	\$ -	\$ 3,951,676	\$ 3,951,676
Other real estate owned	-	396,024	-	396,024
Mortgage servicing rights	-	324,141	-	324,141

17. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS

The estimated fair values of the Company's financial instruments at December 31 are as follows:

	2011		2010	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets:				
Cash and cash equivalents	\$ 41,181,771	\$ 41,181,771	\$ 19,883,331	\$ 19,883,331
Certificates of deposit	1,619,833	1,619,833	2,734,094	2,734,094
Investment securities				
available for sale	114,170,492	114,170,492	120,862,285	120,862,285
Loans held for sale	1,401,376	1,401,376	918,342	918,342
Net loans	362,162,931	367,556,756	367,306,009	372,213,168
Regulatory stock	4,042,400	4,042,400	4,161,800	4,161,800
Bank-owned life insurance	12,097,673	12,097,673	11,684,697	11,684,697
Accrued interest receivable	2,089,706	2,089,706	2,257,625	2,257,625
Mortgage servicing rights	319,725	319,725	324,141	324,141
Financial liabilities:				
Deposits	\$ 454,660,313	\$ 460,020,954	\$ 446,001,986	\$ 449,310,136
Short-term borrowings	5,696,162	5,696,162	7,608,645	7,608,645
Other borrowings	52,049,918	53,352,801	62,871,140	64,412,272
Accrued interest payable	948,603	948,603	1,050,045	1,050,045

Financial instruments are defined as cash, evidence of ownership interest in an entity, or a contract which creates an obligation or right to receive or deliver cash or another financial instrument from/to a second entity on potentially favorable or unfavorable terms.

Fair value is defined as the amount at which a financial instrument could be exchanged in a current transaction between willing parties other than in a forced liquidation sale. If a quoted market price is available for a financial instrument, the estimated fair value would be calculated based upon the market price per trading unit of the instrument.

If no readily available market exists, the fair value estimates for financial instruments should be based upon management's judgment regarding current economic conditions, interest rate risk, expected cash flows, future estimated losses, and other factors as determined through various option pricing formulas or simulation modeling. As many of these assumptions result from judgments made by management based upon estimates, which are inherently uncertain, the resulting estimated fair values may not be indicative of the amount realizable in the sale of a particular financial instrument. In addition, changes in assumptions on which the estimated fair values are based may have a significant impact on the resulting estimated fair values.

As certain assets such as deferred tax assets and premises and equipment are not considered financial instruments, the estimated fair value of financial instruments would not represent the full value of the Company.

The Company employed simulation modeling in determining the estimated fair value of financial instruments for which quoted market prices were not available based upon the following assumptions:

Cash and Cash Equivalents, Certificates of Deposit, Loans Held for Sale, Regulatory Stock, Accrued Interest Receivable, Accrued Interest Payable, and Short-Term Borrowings

The fair value is equal to the current carrying value.

17. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS (Continued)

Investment Securities Available for Sale

The fair value of investment securities is equal to the available quoted market price. If no quoted market price is available, fair value is estimated using the quoted market price for similar securities. Fair values for certain corporate bonds were determined utilizing discounted cash flow models, due to the absence of a current market to provide reliable market quotes for the instruments.

Loans

The fair value is estimated by discounting future cash flows using current market inputs at which loans with similar terms and qualities would be made to borrowers of similar credit quality. Where quoted market prices were available, primarily for certain residential mortgage loans, such market rates were utilized as estimates for fair value.

Bank-Owned Life Insurance

The fair value is equal to the cash surrender value of the life insurance policies.

Mortgage Servicing Rights

The fair value for mortgage servicing rights is estimated by discounting contractual cash flows and adjusting for prepayment estimates. Discount rates are based upon rates generally charged for such loans with similar characteristics.

Deposits

The fair values of certificates of deposit are based on the discounted value of contractual cash flows. The discount rates are estimated using rates currently offered for similar instruments with similar remaining maturities. Demand, savings, and money market deposit accounts are valued at the amount payable on demand as of year-end.

Other Borrowings

Fair values for other borrowings are estimated using a discounted cash flow calculation that applies contractual costs currently being offered for similar borrowings.

Commitments to Extend Credit

These financial instruments are generally not subject to sale, and estimated fair values are not readily available. The carrying value, represented by the net deferred fee arising from the unrecognized commitment or letter of credit, and the fair value, determined by discounting the remaining contractual fee over the term of the commitment using fees currently charged to enter into similar agreements with similar credit risk, are not considered material for disclosure. The contractual amounts of unfunded commitments and letters of credit are presented in Note 13.

18. SUBSEQUENT EVENTS

Management has reviewed events occurring through March 14, 2012, the date the financial statements were issued, and no subsequent events occurred requiring accrual or disclosure.

19. PARENT COMPANY

Following are condensed financial statements for the Company:

CONDENSED BALANCE SHEET

	December 31,	
	2011	2010
ASSETS		
Cash and due from banks	\$ 1,004,609	\$ 1,489,049
Investment securities	363,789	433,540
Investment in subsidiaries	53,317,012	46,537,422
Other assets	1,651,431	1,918,170
TOTAL ASSETS	\$ 56,336,841	\$ 50,378,181
LIABILITIES		
Borrowings	\$ 12,686,000	\$ 14,236,000
Other liabilities	133,855	412,929
TOTAL LIABILITIES	12,819,855	14,648,929
STOCKHOLDERS' EQUITY	43,516,986	35,729,252
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 56,336,841	\$ 50,378,181

CONDENSED STATEMENT OF INCOME

	Year ended December 31,	
	2011	2010
INCOME		
Interest and dividend income	\$ 21,462	\$ 49,219
Investment securities gains (losses), net	10,517	(352,493)
Other income	52,715	52,863
Total income	84,694	(250,411)
EXPENSES		
Interest expense	818,873	661,489
Other expenses	274,540	250,153
Total expenses	1,093,413	911,642
Loss before tax benefit and equity in undistributed net income of subsidiaries	(1,008,719)	(1,162,053)
Income tax benefit	(341,246)	(402,194)
Equity in undistributed net income of subsidiaries	4,298,771	4,315,983
NET INCOME	\$ 3,631,298	\$ 3,556,124

19. PARENT COMPANY (Continued)

CONDENSED STATEMENT OF CASH FLOWS

	Year ended December 31,	
	2011	2010
OPERATING ACTIVITIES		
Net income	\$ 3,631,298	\$ 3,556,124
Adjustments to reconcile net income to net cash used for operating activities:		
Equity in undistributed net income of subsidiaries	(4,298,771)	(4,315,983)
Investment securities losses (gains), net	(10,517)	352,493
Other	232,650	72,359
Net cash used for operating activities	(445,340)	(335,007)
INVESTING ACTIVITIES		
Investment securities:		
Proceeds from sales	52,133	1,363,441
Advance to subsidiaries	(20,000)	-
Net cash provided by investing activities	32,133	1,363,441
FINANCING ACTIVITIES		
Increase (decrease) in short-term borrowings	(2,250,000)	1,000,000
Proceeds from other borrowings	700,000	1,300,000
Repayments of other borrowings	-	(120,464)
Proceeds from sale of common stock	3,176,897	-
Purchases of treasury stock	(23,227)	(197,150)
Proceeds from sale of treasury stock	85,590	85,886
Cash dividends	(1,760,493)	(1,739,714)
Net cash provided by (used for) financing activities	(71,233)	328,558
Increase (decrease) in cash and due from banks	(484,440)	1,356,992
CASH AND DUE FROM BANKS AT BEGINNING OF YEAR	1,489,049	132,057
CASH AND DUE FROM BANKS AT END OF YEAR	\$ 1,004,609	\$ 1,489,049

The People of Kish Bank

BOARD OF DIRECTORS OF KISH BANCORP, INC.

William P. Hayes, Chairman
James J. Lakso, Vice Chairman
William L. Dancy, Secretary
Richard L. Kalin, Member
Alison B. Kurtz, Member
Phyllis L. Palm, Member
Alan J. Metzler, Member
Delmont R. Sunderland, Member

BOARD OF DIRECTORS OF KISH BANK

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Richard L. Kalin, Member
Alison B. Kurtz, Member
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Alan J. Metzler, Member

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Harvard K. McCardle, Member
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Phyllis L. Palm, Member
John Pannizzo, Member

EXECUTIVE OFFICERS

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J. Bradley Scovill, Senior Executive Vice President and Chief Operating Officer
Michael F. Allen, Executive Vice President, Chief Credit Officer
John E. Arrington, Executive Vice President, Sales & Retail Banking Manager
Sangeeta Kishore, Executive Vice President, Chief Financial Officer
Robert S. McMinn, Executive Vice President, Financial Services and General Counsel
James L. Shilling, Jr., Executive Vice President, Senior Lending Officer

SENIOR OFFICERS

Amy M. Muchler, Senior Vice President, Operations and Branch Support Manager
Gerhard Royer, Senior Vice President, Commercial Lender
Ronald B. Beyer, CFA®, Vice President, Profitability & Investment Portfolio Manager
Kathleen M. Boop, Vice President, Personal Lines Insurance Manager
Larry E. Burger, Vice President, Commercial Relationship Manager
David A. Coble, Vice President, Branch Service Manager
John P. Cunningham, II, Vice President, Regional Market Manager
Wade E. Curry, LUTCF, Vice President, Investment Services
Ann K. Guss, Vice President, Consumer Lender
Allana L. Hartung, Vice President, Commercial Relationship Manager
Gregory T. Hayes, Vice President, Business Banker and Branch Service Manager
Carol M. Herrmann, Vice President for Administration
Christopher P. Kelly, Vice President, Information Technology Manager
Marsha K. Kuhns, Vice President, Branch Administration
John Q. Massie, Regional Vice President, Agricultural Manager

Scott R. Reigle, Vice President, Accounting and Controls Manager
Melissa K. Royer, Vice President, Operations Manager & Security Officer
Cheryl E. Shope, Vice President, Consumer Lender
Lana M. Walker, Vice President, Commercial Relationship Manager
Debra K. Weikel, Vice President, Mortgage Underwriter
Suzanne M. White, Vice President, Human Resource Manager
Jeffrey D. Wilson, Vice President, CEO, Kish Agency
William W. Yaudes, Vice President, Regional Market Manager

OFFICERS

Stanley N. Ayers, Assistant Vice President, Credit Administration Manager
Kimberly A. Bubb, Assistant Vice President, Product Development & Business Service Support Manager
Terra L. Decker, BSA/Fraud Manager
Lucinda K. Dell, Assistant Vice President, Assistant Mortgage Underwriter
Paul J. Fochler, Assistant Vice President, Risk Analyst
Carol K. Kennedy, Consumer Lending Officer
Jeremy G. Mattern, Assistant Vice President, Senior Credit Analyst
Peter K. Ort, Branch Manager
Matthew Q. Raptosh, Assistant Vice President, Commercial Loan Officer
Stephanie L. Strickler, CFMP, Assistant Vice President, Marketing Manager
N. Robert Sunday, III, Assistant Vice President, Compliance and Loan Review Officer
Kayelene Sunderland, Assistant Vice President, Wealth Management/Trust Administrator
D. Michael Whalen, General Manager, Travel Agency
Penny L. Zesiger, Assistant Vice President, Consumer Lender

KISH BANK EMPLOYEES

Natalie B. Allison, Business Banking Specialist
Tammy S. Anna, Customer Service Teller

Christina L. Bagrosky, Customer Service Teller
Barry L. Bargo, Courier/Mail Clerk
Katherine A. Bates, Personal Banker
Douglas C. Baxter, Accounting Specialist
Melissa D. Beale, Customer Service Teller
Sara M. Bean, Marketing and Communications Specialist
Stacy A. Boozel, Loan Operations Specialist
Brittany A. Byler, Customer Service Teller
Ruth H. Carper, Mortgage Administration Specialist
Stephanie L. Chilcote, Customer Service Teller
Ashley A. Clark, Personal Banker
Brenda Collins, Mortgage Administration Specialist
Alisha D. Cooper, Regional Personal Banker
Mary A. Cowher, Branch Manager
Richard D. Crider, ALCO & Reporting Manager
Jason M. Cunningham, Branch Manager
Maxi E. Curry, Administrative Assistant
Kati E. Deans, Credit Administration Specialist
Peggy J. Dearing, Credit Administration Specialist
Oksana F. DeArment, Executive Assistant to the CEO
Jannifer N. Diehl, Senior Credit Administration Specialist
Mary S. Dietz, Collections Manager
Megan D. Dietz, Investment Services Assistant
Angela D. Drake, Personal Banker
Brandi M. Dufford, Customer Service Teller
Amanda S. Dutrow, Administrative Assistant
Kathy D. Fisher, Branch Service Support Specialist
Keatyn M. Fletcher, Credit Administration Specialist
Alexis E. Fox, Regional Customer Service Teller
Troy J. Frank, Network Administrator
Jodie M. Gibboney, Personal Banker
Karen S. Gilbert, Business Banking Specialist

Beth N. Metz Gilmore, Human Resources Assistant
Janice Y. Glick, Personal Banking Specialist
Candee A. Gutshall, Branch Operations Specialist
Sharon A. Hall, Personal Banker
Lisa J. Hamler, Customer Service Teller
Jeffrey T. Hayes, Financial Advisor
Ashley L. Henry, Profitability Specialist
R. Michael Henry, Technical Support Specialist
Sallie M. Hicks, Branch Operations Specialist
Donald F. Hindman, Courier/Mail Clerk
Christina A. Hinkle, Business Banking Specialist
Evan S. Hodes, Customer Service Courier
Lara A. Hoffman, Regional Assistant Branch Manager
Sandra D. Hummel, Mortgage Administrative Assistant
Lauren M. Jeranka, Loan Documentation Review Manager
Karen M. Johnson, Trust Operations Specialist
Paula J. Kauffman, Senior Credit Administration Specialist
Michael S. Kearns, Data Analyst
John J. Keeler, Commercial Relationship Manager
Lisa A. Kennedy, Training & Development Manager
Brittany E. Kern, Business Service Support Specialist
Darla S. King, Branch Service Support Specialist
Abbey N. Knepp, Branch Service Support Specialist
Chelcee L. Kyle, Customer Service Teller
Carolyn M. Leacy, Customer Service Teller
Lori A. Legradi, Customer Service Teller
Michael J. Leidy, Personal Banker
Heidi C. Leonard, Consumer Lender
Carmella J. Long, Personal Banker
Tina K. McCurdy, Branch Operations Specialist

Kathryn A. McKnight, Collections Assistant
Kristie R. McKnight, Business Banker Trainee
Shelley V. Merrell, Customer Service Teller
Mary A. Miller, Executive Assistant
Joanna M. Minium, Credit Administration Specialist
Jennifer A. Mitchell, Mortgage Administration Specialist
Tina L. Nace, Senior Credit Administration Specialist
Antonietta M. Naimo, Personal Banker
Seth J. Napikoski, Credit Analyst
Stephanie J. Neff, Branch Service Support Specialist
Carol A. Noland, BSA Specialist
Melissa A. Paladino, Application Support Specialist
Constance F. Palm, Branch Manager
Anne E. Parks, Customer Service Teller
Susan K. Peachey, Branch Operations Specialist
Danielle A. Peck, Credit Administration Specialist
Christine M. Petroski, Branch Support Service Specialist
Susan C. Rainey, Customer Service Teller
Haley L. Ralston, Regional Personal Banker
Jesse L. Reed, Branch Operations Specialist
Amber N. Resto, Personal Banker
Denise M. Rothrock, Branch Operations Specialist
Billie A. Rupert, Investment Services Assistant
Krista M. Rupert, Customer Service Teller
Elise C. Santarelli, Credit Analyst
Leslie J. Sauer, Accounting Specialist
Clayton B. Scovill, Business Banking Representative
Melissa A. Sellers, Business Banking Specialist
April L. Shawver, Customer Service Teller
Glenn E. Snyder, Jr., Facilities Manager

Paula A. Stimeling, Mortgage Administration Specialist
Wendy S. Strohecker, Branch Service Support Manager
Crystal M. Sunderland, Business Service Support Specialist
Lisa M. Sunderland, Branch Service Support Specialist
Angela E. Swartzentruber, Personal Banker
Christopher E. Sweeney, Financial Planner
Cynthia G. Swineford, Customer Service Teller
Quinn L. Swineford, Branch Service Support Specialist
Patricia A. Trinclisti, Customer Service Teller
Donald L. Varner, Courier/Maintenance Supervisor
Jeanne L. Wagner, Customer Service Teller
Roy A. Wagner, Courier/Mail Clerk
Rebecca M. Watt, Senior Mortgage Administration Specialist
Elaine S. Weller, Branch Manager
Debra J. Wert, Business Banking Specialist
Rick W. Wert, Information Security Administrator
Crystal D. Yoder, Customer Service Teller
Delores K. Yoder, Business Banking Specialist
Judy A. Yoder, Customer Service Teller
Roland G. Yoder, Courier/Mail Clerk
Nancy A. Zimmerman, Personal Banker
Scott G. Zimmerman, Branch Operations Specialist

KISH INSURANCE EMPLOYEES

Jennifer R. Beachel, Systems and Operations Manager
Arlene M. Byler, Customer Service Rep/Support Assistant
Duane J. Coy, Commercial Lines Insurance Specialist
Megan S. Diemert, Personal Lines Insurance Specialist
Marlene K. Johnson, Personal Lines CSR
Amber E. Oborski, Personal Lines CSR

Gina K. Perrin, Personal Lines Insurance Specialist
Tracy S. Powell, Personal Lines CSR
Cindy J. Robinson, Commercial Lines CSR
J. Anthony Willard, Commercial Lines Insurance Specialist

KISH TRAVEL EMPLOYEES

Sandra K. Berardis, Travel Officer
Jolene Byler, Assistant Manager, Travel Consultant
Donna R. Feicke, Travel Office Assistant
Sandra L. Hunley, Lead Travel Agent



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