2015

Audited Financial Statements

Table of Contents

Index to Consolidated Financial Statements: Page

Independent Auditor's Report 1

Consolidated Balance Sheets 3

Consolidated Statements of Income 4

Consolidated Statements of Comprehensive Income 5

Consolidated Statements of Shareholders' Equity 6

Consolidated Statements of Cash Flows 7

Notes to Consolidated Financial Statements 8

Crowe Horwath.

Crowe Horwath LLP
Independent Member Crowe Horwath International

INDEPENDENT AUDITOR'S REPORT

Board of Directors and Shareholders
FNBH Bancorp, Inc.
Howell, Michigan

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of FNBH Bancorp, Inc., which comprise the consolidated balance sheet as of December 31, 2015, and the related consolidated statements of income, comprehensive income, shareholders' equity and cash flows for the year then ended, and the related notes to consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

(Continued)

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of FNBH Bancorp, Inc. as of December 31, 2015, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

The consolidated financial statements of FNBH Bancorp, Inc. as of December 31, 2014 and for the years ending December 31, 2014 and 2013, were audited by other auditors whose report dated March 31, 2015, expressed an unqualified opinion on those statements.

Crowe Horwath LLP

Grand Rapids, Michigan
May 18, 2016

FNBH Bancorp, Inc.
Consolidated Balance Sheets

	December 31, 2015	December 31, 2014
	(in thousands, except share amounts)	
Assets		
Cash and due from banks	$ 29,487	$ 26,138
Short term investments	198	198
Total cash and cash equivalents	29,685	26,336
Interest-bearing time deposits with other financial institutions	941	-
Investment securities:		
Investment securities available for sale, at fair value	141,522	132,175
FHLBI and FRB stock, at cost	1,065	1,140
Total investment securities	142,587	133,315
Loans held for investment:		
Commercial	134,419	132,382
Consumer	23,272	17,593
Real estate mortgage	13,135	10,071
Total loans held for investment	170,826	160,046
Less allowance for loan losses	(5,718)	(7,109)
Net loans held for investment	165,108	152,937
Premises and equipment, net	7,161	7,366
Other real estate owned, held for sale	971	1,174
Accrued interest receivable and other assets	1,716	1,698
Total assets	$ 348,169	$ 322,826
Liabilities and Shareholders' Equity		
Liabilities		
Deposits:		
Demand (non-interest bearing)	$ 114,414	$ 102,258
NOW	39,376	31,652
Savings and money market	98,370	88,247
Time deposits	60,906	68,222
Total deposits	313,066	290,379
Accrued interest payable and other liabilities	1,070	1,303
Total liabilities	314,136	291,682
Shareholders' Equity		
Preferred stock, no par value		
Series A - Authorized 10,000 shares; no shares issued and outstanding	-	-
Series B - Authorized 20,000 shares; no shares issued and outstanding		
Common stock, no par value. Authorized 40,000,000 shares at both December 31,	-	-
2015 and 2014; 27,770,423 shares issured and outstanding at December 31, 2015		
and 27,770,143 shares issued and outstanding at December 31, 2014	25,490	25,449
Retained earnings	8,934	5,528
Deferred directors' compensation	183	224
Accumulated other comprehensive loss	(574)	(57)
Total shareholders' equity	34,033	31,144
Total liabilities and shareholders' equity	$ 348,169	$ 322,826

See accompanying notes to consolidated financial statements.

FNBH BANCORP, INC.

Consolidated Statements of Income

	Year Ended December 31,		
	2015	2014	2013
	(in thousands, except per share and share amounts)		
Interest and dividend income:			
Interest and fees on loans	$ 7,882	$ 8,286	$ 9,311
Interest and dividends on investment securities:			
Taxable	2,368	1,905	1,094
Tax-exempt	33	43	47
Interest on time deposits with other financial institutions	10	-	-
Interest on short term investments and due from banks balances	8	5	3
Total interest and dividend income	10,301	10,239	10,455
Interest expense	550	703	925
Net interest income	9,751	9,536	9,530
Provision (credit) for loan losses	(2,250)	(2,500)	(2,250)
Net interest income after provison (credit) for loan losses	12,001	12,036	11,780
Noninterest income:			
Service charges and other fee income	2,213	2,280	2,585
Trust income	-	107	148
Net gain on investment securities available for sale	4	2	-
Net gain on sale/write-down of other real estate owned	66	123	91
Other	51	35	132
Total noninterest income	2,334	2,547	2,956
Noninterest expense:			
Salaries and employee benefits	5,722	6,041	5,369
Net occupancy expense	860	929	882
Equipment expense	335	350	344
Professional and service fees	1,382	1,611	1,753
Loan collection and foreclosed property expenses	229	208	327
Computer service fees	502	524	477
Computer software amortization expense	38	38	39
Director fees	108	-	-
FDIC assessment fees	436	528	1,026
Insurance	143	338	518
Printing and supplies	121	170	173
Advertising and marketing expenses	165	95	97
Other	826	681	653
Total noninterest expense	10,867	11,513	11,658
Income before income taxes	3,468	3,070	3,078
Income tax expense	62	20	104
Net income	$ 3,406	$ 3,050	$ 2,974
Per share statistics:			
Basic and diluted earnings per share	$ 0.12	$ 0.11	$ 1.57
Weighted-average common shares outstanding	27,771,678	17,498,168	457,435
Weighted-average common stock equivalent preferred shares outstanding, as converted	-	9,731,574	1,439,178
Total basic and diluted shares	27,771,678	27,229,742	1,896,613

See accompanying notes to consolidated financial statements.

FNBH BANCORP, INC.
Consolidated Statements of Comprehensive Income

	Year Ending December 31,		
	2015	2014	2013
		(in thousands)	
Net income	$ 3,406	$ 3,050	$ 2,974
Other comprehensive income (loss):			
Unrealized gains/losses on investment securities available for sale:			
Net unrealized holding gain (loss) during the period	(513)	1,500	(1,757)
Reclassification adjustment for net gain included in net income (presented in net gain on investment securities available for sale)	(4)	(2)	-
Total other comprehensive income (loss)	(517)	1,498	(1,757)
Comprehensive income	$ 2,889	$ 4,548	$ 1,217

See accompanying notes to consolidated financial statements.

FNBH BANCORP, INC.
Consolidated Statements of Shareholders' Equity

	Preferred Stock	Common Stock	Retained Earnings	Deferred Directors' Compensation	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
			(in thousands)			
Balances at January 1, 2013	$ -	$ 7,202	$ (496)	$ 461	$ 202	7,369
Issuance of preferred stock	16,520	-	-	-	-	16,520
Issued 784 shares for deferred directors' fees	-	119	-	(119)	-	-
Net income	-	-	2,974	-	-	2,974
Other comprehensive loss	-	-	-	-	(1,757)	(1,757)
Balances at December 31, 2013	16,520	7,321	2,478	342	(1,555)	25,106
Issued 772 shares for deferred directors' fees	-	118	-	(118)	-	-
Issuance of common stock	-	1,490	-	-	-	1,490
Preferred stock converted to common stock	(16,520)	16,520	-	-	-	-
Net income	-	-	3,050	-	-	3,050
Other comprehensive income	-	-	-	-	1,498	1,498
Balances at December 31, 2014	-	25,449	5,528	224	(57)	31,144
Issued 280 shares for deferred directors' fees	-	41	-	(41)	-	-
Net income	-	-	3,406	-	-	3,406
Other comprehensive loss	-	-	-	-	(517)	(517)
Balances at December 31, 2015	$ -	$ 25,490	$ 8,934	$ 183	$ (574)	$ 34,033

See accompanying notes to consolidated financial statements.

FNBH BANCORP, INC.
Consolidated Statements of Cash Flows

	Year Ended December 31,		
	2015	2014	2013
		(in thousands)	
Cash flows from operating activities:			
Net income	$ 3,406	$ 3,050	$ 2,974
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision (credit) for loan losses	(2,250)	(2,500)	(2,250)
Depreciation and amortization	481	479	454
Deferred income tax expense	-	-	104
Net amortization on investment securities available for sale	1,511	1,166	1,071
Net gain on investment securities available for sale	(4)	(2)	-
Net gain on sale/write-down of other real estate owned	(66)	(123)	(91)
Change in assets and liabilities:			
Accrued interest receivable and other assets	(73)	310	378
Accrued interest payable and other liabilities	(233)	(552)	183
Net cash provided by operating activities	2,772	1,828	2,823
Cash flows from investing activities			
Purchases of investment securities available for sale	(57,693)	(86,416)	(20,684)
Proceeds from sales of investment securities available for sale	12,703	202	-
Proceeds from maturities and calls of investment securities available for sale	8,600	3,350	3,000
Proceeds from principal paydowns on investment securities available for sale	25,019	18,703	19,658
Purchase of FRB stock	-	(479)	-
Proceeds from repurchase of FHLBI stock	75	118	-
Purchases of interest-bearing time deposits with other financial institutions	(941)	-	-
Proceeds from sale of other real estate owned	745	670	3,124
Loan originations and payments, net	(10,348)	4,223	14,685
Capital expenditures	(270)	(428)	(621)
Net cash provided by (used in) investing activities	(22,110)	(60,057)	19,162
Cash flows from financing activities:			
Net change in deposits	22,687	5,066	(2,369)
Common stock issued, net of offering costs	-	1,490	-
Preferred stock issued, net of offering costs	-	-	16,348
(Repayment of) proceeds from other borrowings	-	(16)	40
Net cash provided by financing activities	22,687	6,540	14,019
Net change in cash and cash equivalents	3,349	(51,689)	36,004
Cash and cash equivalents at beginning of year	26,336	78,025	42,021
Cash and cash equivalents at end of year	$ 29,685	$ 26,336	$ 78,025
Supplemental disclosures:			
Interest paid	$ 557	$ 727	$ 935
Loans transferred to other real estate owned	396	1,145	86
Loans charged off	121	474	1,205
Other borrowings exchanged for preferred stock	-	-	172
Cash paid for income taxes	61	10	-

See accompanying notes to consolidated financial statements.

FNBH Bancorp, Inc.
Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and the disclosures provided, and actual results could differ.

Principles of Consolidation
The consolidated financial statements include the accounts of FNBH Bancorp, Inc. and its wholly owned subsidiaries, First National Bank in Howell ("the Bank") and H.B. Realty Co. (herein collectively the "Corporation"). All significant intercompany balances and transactions have been eliminated in consolidation.

The Bank is a full-service bank offering a wide range of commercial and personal banking services. These services include checking accounts, savings accounts, certificates of deposit, commercial loans, real estate loans, installment loans, collections, night depository, safe deposit box, and wealth management services. The Bank serves primarily five communities – Howell, Brighton, Green Oak Township, Hartland, and Fowlerville – all of which are located in Livingston County, Michigan. The Bank is not dependent upon any single industry or business for its banking opportunities.

H.B. Realty Co. was established to purchase land for a future branch site of the Bank and to hold title to other Bank real estate when it is considered prudent to do so.

The accounting and reporting policies of the Corporation conform to accounting principles generally accepted in the United States of America and to general practice within the banking industry. The following is a description of the more significant of these policies.

(a) Cash and Cash Equivalents
Cash and cash equivalents include cash on hand, due from banks and short-term investments (securities with maturities equal to or less than 90 days and federal funds sold). Cash flows are reported net for customer loan and deposit transactions, interest-bearing time deposits with other financial institutions and short-term borrowings with maturities of 90 days or less, as applicable.

(b) Interest-Bearing Time Deposits with Other Financial Institutions
Interest-bearing time deposits with other financial institutions are recorded at cost and are federally insured. Reported balances at December 31, 2015 are scheduled to mature in 2020.

(c) Investment Securities
The Bank classifies debt and equity investments as follows:

Investment securities the Bank may not hold until maturity are accounted for as available for sale and are stated at fair value, with unrealized gains and losses reported as a separate component of other comprehensive income (loss) until realized. Fair value measurement for investment securities available for sale is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Interest income includes amortization or accretion of purchase premium or discount. Premiums and discounts are amortized or accreted using the level-yield method. Realized gains or losses on the sale of investment securities available for sale are recorded on the trade date and determined using the specific identification method.

Investment securities available for sale are reviewed quarterly for possible other-than-temporary impairment (OTTI). Management's evaluation considers various qualitative and quantitative factors regarding each investment category, including if investment securities were U.S. Government issued, the credit rating on the securities, credit outlook, payment status and financial condition, the length of time a security has been in a loss position, the size of the loss position and other meaningful information. In addition, with respect to the Corporation's non-government agency CMO security, management regularly completes a cash flow analysis with the assistance of a third party specialist. The analysis considers assumptions regarding voluntary prepayment speed, default rate, and loss severity using the CMO's original yield as the discount rate.

For debt securities, the Corporation distinguishes between the credit and noncredit components of an OTTI event. The credit component of an OTTI charge is the difference between the present value of the cash flows expected to be collected and the amortized cost basis of the debt security. If the Corporation does not intend to sell the security and it is more likely than not that the Corporation will not have to sell the security before the anticipated recovery of the remaining amortized cost basis, the credit component of the OTTI charge is recognized in earnings and the remaining noncredit portion is reported in other comprehensive income. If either of the above criteria is met, the entire difference between the amortized cost and fair value is recognized in earnings.

(d) Federal Home Loan Bank of Indianapolis and Federal Reserve Bank (FRB) Stock
The Bank is a member of the Federal Home Loan Bank System of Indianapolis ("FHLBI") and the Federal Reserve Bank ("FRB") and is required to invest in capital stock of the FHLBI and the FRB. The amount of required investment in the FHLBI is based on the level of borrowings and other factors, and the Bank may invest in additional amounts. FHLBI stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on the ultimate recovery of par value. The amount of the required investment in the FRB is determined by the FRB and is carried at cost based on the Bank's capital and surplus. Both cash and stock dividends on FHLBI and FRB stock are recorded in interest and dividends on investment securities on the consolidated statements of income.

(e) ***Loans Held for Investment***

Loans are classified within loans held for investment when management has the intent and ability to hold the loan for the foreseeable future, or until maturity or payoff. The foreseeable future is a management judgment which is determined based upon the type of loan, business strategies, current market conditions, balance sheet management and liquidity needs. Management's view of the foreseeable future may change based on changes in these conditions. When a decision is made to sell or securitize a loan that was not originated or initially acquired with the intent to sell or securitize, the loan is reclassified from loans held for investment into held for sale. Loans are classified as held for sale when management has the intent and ability to sell or securitize. Due to changing market conditions or other strategic initiatives, management's intent with respect to the disposition of the loan may change, and accordingly, loans previously classified as held for sale may be reclassified into loans held for investment. Loans transferred between loans held for sale and loans held for investment classifications are recorded at the lower of cost or market at the date of transfer.

Loans held for investment are carried at the principal amount outstanding net of unamortized purchase premiums or discounts, deferred loan origination fees and costs, the allowance for loan losses, and fair value adjustments, if any.

Interest income on loans is accrued daily based on the outstanding principal balance. In general, for each loan class, the accrual of interest income is discontinued when a loan becomes 90 days past due and the borrower's capacity to repay the loan and collateral values appear insufficient. However, loans may be placed on nonaccrual status regardless of whether or not such loans are considered past due if, in management's judgement, the borrower is unable to meet payment obligations as they become due or as required by regulatory provisions. All interest accrued but not received for all loans placed on nonaccrual is reversed from interest income. Delinquency status for all commercial and installment loans is based on the actual number of days past due as required by the contractual terms of the loan agreement.

Loan origination fees and certain direct loan origination costs are deferred and recognized as an adjustment of yield generally over the contractual life of the related loan. Net unamortized deferred loan fees amounted to $179,000 and $159,000 at December 31, 2015 and 2014, respectively.

(f) ***Allowance for Loan Losses and Credit Commitments***

Some loans will not be repaid in full. Therefore, an allowance for loan losses is established based on management's periodic evaluation of the loan portfolio and reflects an amount that, in management's judgement, is adequate to absorb probable incurred credit losses in the existing portfolio. In evaluating the portfolio, management takes into consideration numerous factors, including current economic conditions, prior loan loss experience, nonperforming loan levels, the composition of the loan portfolio, and management's evaluation of the collectability of specific loans, which includes analysis of the value of the underlying collateral or the present value of expected future cash flows. This overall evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. In addition, although management evaluates the adequacy of the allowance for loan losses based on information known to management at a given time, various regulatory agencies, based on the timing of their normal examination process, may require future additions to the allowance for loan losses.

The methodology for measuring the appropriate level of allowance and related provision (credit) for loan losses for each portfolio segment relies on several key elements, which include specific allowances for loans considered impaired and general allowances for non-impaired loans, based on our internal loan grading system. General allocations, based primarily on historical trends, are provided for homogeneous groups or classes of loans with similar risk characteristics.

Loss factors are determined based on either actual loss history or migration analysis, by portfolio class and loan grade, and adjusted for significant qualitative and environmental factors that, in management's judgement, affect the collectability of the portfolio at the analysis date. Migration analysis is used to determine loss factors for those portfolio classes containing a sufficient number and volume of loans (e.g., commercial, owner occupied, non-owner occupied, consumer home equity, residential mortgages and consumer loans) to generate loss rate information. For other portfolio classes, a rolling 12 quarter net loss history is used to compute historical loss experience, which may also be weighted to give emphasis to more recent quarters. However, in successive periods of either limited losses or net recoveries, look-back periods may be extended and/or current period weighting may be suspended to allow for inclusion of some representative estimate of probable credit losses to provide general allowance allocations.

In determining qualitative and environmental factor adjustments, especially in instances where current facts and circumstances have changed significantly enough to cause estimated credit losses to differ from historical loss experience, management considers both internal and external factors specific to each portfolio segment including, but not limited to, changes in lending policies and procedures, underwriting standards in effect when existing loans were originated, current economic conditions, and values for underlying collateral for collateral dependent loans, as examples.

Within each commercial portfolio segment, a general allowance allocation is assigned to non-impaired loans based on the internal risk grade and class of such loans, as primarily determined based on underlying collateral; and if real estate secured, the type of real estate. Each risk grade within a portfolio class is assigned a loss allocation factor, adjusted for qualitative and environmental factors, as deemed appropriate. The higher a risk grade, the greater the assigned loss allocation factor.

Groups of homogeneous noncommercial loans, such as mortgage - residential, home equity and home equity lines of credit, and consumer and other loans receive allowance allocations using loss rates determined by migration analysis, based on loan type rather than by risk grade. These allocations are adjusted for consideration of general economic and business conditions, credit quality and delinquency trends, collateral values, and recent loss experience for these similar pools of loans.

The Bank also maintains a reserve for losses on unfunded credit commitments and letters of credit to provide for the risk of loss inherent in these arrangements. The reserve is computed using the same methodology as that used to determine the allowance for loan losses. This reserve is reported as a liability on the consolidated balance sheets within accrued interest payable and other liabilities, while the corresponding provision for these losses is recorded in noninterest expense-other on the consolidated statements of income.

(g) *Nonperforming Assets*

Nonperforming assets are comprised of loans for which the accrual of interest has been discontinued, loans 90 days past due and still accruing, and other real estate owned, which has been acquired primarily through foreclosure and is awaiting disposition. Troubled debt restructured loans (TDRs) that are on accrual status and not past due 90 days or more are excluded from nonperforming loan totals.

Loans are generally placed on a nonaccrual status when principal or interest is past due 90 days or more and when, in the judgement of management, full collection of principal and interest is unlikely. At the time a loan is placed on nonaccrual status, interest previously accrued but not yet collected is charged against current interest income. Income on such loans is then recognized only to the extent that cash is received and where future collection of principal is probable. Payments on such loans are generally applied to the principal balance until qualifying to be returned to accrual status. Loans are considered for return to accrual status on an individual basis when interest and principal payments are current and future payments are reasonably assured.

TDRs represent loan modifications, including renewals, where concessions have been extended by the Bank due to financial difficulties experienced by the borrower. In addition, if the restructured loan is renewed at a market rate of interest and is structured consistent with normal lending practices, TDR classification may be removed. TDR loans may be considered for return to accrual status upon satisfaction of the timely, sustained performance requirements identified above and management's determination that future payments under the modified terms are reasonably assured.

The Bank considers a loan to be impaired when it is probable that it will be unable to collect all or part of amounts due according to the contractual terms of the loan agreement or the loan has been restructured and is classified as a troubled debt restructuring. Using an internal loan grading system, commercial purpose loans graded 7 and higher are individually evaluated for impairment if reported as nonaccrual and are greater than $100,000 or part of an aggregate relationship exceeding $100,000. Noncommercial purpose loans within the consumer real estate and consumer and other portfolio segments are subjected to impairment assessment upon certain triggering events such as delinquency, bankruptcy and restructuring, etc. Impairment is measured by comparing the Bank's recorded investment in the loan to the present value of expected future cash flows at the loan's effective interest rate, or, as a practical expedient, at the loan's observable market price, or the fair value of the collateral less costs to sell if the loan is collateral dependent. Interest income on impaired loans is accrued based on the principal amounts outstanding. The accrual of interest is generally discontinued when an impaired loan becomes 90 days past due.

All cash payments received on impaired nonaccrual loans are generally applied to the principal balance until qualifying to be returned to accrual status. Cash payments received on accruing impaired loans, including accruing TDRs are applied to principal and interest pursuant to the terms of the related loan agreement.

The Bank charges off all or part of loans when amounts are deemed to be uncollectible, although collection efforts may continue and future recoveries may occur. In general, when available information confirms that loans or portions thereof, other than collateral dependent loans, are uncollectible, such amounts are promptly charged-off against the allowance for loan losses. When an impaired loan is collateral dependent, any portion of the loan balance in excess of the fair value of the collateral (or fair value less cost to sell) is promptly charged-off against the allowance for loan losses.

(h) *Other Real Estate Owned*

Other real estate owned is recorded at the asset's estimated fair value, net of estimated disposal costs, at the time of foreclosure, establishing a new cost basis. Any write-downs at the time of foreclosure are charged to the allowance for loan losses. Expenses incurred in maintaining assets are recorded in loan collection and foreclosed property expenses on the consolidated statements of income. Any subsequent write-down to reflect a decline in fair value is recorded through a valuation allowance and a charge to net gain on sale/write-down of other real estate owned on the consolidated statements of income.

(i) *Transfer of Financial 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 Bank, (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 Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

(j) *Premises and Equipment*

Premises and equipment are stated at cost less accumulated depreciation. Depreciation, computed on the straight-line method, is recorded over the estimated useful lives of the assets. Estimated useful lives range up to 40 years for buildings, up to 7 years for furniture and equipment and up to 15 years for land improvements. Leasehold improvements are generally depreciated over the shorter of the respective lease term or estimated useful life.

Premises and equipment are evaluated periodically for impairment when events or changes in circumstances indicate the carrying amount may not be recoverable. Impairment exists when the expected undiscounted future cash flows of a long-lived asset are less than its carrying value. In that event, the Bank recognizes a loss for the difference between the carrying amount and the estimated fair value of the asset based on a quoted market price, if applicable, or a discounted cash flow analysis. Impairment losses on premises and equipment are recorded in noninterest expense-other on the consolidated statements of income.

(k) *Income Taxes*

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the consolidated financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

A valuation allowance, if needed, reduces deferred tax assets to the expected amount more likely than not that is to be realized. Realization of the Corporation's deferred tax assets is primarily dependent upon the generation of a sufficient level of future taxable income. At December

31, 2015 and 2014, management did not believe it was more likely than not that all of the deferred tax assets would be realized and, accordingly, recorded a valuation allowance of $8.7 million and $9.7 million at each respective year-end date.

In preparation of income tax returns, tax positions are taken based on interpretation of federal and state income tax laws for which the outcome is uncertain. Management reviews and evaluates the status of tax positions. There were no unrecognized tax benefits during 2015, 2014 or 2013. Interest or penalties related to unrecognized tax benefits would be recorded in income tax expense. The Corporation files U.S. federal income tax returns which are subject to final examination for all years after 2011.

(l) Stock-Based Compensation

The Corporation has one legacy stock-based compensation plan which is described more fully in Note 15.

(m) Loan Commitments and Related Financial Instruments

Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded. Financial instruments with off-balance risk are disclosed more fully in Note 16.

(n) Fair Value of Financial Instruments

Fair values of financial instruments are estimated using market information and other assumptions (as more fully described in Note 21) and involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, assumptions and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or market conditions could significantly affect such estimates.

(o) Common Stock Repurchases

The Corporation records common stock repurchases at cost. A portion of the repurchase is charged to common stock based on the average per share dollar amount of stock outstanding, multiplied by the number of shares repurchased, with the remainder charged to retained earnings. Shares repurchased are retired. No common stock repurchases were made by the Corporation during 2015, 2014, or 2013.

(p) Statement of Cash Flows

For purposes of reporting cash flows, cash equivalents include amounts due from banks, federal funds sold and short-term investments with original maturities of 90 days or less.

(q) Comprehensive Income

Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains and losses on investment securities available for sale which is also recognized as separate component of shareholders' equity.

(r) Earnings Per Common Share

Basic earnings per common share is calculated by dividing net income by the weighted average number of common shares and participating securities outstanding during the period. Diluted earnings per share is the same as basic earnings per share because any additional potential common shares currently issuable are included in the basic earnings per share calculation.

As explained more fully in Notes 13 and 14, for purposes of computing 2014 and 2013 basic and diluted earnings per share, while the Corporation's 17,510 shares of Mandatorily Convertible Non-Cumulative Junior Participating Preferred Stock, Series B (the "Series B Preferred Shares"), were outstanding (issued on December 11, 2013 and converted into common stock on May 22, 2014), they were considered a common stock equivalent and converted to common shares at a rate reflecting the conversion price per share of common stock of $0.70.

(s) Reclassifications

Certain reclassifications in the prior years' consolidated financial statements have been made to conform to the current year presentation. Reclassifications had no effect on prior year net income or total shareholders' equity.

2. Investment Securities Available for Sale

Investment securities available for sale consist of the following:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
		(in thousands)		
December 31, 2015				
Mortgage-backed/CMO - residential	$ 124,966	$ 179	$ (1,000)	$ 124,145
US agency	7,924	30	-	7,954
Obligations of state and political subdivisions	4,892	20	(13)	4,899
Corporate bonds	4,265	6	(19)	4,252
Preferred stock[1]	49	223	-	272
Total investment securities available for sale	$ 142,096	$ 458	$ (1,032)	$ 141,522
December 31, 2014				
Mortgage-backed/CMO - residential	$ 107,489	$ 409	$ (761)	$ 107,137
U.S. agency	23,108	28	(6)	23,130
Obligations of state and political subdivisions	1,586	19	-	1,605
Preferred stock[1]	49	254	-	303
Total investment securities available for sale	$ 132,232	$ 710	$ (767)	$ 132,175

[1] Represents preferred stocks issued by Freddie Mac and Fannie Mae

Securities are reviewed quarterly for possible other-than-temporary impairment (OTTI) based on guidance included in ASC Topic 320, *Investments–Debt and Equity Instruments*. This guidance requires an entity to assess whether it intends to sell, or whether it is more likely than not that it will be required to sell, a security in an unrealized loss position before the recovery of the security's amortized cost basis. If either of these criteria is met, the entire difference between the amortized cost and fair value is recognized in earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment recognized in earnings is limited to the amount related to credit losses, while impairment related to other factors is recognized in other comprehensive income.

Management's review of the securities portfolio for the existence of OTTI considers various qualitative and quantitative factors regarding each investment category, including if the securities were U.S. Government issued, the credit rating on the securities, credit outlook, payment status and financial condition, the length of time the security has been in a loss position, the size of the loss position and other meaningful information.

As of December 31, 2015, the Corporation's investment securities portfolio consisted of 99 securities, 54 of which were in an unrealized loss position.

At December 31, 2015, the Corporation held 43 mortgage-backed/CMO securities in an unrealized loss position, all of which were issued by Ginnie Mae, Fannie Mae or Freddie Mac which are U.S. government-sponsored agencies that the government has affirmed its commitment to support. Additionally, the Corporation held 4 obligations of state and political subdivision securities and 7 corporate bonds in an unrealized loss position. Because the decline in the market value is attributable to changes in interest rates and illiquidity, and not credit quality and because the Corporation does not have the intent to sell these securities and it is likely that it will not be required to sell the securities before their anticipated recovery, the Corporation does not consider these securities to be other than temporary impaired at December 31, 2015.

The Corporation makes a quarterly assessment of OTTI on its non-government agency collateralized mortgage obligation (CMO) security primarily based on a quarterly cash flow analysis performed by an independent third-party specialist. The evaluation includes a comparison of the present value of the expected cash flows to previous estimates to determine whether adverse changes in cash flows resulted during the period. The analysis considers attributes of the security, such as its super tranche position, and specific loan level collateral underlying the security. A summary of the par value, book value, carrying value (fair value) and unrealized loss for the security is presented below:

	December 31, 2015		**2014**	
	Amount	**% of Par**	**Amount**	**% of Par**
		(dollars in thousands)		
Par value	$ 1,054	100.00%	$ 1,269	100.00%
Book value	941	89.28%	1,129	88.97%
Carrying value	969	91.94%	1,195	94.17%
Unrealized loss	-	0.00%	-	0.00%

Certain key attributes of the underlying loans supporting the security included the following:

	December 31,	
	2015	2014
Weighted average remaining credit score (based on original FICO)	736	737
Primary location of underlying loans:		
California	71%	69%
Other	29%	31%
Delinquency status of underlying loans:		
Past due 30-59 days	3.53%	3.28%
Past due 60-89 days	0.00%	0.88%
Past due 90 days or more	2.04%	5.80%
In process of foreclosure	10.24%	7.30%
Held as other real estate owned	0.00%	0.89%

The specialist calculates an estimate of the fair value of the security's cash flows using an INTEX valuation model, subject to certain assumptions regarding collateral related cash flows such as expected prepayment rates, default rates, loss severity estimates, and discount rates as key valuation inputs.

	December 31,	
	2015	2014
Voluntary repayment rate (CRR)	11.90%	15.97%
Default rates:		
Within next 24 months	7.18%	7.77%
Decreasing to (by month 37)	3.41%	3.68%
Decreasing to (by month 188 at December 31, 2015 and by month 200 at December 31, 2014)	0.00%	0.00%
Loss severity rates:		
Initial loss upon default (Year 1)	43.50%	47.20%
Per annum decrease (Years 2 - 11)	3.50%	3.50%
Floor (Year 12)	23.00%	23.00%
Discount rate [(1)]:	6.00%	5.50%
Remaining credit support provided by other collateral pools of underlying loans within the security:	0.03%	0.04%

[(1)] Intended to reflect estimated uncertainty and liquidity premiums, after adjustment for estimated credit loss cash flows.

The prepayment assumptions used within the model consider borrowers' incentive to prepay based on market interest rates and borrowers' ability to prepay based on underlying assumptions for borrowers' ability to qualify for a new loan based on their credit and appraised property value, by location. As such, prepayment speeds decrease as credit quality and home prices deteriorate, reflecting a diminished ability to refinance.

In addition, collateral cash flow assumptions utilize a valuation technique under a "Liquidation Scenario" whereby loans are evaluated by delinquency and are assigned probability of default and loss factors deemed appropriate in the current economic environment. The liquidation scenarios assume that all loans 60 or more days past due migrate to default, are liquidated, and losses are realized over a period of between six and twenty four months based in part upon initial loan to value ratios and estimated changes in both historical and future property values since origination as obtained from financial data sources.

At December 31, 2015 and 2014, based on a present value at a prospective yield of future cash flows for the investment as provided by the specialist and after management's evaluation of the reasonableness of the specialist's underlying assumptions regarding Level 2 and Level 3 inputs, the Corporation concluded that the security's expected cash flows continued to support the amortized cost of the security and no additional other-than-temporary impairment had been incurred. Approximately $290,000 of cumulative credit-loss OTTI charges have been incurred on the security but none during 2015, 2014 and 2013, respectively.

The following is a summary of the gross unrealized losses and fair value of investment securities available for sale by length of time that individual securities have been in a continuous loss position:

	Less than 12 months		12 months or more		Total	
	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
			(in thousands)			
December 31, 2015						
Mortgage-backed/CMO - residential	$ (440)	$ 64,802	$ (560)	$ 25,840	$ (1,000)	$ 90,642
Obligations of state and political subdivisions	(13)	1,532	-	-	(13)	1,532
Corporate bonds	(19)	3,678	-	-	(19)	3,678
Total	$ (472)	$ 70,012	$ (560)	$ 25,840	$ (1,032)	$ 95,852
December 31, 2014						
Mortgage-backed/CMO - residential	$ (185)	$ 28,453	$ (576)	$ 22,141	$ (761)	$ 50,594
Obligations of state and political subdivisions	(6)	4,687	-	-	(6)	4,687
Total	$ (191)	$ 33,140	$ (576)	$ 22,141	$ (767)	$ 55,281

The amortized cost and fair value of investment securities available for sale, by contractual maturity, follow. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	December 31, 2015		December 31, 2014	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
		(in thousands)		
Maturing within one year	$ -	$ -	$ 4,276	$ 4,278
Maturing after one year but within five years	12,120	12,125	17,587	17,606
Maturing after five years but within ten years	4,436	4,448	2,305	2,312
Maturing after ten years	574	804	575	842
	$ 17,130	$ 17,377	$ 24,743	$ 25,038
Mortgage-backed/CMO securities - residential	124,966	124,145	107,489	107,137
Total	$ 142,096	$ 141,522	$ 132,232	$ 132,175

Proceeds from sales and calls of investment securities available for sale and the associated gains and losses are as follows:

	2015	2014	2013
		(in thousands)	
Proceeds	$ 21,053	$ 3,522	$ 3,000
Gross gains	8	2	-
Gross losses	(4)	-	-

At December 31, 2015 and 2014, the Corporation did not own any investment securities issued by states and political subdivisions in which the amortized cost and fair value of such securities individually exceeded 10% of shareholders' equity.

Investment securities, with an amortized cost of approximately $47.5 million at December 31, 2015 were pledged to secure public deposits and for other purposes required or permitted by law, including approximately $14.4 million of securities pledged as collateral at the Federal Home Loan Bank of Indianapolis (FHLBI) to support potential liquidity needs of the Bank. At December 31, 2014, the amortized cost of pledged investment securities totaled $53.0 million of which $19.7 million of securities were pledged as collateral at the FHLBI for contingent liquidity needs of the Bank.

The Bank owns stock in both the Federal Home Loan Bank of Indianapolis (FHLBI) and the Federal Reserve Bank (FRB), both of which are recorded at cost. The Bank is required to hold stock in the FHLBI equal to 5% of the institution's borrowing capacity with the FHLBI. The Bank's investment in FHLBI stock amounted to $542,000 at December 31, 2015 and $617,000 at December 31, 2014. The Bank's investment in FRB stock, which totaled $523,000 at December 31, 2015 and December 31, 2014, is a requirement for the Bank's membership in the Federal Reserve System. These investments can only be resold to, or redeemed by, the issuer. In May 2015, the FHLBI repurchased $75,000 of its stock resulting in no gain or loss to the Bank.

3. Loans Held for Investment

Loans held for investment consists of the following:

	December 31, 2015	December 31, 2014
	(in thousands)	
Commercial	$ 14,413	$ 15,130
Commercial real estate:		
Construction, land development, and other land	4,678	5,050
Owner occupied	49,949	47,434
Nonowner occupied	58,604	59,440
Consumer real estate:		
Commercial purpose	6,931	5,463
Mortgage - residential	15,154	11,631
Home equity and home equity lines of credit	13,084	9,613
Consumer and other	8,192	6,444
Subtotal	171,005	160,205
Net deferred fees	(179)	(159)
Total loans held for investment	$ 170,826	$ 160,046

Included in the consumer real estate loans above are residential first mortgages reported as "real estate mortgages" on the consolidated balance sheets. In addition, a portion of these consumer real estate loans include commercial purpose loans where the borrower has pledged a 1-4 family residential property as collateral. Loans also include the reclassification of demand deposit overdrafts, which amounted to $60,000 and $59,000 at December 31, 2015 and 2014, respectively.

Loans serviced for others, including commercial participations sold, are not reported as assets of the Bank and approximated $1.4 million at December 31, 2015 and $1.5 million at December 31, 2014.

4. Allowance for Loan Losses and Credit Quality of Loans

The Corporation separates its loan portfolio into segments to perform the calculation and analysis of the allowance for loan losses. The four portfolio segments analyzed are Commercial, Commercial Real Estate, Consumer Real Estate, and Consumer and Other. The Commercial portfolio segment includes loans to finance commercial and industrial businesses that are not secured by real estate. The Commercial Real Estate portfolio segment includes: i) construction real estate loans to finance construction and land development and/or loans secured by vacant land and ii) commercial real estate loans secured by non-farm, non-residential real estate which are further classified as either owner occupied or non-owner occupied based on the underlying collateral type. The Consumer Real Estate portfolio segment includes (commercial and non-commercial purpose) loans that are secured by 1 – 4 family residential real estate properties, including first mortgages on residential properties and home equity loans and lines of credit that are secured by first or second liens on residential properties. The Consumer and Other portfolio segment includes all loans not included in any other segment. These are primarily loans to consumers for household, family, and other personal expenditures, such as autos, boats, and recreational vehicles.

Activity in the allowance for loan losses by portfolio segment is a follows:

	Commercial	Commercial Real Estate	Consumer Real Estate	Consumer and Other	Total
			(in thousands)		
2015					
Allowance for loan losses:					
Beginning balance	$ 415	$ 5,371	$ 1,084	$ 239	$ 7,109
Charge offs	-	-	(22)	(99)	(121)
Recoveries	288	367	239	86	980
Provision (credit)	(364)	(2,394)	150	358	(2,250)
Ending balance	$ 339	$ 3,344	$ 1,451	$ 584	$ 5,718
2014					
Allowance for loan losses:					
Beginning balance	$ 633	$ 7,180	$ 1,215	$ 183	$ 9,214
Charge offs	(95)	(127)	(170)	(82)	(474)
Recoveries	147	334	316	72	869
Provision (credit)	(270)	(2,016)	(277)	63	(2,500)
Ending balance	$ 415	$ 5,371	$ 1,084	$ 236	$ 7,109

	Commercial	Commercial Real Estate	Consumer Real Estate	Consumer and Other	Total
			(in thousands)		
2013					
Allowance for loan losses:					
Beginning balance	$ 908	$ 8,682	$ 2,036	$ 143	$ 11,769
Charge offs	(177)	(836)	(87)	(105)	(1,205)
Recoveries	212	224	363	101	900
Provision (credit)	(310)	(890)	(1,097)	47	(2,250)
Ending balance	$ 633	$ 7,180	$ 1,215	$ 186	$ 9,214

The following presents the balance in allowance for loan losses and loan balances by portfolio segment based on impairment method:

	Commercial	**Commercial Real Estate**	**Consumer Real Estate**	**Consumer and Other**	**Total**
			(in thousands)		
December 31, 2015					
Allowance for loan losses:					
Individually evaluated for impairment	$ -	$ 201	$ -	$ -	$ 201
Collectively evaluated for impairment	339	3,143	1,451	584	5,517
Total allowance for loan losses	$ 339	$ 3,344	$ 1,451	$ 584	$ 5,718
Recorded investment in loans:					
Individually evaluated for impairment	$ 55	$ 6,078	$ 133	$ -	$ 6,266
Collectively evaluated for impairment	14,358	107,153	35,036	8,192	164,739
Total recorded investment in loans	$ 14,413	$ 113,231	$ 35,169	$ 8,192	$ 171,005
December 31, 2014					
Allowance for loan losses:					
Individually evaluated for impairment	$ 1	$ 1,681	$ 5	$ -	$ 1,687
Collectively evaluated for impairment	414	3,690	1,079	239	5,422
Total allowance for loan losses	$ 415	$ 5,371	$ 1,084	$ 239	$ 7,109
Recorded investment in loans:					
Individually evaluated for impairment	$ 234	$ 11,324	$ 1,014	$ -	$ 12,572
Collectively evaluated for impairment	14,896	100,600	25,693	6,444	147,633
Total recorded investment in loans	$ 15,130	$ 111,924	$ 26,707	$ 6,444	$ 160,205

Management's on-going monitoring of the credit quality of the portfolio relies on an extensive credit risk monitoring process that considers several factors including: current economic conditions affecting the Bank's customers, the payment performance of individual loans and pools of homogenous loans, portfolio seasoning, changes in collateral values, and detailed reviews of specific relationships.

Our internal loan grading system assigns a risk grade to all commercial, commercial real estate, and consumer real estate - commercial purpose loans. This grading system is similar to those employed by banking regulators. Grades 1 through 5 are considered "pass" credits and grade 6 are considered "watch" credits and are subject to greater scrutiny. Those loans graded 7 and higher are considered substandard and are individually evaluated for impairment if reported as nonaccrual and are greater than $100,000 or part of an aggregate relationship exceeding $100,000. All commercial loans are graded at inception and reviewed, and if appropriate, re-graded at various intervals thereafter. Additionally, our commercial loan portfolio and assigned risk grades are periodically subjected to review by external loan reviewers and banking regulators. Certain of the key factors considered in assigning loan grades include: cash flows, operating performance, financial condition, collateral, industry condition, management, and the strength, liquidity and willingness of guarantors' support.

A description of the general characteristics of each risk grade follows:

- **RATING 1 (Satisfactory – Minimal Risk)** - Loans in this category are to persons or entities of unquestioned financial strength, a highly liquid financial position, with collateral that is liquid and well margined. These borrowers have performed without question on past obligations, and the Bank expects their performance to continue. Internally generated cash flow covers current maturities of long-term debt by a substantial margin.
- **RATING 2 (Satisfactory – Modest Risk)** – These loans to persons or entities with strong financial condition and above-average liquidity who have previously satisfactorily handled their obligations with the Bank. Collateral securing the Bank's debt is margined in accordance with policy guidelines. Internally generated cash flow covers current maturities of long-term debt more than adequately.

- **RATING 3 (Satisfactory - Average)** – These are loans with average cash flow and ratios compared to peers. Usually RMA comparisons show where companies fall in the performance spectrum. Companies have consistent performance for 3 or more years.
- **RATING 4 (Satisfactory – Acceptable Risk)** – Loans to persons or entities with an average financial condition, adequate collateral margins, adequate cash flow to service long-term debt, and net worth comprised mainly of fixed assets are included in this category. These entities are minimally profitable now, with projections indicating continued profitability into the foreseeable future. Overall, these loans are basically sound.
- **RATING 5 (Satisfactory - Acceptable – Monitor) -** These loans are characterized by borrowers who have marginal, but adequate cash flow, marginal profitability, but currently have been meeting the obligations of their loan structure. However, adverse changes in the borrower's circumstances and/ or current economic conditions are more likely to impair their capacity for repayment. The borrower has in the past satisfactorily handled debts with the Bank, but may be experiencing some minor delinquency in making payments, or other signs of temporary cash flow issues. Borrower may be experiencing declining margins or other negative financial trends, despite the borrower's continued satisfactory condition and positive cash flow. Other characteristics of borrowers in this class include inadequate credit information, weakness of financial statements, or declining but positive repayment capacity. This classification includes loans to new or established borrowers with satisfactory loan structure, but where near term economic or business issues appears to remain stable and the near term projections would limit the ability for an improvement in the financial trends of the borrower.
- **RATING 6 (Special Mention - OAEM) -** Loans in this class have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the Bank's credit position at some future date. These potential weaknesses may result in a deterioration of the repayment of the loan and increase the credit risk. Special mention assets are not adversely classified and do not expose the Bank to sufficient risk to warrant adverse classification. Special mention credits may include a borrower that pays the Bank on a timely basis (occasional 30 day delinquent) and may be experiencing temporary cash flow deficiencies.
- **RATING 7 (Substandard) –** A substandard loan is inadequately protected by the current net worth and paying capacity of the borrower or of the collateral pledged, if any. Loans so classified must have a well-defined weakness, or weaknesses, that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard loans, does not have to exist in individual loans. Substandard credits may include a borrower that pays consistently past due, has significant cash flow shortages and may have a collateral shortfall that requires a specific reserve.
- **RATING 8 (Doubtful) -** This risk rating class has all of the weaknesses inherent in the substandard rating but with the added characteristic that the weaknesses make collection in full or liquidation, on the basis of currently known existing facts, condition, and values, highly questionable and improbable. These are poor quality loans in which neither the collateral, if any, nor the financial condition of the borrower presently ensure collectability in full within a reasonable period of time; in fact, there is permanent impairment in the collateral securing the Bank's loan. These loans are in a work-out status, are on non-accrual status and have a defined work-out strategy.

  This is a transitional risk rating class while collateral value and other factors are assessed. Loans will remain in this class for the assessment period, but in no event for more than 1 year. If there is no improvement in the Bank's position during that time, a charge-off will be taken to best reflect known asset collateral value. If the loan goes into a "Deeds in Redemption" status before 1 year, any shortfall will be charged-off immediately.

The assessment of compensating factors may result in a rating plus or minus one grade from those listed above. These factors include, but are not limited to collateral, guarantors, environmental conditions, history, plan/projection reasonableness, quality of information, and payment delinquency.

The internal loan grading system is applied to the residential real estate portion of our consumer loan portfolio upon certain triggering events (e.g., delinquency, bankruptcy, restructuring, etc.). However, large groups of smaller balance homogeneous loans, such as mortgage – residential, home equity and home equity lines of credit and consumer and other are collectively evaluated for impairment and are not separately identified for impairment disclosures. The primary risk element for these classes of loans is the timeliness of borrowers' scheduled payments. We rely primarily on our internal reporting system to monitor past due loans and have internal policies and procedures to pursue collection and protect our collateral interests in order to mitigate losses.

Our monitoring of credit quality is further denoted by classification of loans as nonperforming, which reflects loans where the accrual of interest has been discontinued and loans that are past due 90 days or more and still accruing interest. Nonperforming loans include troubled debt restructured loans (as discussed below) that are on nonaccrual status or past due 90 days or more. Troubled debt restructured loans that are accruing interest and not past due 90 days or more are excluded from nonperforming loans.

The following presents the recorded investment in loans by risk grade and a summary of nonperforming loans, by class of loan:

	Not Rated	1	2	3	4	5	6	7	8	Total	Nonperforming
						(in thousands)					
December 31, 2015											
Commercial	$ 57	$ 630	$ 41	$ 2,399	$ 5,027	$ 6,188	$ 6	$ 65	$ -	$ 14,413	$ 62
Commercial real estate:											
Construction, land development, and other land	-	-	-	-	598	2,229	234	1,617	-	4,678	1,617
Owner occupied	-	-	368	1,751	26,426	19,962	858	584	-	49,949	584
Nonowner occupied	-	-	3,160	3,797	22,552	26,097	1,829	1,169	-	58,604	1,000
Consumer real estate:											
Commercial purpose	-	-	-	49	1,769	4,530	375	208	-	6,931	208
Mortgage - residential	9,188	-	-	-	-	4,208	-	1,758	-	15,154	1,642
Home equity and home equity lines of credit	12,176	-	-	-	-	631	-	277	-	13,084	277
Consumer and other	7,848	10	-	-	-	260	-	74	-	8,192	74
Total	$ 29,269	$ 640	$ 3,569	$ 7,996	$ 56,372	$ 64,105	$ 3,302	$ 5,752	$ -	$ 171,005	$ 5,464

	Not Rated	1	2	3	4	5	6	7	8	Total	Nonperforming
						(in thousands)					
December 31, 2014											
Commercial	$ -	$ 239	$ 44	$ 3,294	$ 4,959	$ 6,139	$ 194	$ 261	$ -	$ 15,130	$ 233
Commercial real estate:											
Construction, land development, and other land	-	-	-	-	1,072	1,796	377	366	1,439	5,050	1,740
Owner occupied	-	-	415	4,949	23,632	15,906	496	2,036	-	47,434	965
Nonowner occupied	-	-	337	4,035	20,287	27,741	4,685	2,355	-	59,440	2,148
Consumer real estate:											
Commercial purpose	-	-	-	55	1,172	2,575	654	1,007	-	5,463	517
Mortgage - residential	4,589	-	-	-	-	4,381	-	2,661	-	11,631	2,497
Home equity and home equity lines of credit	8,314	-	-	-	-	986	-	313	-	9,613	137
Consumer and other	6,038	-	-	-	-	285	-	121	-	6,444	71
Total	$ 18,941	$ 239	$ 796	$ 12,333	$ 51,122	$ 59,809	$ 6,406	$ 9,120	$ 1,439	$ 160,205	$ 8,308

The recorded investment in loans excludes accrued interest receivable and net deferred fees due to immateriality.

Loans are considered past due when contractually required principal or interest has not been received. The amount classified as past due is the entire principal balance outstanding of the loan, not just the amount of payments that are past due.

An aging analysis of the recorded investment in past due loans, segregated by class of loans follows:

	Loans Past Due						90+ Days Past Due and Accruing
	30-59 Days	60-89 Days	90+ Days	Total	Current	Total	
				(in thousands)			
December 31, 2015							
Commercial	$ 18	$ -	$ -	$ 18	$ 14,395	$ 14,413	$ -
Commercial real estate:							
Construction, land development, and other land	-	-	47	47	4,631	4,678	-
Owner occupied	227	-	-	227	49,722	49,949	-
Nonowner occupied	-	-	62	62	58,542	58,604	-
Consumer real estate:							
Commercial purpose	95	-	-	95	6,836	6,931	-
Mortgage - residential	3,607	291	199	4,097	11,057	15,154	-
Home equity and home equity lines of credit	66	-	2	68	13,016	13,084	-
Consumer and other	71	32	-	103	8,089	8,192	-
Total	$ 4,084	$ 323	$ 310	$ 4,717	$ 166,288	$ 171,005	$ -

	Loans Past Due						90+ Days Past Due and
	30-59 Days	60-89 Days	90+ Days	Total	Current	Total	Accruing
				(in thousands)			
December 31, 2014							
Commercial	$ -	$ -	$ -	$ -	$ 15,130	$ 15,130	$ -
Commercial real estate:							
Construction, land development, and other land	-	105	43	148	4,902	5,050	-
Owner occupied	24	-	20	44	47,390	47,434	-
Nonowner occupied	174	-	97	271	59,169	59,440	-
Consumer real estate:							
Commercial purpose	-	112	191	303	5,160	5,463	-
Mortgage - residential	868	521	375	1,764	9,867	11,631	4
Home equity and home equity lines of credit	2	-	-	2	9,611	9,613	-
Consumer and other	33	6	-	39	6,405	6,444	-
Total	$ 1,101	$ 744	$ 726	$ 2,571	$ 157,634	$ 160,205	$ 4

The recorded investment in loans excludes accrued interest receivable and net deferred fees due to immateriality.

Loans are placed on nonaccrual when, in the judgement of management, the collection of additional interest is doubtful. Loans are generally placed on nonaccrual upon becoming 90 days past due. However, loans may be placed on nonaccrual regardless of whether or not they are past due. All cash received on nonaccrual loans is applied to the principal balance. Loans are considered for return to accrual status on an individual basis when all principal and interest amounts contractually due are brought and future payments reasonably assured.

The following is a summary of the recorded investment in nonaccrual loans, by class of loan:

	December 31, 2015	December 31, 2014
	(in thousands)	
Commercial	$ 62	$ 233
Commercial real estate:		
Construction, land development, and other land	1,617	1,692
Owner occupied	584	965
Nonowner occupied	1,000	2,148
Consumer real estate:		
Commercial purpose	208	517
Mortgage - residential	1,642	2,497
Home equity and home equity lines of credit	277	137
Consumer and other	74	119
Total	$ 5,464	$ 8,308

The recorded investment in loans excludes accrued interest receivable and net deferred fees due to immateriality.

The following presents information pertaining to impaired loans and related valuation allowance allocations by class of loan:

	December 31, 2015			December 31, 2014		
	Recorded Investment	Unpaid Principal Balance	Valuation Allowance	Recorded Investment	Unpaid Principal Balance	Valuation Allowance
	(in thousands)					
With an allowance recorded:						
Commercial	$ -	$ -	$ -	$ 30	$ 32	$ 1
Commercial real estate:						
Construction, land development, and other land	1,969	4,298	191	2,144	4,411	1,567
Owner occupied	1,095	1,095	10	1,182	1,483	111
Nonowner occupied	-	-	-	97	104	4
Consumer real estate:						
Commercial purpose	-	-	-	94	100	4
Mortgage - residential	-	-	-	-	-	-
Home equity and home equity lines of credit	-	-	-	-	-	-
Consumer and other	-	-	-	-	-	-
Total	3,064	5,393	201	3,547	6,130	1,687
With no related allowance recorded:						
Commercial	55	63	-	203	209	-
Commercial real estate:						
Construction, land development, and other land	263	361	-	317	451	-
Owner occupied	1,032	1,206	-	1,368	1,605	-
Nonowner occupied	1,719	1,962	-	6,216	6,673	-
Consumer real estate:						
Commercial purpose	133	194	-	921	1,024	-
Mortgage - residential	-	-	-	-	-	-
Home equity and home equity lines of credit	-	-	-	-	-	-
Consumer and other	-	-	-	-	-	-
Total	3,202	3,786	-	9,025	9,962	-
Total:						
Commercial	55	63	-	233	241	1
Commercial real estate:						
Construction, land development, and other land	2,232	4,659	191	2,461	4,862	1,567
Owner occupied	2,127	2,301	10	2,550	3,088	111
Nonowner occupied	1,719	1,962	-	6,313	6,777	4
Consumer real estate:						
Commercial purpose	133	194	-	1,015	1,124	4
Mortgage - residential	-	-	-	-	-	-
Home equity and home equity lines of credit	-	-	-	-	-	-
Consumer and other	-	-	-	-	-	-
Total impaired loans	$ 6,266	$ 9,179	$ 201	$ 12,572	$ 16,092	$ 1,687

The recorded investment in loans excludes accrued interest receivable and net deferred fees due to immateriality.

The following presents information pertaining to the recorded investment in impaired loans as follows:

	December 31, 2015		December 31, 2014		December 31, 2013	
	Average Outstanding Balance	Interest Income Recognized	Average Outstanding Balance	Interest Income Recognized	Average Outstanding Balance	Interest Income Recognized
	(in thousands)					
Commercial	$ 67	$ 9	$ 256	$ 2	$ 230	$ 15
Commercial real estate:						
Construction, land development, and other land	2,294	148	2,522	41	2,925	64
Owner occupied	2,111	215	2,658	164	7,005	318
Nonowner occupied	1,774	203	6,374	243	8,415	314
Consumer real estate:						
Commercial purpose	-	-	878	46	1,947	74
Mortgage - residential	143	35	-	-	-	-
Home equity and home equity lines of credit	-	3	113	-	-	-
Consumer and other	-	-	-	-	-	-
Total	$ 6,389	$ 613	$ 12,801	$ 496	$ 20,522	$ 785

The recorded investment in loans excludes accrued interest receivable and net deferred fees due to immateriality.

For loans where impairment is measured based on the present value of expected future cash flows, subsequent changes in present value and related allowance adjustments resulting from the passage of time are accounted for within the provision (credit) for loan losses rather than interest income.

Troubled Debt Restructurings

The Corporation may agree to modify the terms of a loan to improve its ability to collect amounts due. The modified terms are intended to enable customers to mitigate the risk of foreclosure by creating a payment structure that provides for continued loan payment requirements based on their current cash flow ability. Modifications, including renewals, where concessions are made by the Bank and result from the debtor's financial difficulties are considered troubled debt restructurings (TDRs).

Loan modifications are considered TDRs when the modification includes terms outside of normal lending practices (i.e., concessions) to a borrower who is experiencing financial difficulties.

Typical concessions granted include, but are not limited to:

1. Agreeing to interest rates below prevailing market rates for debt with similar risk characteristics
2. Extending the amortization period beyond typical lending guidelines for debt with similar risk characteristics
3. Forbearance of principal
4. Forbearance of accrued interest

To determine if a borrower is experiencing financial difficulties, the Corporation considers if:

1. The borrower is currently in default on any other of their debt
2. It is likely that the borrower would default on any of their debt if the concession was not granted
3. The borrower's cash flow was sufficient to service all of their debt if the concession was not granted
4. The borrower has declared, or is in the process of declaring bankruptcy
5. The borrower is a going concern (if the entity is a business)

The following summarizes troubled debt restructurings:

	December 31, 2015			December 31, 2014		
	Outstanding Recorded Investment			Outstanding Recorded Investment		
	Accruing	Nonaccrual	Total	Accruing	Nonaccrual	Total
	(in thousands)					
Commercial	$ -	$ 36	$ 36	$ -	$ 104	$ 104
Commercial real estate:						
Construction, land development, and other land	687	1,570	2,257	769	1,512	2,281
Owner occupied	1,598	432	2,030	1,586	907	2,493
Nonowner occupied	963	852	1,815	4,165	566	4,731
Consumer real estate:						
Commercial purpose	-	133	133	497	153	650
Mortgage - residential	797	768	1,565	808	1,002	1,810
Home equity and home equity lines of credit	50	4	54	54	8	62
Consumer and other	2	4	6	5	37	42
Total	$ 4,097	$ 3,799	$ 7,896	$ 7,884	$ 4,289	$ 12,173

Troubled debt restructured loans may qualify for return to accrual status if the borrower complies with the revised terms and conditions and has demonstrated sustained payment performance consistent with the modified terms for a minimum of six consecutive payment cycles after the restructuring date. In addition, the collection of future payments must be reasonably assured.

The following presents information regarding existing loans that were restructured, resulting in the loan being classified as a troubled debt restructuring:

	Loans Restructured in 2015			Loans Restructured in 2014		
	Number of Loans	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Number of Loans	Pre-Modification Recorded Investment	Post-Modification Recorded Investment
	(dollars in thousands)					
Commercial	1	$ 14	$ 14	-	$ -	$ -
Commercial real estate:						
Construction, land development, and other land	-	-	-	1	43	43
Owner occupied	-	-	-	3	237	237
Nonowner occupied	2	122	122	2	500	500
Consumer real estate:						
Commercial purpose	-	-	-	2	170	170
Mortgage - residential	1	15	15	1	62	62
Home equity and home equity lines of credit	1	64	64	-	-	-
Consumer and other	-	-	-	1	25	25
Total	5	$ 215	$ 215	10	$ 1,037	$ 1,037

During the year ended December 31, 2015, the Corporation had three troubled debt restructured loans with a recorded investment of $118,000 that defaulted within 12 months of restructuring. During the year ended December 31, 2014, the Corporation had five troubled debt restructured loans with a recorded investment of $242,000 that defaulted within 12 months of restructuring. A loan is considered to be in payment default generally once it is 90 days contractually past due under the modified terms. These payment defaults on troubled debt restructured loans had an immaterial impact on the allowance for loan losses and resulted in an immaterial amount of charge offs during the years ended December 31, 2015 and 2014, respectively.

The following summarizes the nature of concessions granted by the Corporation to borrowers experiencing financial difficulties which resulted in troubled debt restructurings:

	Non-Market Interest Rate		Extension of Amortization Period	
	Number of Loans	Pre-Modification Recorded Investment	Number of Loans	Pre-Modification Recorded Investment
	(dollars in thousands)			
December 31, 2015				
Commercial	-	$ -	1	$ 14
Commercial real estate:				
Construction, land development, and other land	-	-	-	-
Owner occupied	-	-	-	-
Nonowner occupied	-	-	2	122
Consumer real estate:				
Commercial purpose	-	-	-	-
Mortgage - residential	-	-	1	15
Home equity and home equity lines of credit	-	-	1	64
Consumer and other	-	-	-	-
Total	-	$ -	5	$ 215
December 31, 2014				
Commercial	-	$ -	-	$ -
Commercial real estate:				
Construction, land development, and other land	-	-	1	43
Owner occupied	-	-	3	237
Nonowner occupied	-	-	2	500
Consumer real estate:				
Commercial purpose	-	-	2	170
Mortgage - residential	1	62	-	-
Home equity and home equity lines of credit	-	-	-	-
Consumer and other	-	-	1	25
Total	1	$ 62	9	$ 975

During the year ended December 31, 2014, non-market interest rate restructurings included pre-modification recorded investments of $62,000 related to performing loans that were renewed at either their existing contractual rates or non-market interest rates. Because these performing loans were graded substandard and the modified rates were not market rates for similar loans, these renewals are considered troubled debt restructurings. The troubled debt restructurings identified above had an immaterial impact on the allowance for loan losses and resulted in an immaterial amount of charge offs during the years ended December 31, 2015 and 2014.

5. Premises and Equipment

A summary of premises and equipment and related accumulated depreciation follows:

	December 31, 2015	December 31, 2014
	(in thousands)	
Land and land improvements	$ 2,888	$ 2,882
Premises	10,209	10,199
Furniture and equipment	3,779	3,634
	16,876	16,715
Less accumulated depreciation	(9,715)	(9,349)
Premises and equipment, net	$ 7,161	$ 7,366

6. Other Real Estate Owned

The Bank owned five foreclosed properties with a carrying value of $971,000 at December 31, 2015 and five foreclosed properties with a carrying value of $1.2 million at December 31, 2014. During 2015, one residential and two commercial properties were transferred into other real estate owned at a cost basis of $476,000, which included $80,000 of valuation write-ups based on current appraisals less estimated selling costs. Valuation write-downs recognized for impairment below appraised values were recognized on two existing other real estate owned properties during 2015 and totaled $74,000. Other real estate owned activity in 2015 also included sale of four properties for $745,000, which generated gains of $140,000. In 2014 and 2013, net gain on sale/write-down of other real estate owned totaled $123,000 and $91,000, respectively. Net gain on the sale/write-down of other real estate owned is included in noninterest income on the consolidated statements of income.

7. Time Deposits

The scheduled maturities of time deposits at December 31, 2015 and 2014 were:

	2015	2014
Year ending December 31:	(in thousands)	
2015	$ -	$ 38,915
2016	38,622	17,115
2017	13,685	4,785
2018	6,370	6,574
2019	1,793	833
2020 and thereafter	436	-
Total	$ 60,906	$ 68,222

Included in time deposits are certificates of deposit in excess of $250,000. These certificates and their remaining maturities at December 31, 2015 and 2014 are as follows:

	2015	2014
Year ending December 31:	(in thousands)	
2015	$ -	$ 1,292
2016	3,604	1,870
2017	271	270
2018	1,166	890
Total	$ 5,041	$ 4,322

Interest expense on time deposits, including time deposits issued in denominations of $250,000 or more, amounted to approximately $421,000, $573,000 and $739,000 in 2015, 2014, and 2013, respectively.

8. Other Borrowings

The Bank maintains a line-of-credit with the Federal Home Loan Bank of Indianapolis (“FHLBI”) which provides maximum borrowing capacity of $17.5 million as of December 31, 2015. The line is secured by unencumbered qualified residential mortgage and home equity loans with outstanding balances of $6.4 million and unencumbered investment securities available for sale with a fair value of $14.2 million.

No advances were outstanding on the FHLBI line of credit as of December 31, 2015 and 2014 and no advances were drawn against the FHLBI line of credit during the years ended December 31, 2015 and 2014.

The Board of Directors and a member of executive management had previously extended $188,000 of unsecured non-interest bearing loans to FNBH Bancorp, Inc. to fund operating expenses of the Corporation. In conjunction with the Corporation's December 2013 private placement transaction, $172,000 of the loans were repaid in connection with the Corporation's issuance of the Series B Preferred Shares. The remaining $16,000 was repaid by the Corporation in 2014.

9. Income Taxes

Income tax expense consists of:

	2015	2014	2013
		(in thousands)	
Current	$ 62	$ 20	$ -
Deferred	-	-	104
Total income tax expense	$ 62	$ 20	$ 104

Income tax expense differed from the amounts computed by applying the U.S. Federal income tax rate of 34% to income before taxes as a result of the following:

	2015	2014	2013
		(in thousands)	
Computed "expected" tax expense	$ 1,179	$ 1,044	$ 1,047
Increase (reduction) in tax resulting from:			
Tax-exempt interest and dividends, net	(21)	(45)	(28)
Change in valuation allowance	(1,172)	(965)	(893)
Other, net	76	(14)	(22)
Total income tax expense	$ 62	$ 20	$ 104

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below:

	December 31,	
	2015	2014
	(in thousands)	
Deferred tax assets:		
Allowance for loan losses	$ 348	$ 1,113
Net operating loss carryforward	6,992	7,370
AMT credit carryforward	39	32
Charitable contributions carryforward	92	50
Other-than-temporary impairment on investment securities available for sale	769	769
Premises and equipment	249	277
Deferred directors' fees	62	76
Reserve for other real estate owned	26	9
Unrealized loss on investment securites available for sale	195	19
Other	18	87
Total gross deferred tax assets	8,790	9,802
Deferred tax liabilities:		
Deferred loan fees	(61)	(59)
Other	(48)	(66)
Total gross deferred tax liabilities	(109)	(125)
Net deferred tax asset before valuation allowance	8,681	9,677
Valuation allowance	(8,681)	(9,677)
Net deferred tax asset	$ -	$ -

Deferred tax assets are subject to periodic asset realization tests. Management believes the above valuation allowances are required at December 31, 2015 and 2014, due to the uncertainty of future taxable income necessary to fully realize the recorded net deferred tax asset.

It is the Corporation’s policy to evaluate the realizability of deferred tax assets related to unrealized losses on investment securities available for sale separately from its other deferred tax assets when it has the intent and ability to hold the security to recovery (maturity, if necessary). Because the future taxable income implicit in the recovery of the basis of investment securities available for sale for financial reporting purposes will offset the deductions underlying the deferred tax asset, a valuation allowance would generally not be necessary, even in cases where a valuation allowance might be necessary related to the Corporation’s other deferred tax assets.

At December 31, 2015, the Corporation had a net operating loss carryforward of approximately $20.6 million that expires beginning in 2029 if not previously utilized.

The Corporation has no unrecognized tax benefits and does not anticipate any increase to unrecognized tax benefits in the next twelve months. Tax years from 2012 through the current year remain open to examination. The Corporation does not believe the results from any exam of these open years would have a material adverse effect on the Corporation.

10. Related Party Transactions

Certain directors and executive officers, including their immediate families and companies in which they are principal owners, were loan customers of the Bank during 2015 and 2014. Deposits from such individuals and their related interests totaled approximately $1.3 million at both December 31, 2015 and 2014, respectively. Loans were made to such individuals in the ordinary course of business, in accordance with the Bank's normal lending policies, including the interest rate charged and collateralization, and do not represent more than a normal credit risk.

Loans to related parties are summarized below for the periods indicated:

	December 31,	
	2015	2014
	(in thousands)	
Balance at beginning of year	$ 175	$ 180
New loans and related parties	60	45
Loan repayments	(163)	(50)
Balance at end of year	$ 72	$ 175

11. Leases

The Bank has noncancelable operating leases for a branch facility and space at third-party location that houses auxiliary communications equipment. The branch facility lease provides for renewal options. Total future minimum lease payments under the noncancelable leases as of December 31, 2015, are as follows:

Year ending December 31 (in thousands):

2016	$ 69
2017	57
Total lease payments	$ 126

Rental expense charged to operations in 2015, 2014 and 2013 amounted to approximately $72,000, $85,000, and $92,000, respectively, including amounts paid under short term, cancelable leases.

12. Retirement Plan

The Bank sponsors a 401(k) defined contribution plan covering all employees 21 years of age or older who have completed six months of service as defined in the plan agreement. Plan expenses recognized for discretionary employer contributions equal to 50% of an employee's contribution, limited to 3% of the employee's base compensation or the maximum amount permitted by the Internal Revenue Code totaled approximately $97,000, $100,000 and $75,000 in 2015, 2014 and 2013, respectively.

13. Shareholders' Equity

On December 11, 2013, the Corporation closed a private placement offering to accredited investors and issued 17,510 shares of its Mandatorily Convertible Non-Cumulative Junior Participating Preferred Stock, Series B (the "Series B Preferred Shares"). The transaction generated gross proceeds to the Corporation of approximately $17.5 million which provided approximately $16.5 million of additional equity after related offering costs. At that time, shares of preferred stock were offered in the private placement instead of common stock because the Corporation did not have a sufficient number of authorized common shares to raise the desired amount of capital needed from the private placement.

On March 27, 2014, the Corporation completed the issuance and sale of new shares of common stock to shareholders of record on January 8, 2014 pursuant to a rights offering that was registered with the SEC. The Corporation issued a total of approximately 2.3 million common shares in the rights offering. The rights offering generated gross proceeds of approximately $1.6 million and provided additional equity to the Corporation of approximately $1.5 million, after offering costs.

At the Corporation's annual shareholder meeting held on May 22, 2014, shareholders voted to amend the Corporation's Restated Articles of Incorporation to increase the amount of authorized shares of common stock from 11 million to 40 million shares. The increase in authorized common shares triggered the mandatory conversion of the Series B Preferred Shares to common stock. As a result, effective May 22, 2014, the 17,510 issued and outstanding shares of Series B Preferred Shares were converted into 25,014,256 shares of common stock at a rate of $0.70 per share of common stock.

Prior to the conversion into common stock, the terms of the Series B Preferred Shares were substantially identical to the terms applicable to the outstanding common stock with respect to dividends, distributions, voting, and all other matters. Given the parity of the rights and limitations and the lack of preferences of the Series B Preferred Shares relative to the Corporation's common stock, the Series B Preferred Shares were, for all purposes, considered a common stock equivalent while they were outstanding.

Because the sale of the Series B Preferred Shares was not registered under federal securities laws pursuant to an exemption from such registration requirements, the related shares of common stock issued upon conversion of the Series B Preferred Shares are also not registered under federal securities laws.

14. Net Income per Common Share

Basic earnings per common share are based on the weighted average number of common shares and participating securities outstanding during the period. Diluted earnings per share are the same as basic earnings per share because any additional potential common shares issuable are included in the basic earnings per share calculation.

For purposes of determining basic and diluted net income per share for 2014 and 2013, while the Corporation's 17,510 shares of Series B Preferred Shares were outstanding (issued on December 11, 2013 and converted into common stock on May 22, 2014), the shares were considered a common stock equivalent and converted to common shares at a rate reflecting a price per share of common stock of $0.70.

The following presents basic and diluted net income per share:

	2015	2014	2013
	(dollars in thousands, except per share amounts)		
Weighted average basic and diluted common shares outstanding	27,771,678	17,498,168	457,435
Weighted average common stock equivalent preferred shares outstanding, as converted	-	9,731,574	1,439,178
Total weighted average basic and diluted shares outstanding	27,771,678	27,229,742	1,896,613
Net income available to common shareholders	$ 3,406	$ 3,050	$ 2,974
Basic and diluted net income per share	$ 0.12	$ 0.11	$ 1.57

15. Director Compensation

Under a legacy Director Stock Fee Plan, nonemployee directors could receive stock in lieu of all or a portion of the fees payable to them as directors. Under the Plan, director fees consisted of a fixed per-meeting fee paid for attendance at board and committee meetings and a variable fee based on a director's fixed fees earned during the preceding calendar year, multiplied by the bonus percentage of base compensation paid to Bank officers in the preceding calendar year.

The Plan allowed for payment of director fees into a deferred stock account for which stock units were recorded until converted to shares and issued upon retirement, pursuant to a director's installment payment election. At December 31, 2015, there were approximately 1,267 remaining shares earned and available for distribution in deferred stock accounts owned by former directors. No director fee compensation expense related to the legacy Plan was recognized in 2015, 2014, or 2013.

Effective in 2015 and in light of the improved financial and regulatory condition of the Corporation and the Bank, director fee compensation was reinstated and totaled $108,000. All director fee compensation had been previously suspended since October 2012. Under the current Director Compensation Plan, nonemployee directors are paid a fixed monthly fee for their services to the Corporation and Bank.

16. Financial Instruments with Off-Balance-Sheet Risk

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments are loan commitments to extend credit and letters of credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amounts recognized in the consolidated balance sheets.

The Bank's exposure to credit loss in the event of the nonperformance by the other party to the financial instruments for loan commitments to extend credit and letters of credit is represented by the contractual amounts of these instruments. The Bank uses the same credit policies in making credit commitments as it does for on-balance-sheet loans.

Financial instruments whose contract amounts represent credit risk are as follows:

	December 31,	
	2015	2014
	(in thousands)	
Commercial	$ 15,752	$ 10,118
Commercial real estate	12,949	2,977
Consumer real estate	2,302	5,729
Consumer and other	7,614	2,752
Total credit commitments	$ 38,617	$ 21,576

Loan 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. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable;

inventory; property, plant, and equipment; residential real estate; and income-producing commercial properties. Market risk may arise if interest rates move adversely subsequent to the extension of commitments.

As of December 31, 2015 and 2014, the Bank had outstanding irrevocable standby letters of credit, which carry a maximum potential commitment of approximately $537,000 and $10,000, respectively. These letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The majority of these letters of credit are short term guarantees of one year or less, although some have maturities which extend as long as two years. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. The Bank primarily holds real estate as collateral supporting those commitments for which collateral is deemed necessary. The extent of collateral held on those commitments at December 31, 2015 and 2014, where there is collateral, is in excess of the committed amount. A letter of credit is not recorded on the consolidated balance sheets until a customer fails to perform.

17. Regulatory Capital

The Corporation and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can result in the initiation of certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct, material effect on the Corporation's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action ("PCA"), the Corporation and the Bank must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators with regard to components, risk weightings, and other factors.

The final rules implementing Basel Committee on Banking Supervision's capital guidelines for US banks (Basel III rules) became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Basel III redefined Tier 1 capital as two components (Common Equity Tier 1 and Additional Tier 1), created a new capital ratio (Common Equity Tier 1 Risk-based Capital Ratio) and implemented a capital conservation buffer. It also revised the PCA thresholds and changed risk weights for certain assets and off-balance-sheet exposures to enhance risk sensitivity. Pursuant to Basel III, the Bank continues to exclude the net unrealized gain or loss on investment securities available for sale from the computation of regulatory capital. Capital amounts and ratios for December 31, 2014 are calculated using Basel I rules. Management believes as of December 31, 2015, the Corporation and the Bank meet all capital adequacy requirements to which they are subject.

Prompt corrective action ("PCA") regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At December 31, 2015, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for PCA. At December 31, 2014, despite the Bank's capital ratios exceeding minimum ratios for a well-capitalized institution, the Bank was considered "adequately capitalized" for purposes of the OCC's PCA enforcement powers due to an outstanding Consent Order issued to the Bank by the OCC on October 31, 2013 that was terminated by the OCC on November 17, 2015. At December 31, 2014, the Bank was subject to higher minimum capital ratios than those shown below due to the Consent Order which required the Bank to maintain a Total risk-based capital ratio of 11% and a Tier 1 leverage ratio of 8.5%. As shown below, the Bank's actual ratios as of December 31, 2014 were in compliance with the minimum ratios required by the Consent Order.

The Bank's actual capital amounts and ratios are presented in the following table:

	Actual		Minimum for Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provision	
As of December 31, 2015	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(dollars in thousands)			
Common Equity Tier 1 Capital (to risk weighted assets)						
Bank	$ 33,384	15.57%	$ 9,651	4.50%	$ 13,941	6.50%
Total Capital (to risk weighted assets)						
Bank	36,206	16.88%	17,158	8.00%	21,448	10.00%
Tier 1 Capital (to risk weighted assets)						
Bank	33,384	15.57%	12,869	6.00%	17,158	8.00%
Tier 1 Capital (to average assets)						
Bank	33,384	9.90%	13,493	4.00%	16,866	5.00%
As of December 31, 2014	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total Capital (to risk weighted assets)						
Bank	$ 32,346	16.46%	$ 15,721	8.00%	$ 19,651	10.00%
Tier 1 Capital (to risk weighted assets)						
Bank	29,828	15.18%	7,860	4.00%	11,791	6.00%
Tier 1 Capital (to average assets)						
Bank	29,828	9.34%	12,780	4.00%	15,975	5.00%

Consolidated capital amounts and ratios are not presented above as they are not considered significantly different from the Bank due to the Bank comprising greater than 99% of the consolidated assets of the holding company and due to total consolidated assets being less than $1 billion.

18. Dividend Restrictions

On a parent company-only basis, the Corporation's only source of funds is dividends paid by the Bank. The ability of the Bank to pay dividends is subject to limitations under various laws and regulations and to prudent and sound banking principles. The Bank may declare a dividend without the approval of the Office of the Comptroller of the Currency (OCC) unless the total dividends in a calendar year exceeds the total of its net profits for the year combined with its retained profits of the two preceding years. Under these provisions, approximately $9.8 million was available for dividends by the Bank to the Corporation on December 31, 2015, without the approval of the OCC.

19. Contingent Liabilities

The Corporation is subject to various claims and legal proceedings arising out of the normal course of business, none of which, in the judgement of management, based on the advice of legal counsel, is expected to have a material effect on the Corporation's financial position or results of operations.

20. Fair Value Measurements

ASC Topic 820 defines fair value and establishes a consistent framework for measuring fair value and expands disclosure requirements for fair value measurements. Fair values represent the estimated price that would be received from selling an asset or paid to transfer a liability, otherwise known as an "exit price". The three levels of inputs that may be used to measure fair value are as follows:

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

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

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

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

Investment securities available for sale. Investment securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based on quoted prices, if available (Level 1). If quoted prices are not available, fair values are measured using independent pricing models such as matrix pricing models (Level 2). Matrix pricing is a mathematical technique widely used in the financial industry to value debt securities without relying exclusively on quoted market prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted prices. Level 2 securities include U.S. agency securities, U.S. government and agency mortgage-backed securities, obligations of state and political subdivisions, corporate bonds and preferred stock securities. Level 3 securities include private collateralized mortgage obligations. The fair value measurement of our only Level 3 security, a non-investment grade, non-government agency CMO, and details regarding significant inputs and assumptions used in estimating its fair value, is detailed in Note 2, Securities.

Fair value of assets measured on a recurring basis:

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in thousands)			
December 31, 2015				
Mortgage-backed/CMO - residential	$ 124,145	$ -	$ 123,176	$ 969
U.S. agency	7,954	-	7,954	-
Obligations of state and political subdivisions	4,899	-	4,899	-
Corporate bonds	4,252	-	4,252	-
Preferred stock	272	-	272	-
Total investment securities available for sale	$ 141,522	$ -	$ 140,553	$ 969
December 31, 2014				
Mortgage-backed/CMO - residential	$ 107,137	$ -	$ 105,942	$ 1,195
U.S. agency	23,130	-	23,130	-
Obligations of state and political subdivisions	1,605	-	1,605	-
Preferred stock	303	-	303	-
Total investment securities available for sale	$ 132,175	$ -	$ 130,980	$ 1,195

The reconciliation of the beginning and ending balances of the asset classified by the Corporation within Level 3 of the valuation hierarchy is as follows:

	2015		2014	
	Fair Value Measurement Using Significant Unobservable Inputs (Level 3)		Fair Value Measurement Using Significant Unobservable Inputs (Level 3)	
Fair value of non-government agency CMO security, beginning of year[1]	$	1,195	$	1,454
Total gains (losses) realized/unrealized:				
Included in earnings[2]		-		-
Included in other comprehensive income (loss) [2]		(38)		66
Purchases, sales, issuances, and other settlements		(188)		(325)
Transfers into Level 3		-		-
Fair value of non-government agency CMO security, end of year	$	969	$	1,195
Total amount of losses for the year included in earnings attributable to the change in unrealized losses relating to assets still held at end of year	$	-	$	-

(1) Non-government agency CMO security classified as available for sale is valued using internal valuation models and pricing information from third parties.

(2) Realized gains (losses), including unrealized losses deemed other-than-temporary, are reported in noninterest income. Unrealized gains (losses) are reported in accumulated other comprehensive loss.

The following is a description of the Corporation's valuation methodologies used to measure and disclose the fair values of its financial assets on a non-recurring basis:

Loans. The Corporation does not record loans at fair value on a recurring basis. However, from time to time, the Corporation records nonrecurring fair value adjustments to collateral dependent loans to reflect partial write-downs or specific reserves that are based on the observable market price or current appraised value of the collateral. These loans are reported in the nonrecurring table below at initial recognition of impairment and on an ongoing basis until recovery or charge off. When the fair value of the collateral is based on an observable market price or a current appraised value, the Corporation records the impaired loan as nonrecurring Level 2. When a current appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Corporation records the impaired loan as nonrecurring Level 3.

Other real estate owned. Real estate acquired through foreclosure or deed-in-lieu is adjusted to fair value less costs to sell upon transfer of the loan to other real estate owned, usually based on an appraisal of the property. Subsequently, other real estate owned is carried at the lower of carrying value or fair value, less cost to sell. A valuation based on a current appraisal or by a broker's opinion is considered a Level 2 fair value. If management determines the fair value of the property is further impaired below the appraised value and there is no observable market price, the Corporation records the property as nonrecurring Level 3.

Appraisals for both collateral-dependent impaired loans and other real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Corporation. Management reviews the assumptions and approaches utilized in the appraisal. Management periodically evaluates the appraised values and will discount a property's appraised value to account for a number of factors including but not limited to the cost of liquidating the collateral, the age of the appraisal, observable deterioration since the appraisal, or other factors unique to the property.

Fair value of assets on a non-recurring basis:

	Total		Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)		Significant Unobservable Inputs (Level 3)	
			(in thousands)					
December 31, 2015								
Impaired loans [1]	$	1,251	$	-	$	-	$	1,251
Other real estate owned		505		-		-		505
December 31, 2014								
Impaired loans [1]	$	-	$	-	$	-	$	-

(1) Represents carrying value and related write-downs and specific reserves pertaining to collateral dependent loans for which adjustments are based on the appraised value of the collateral or by other unobservable inputs.

Impaired loans as of December 31, 2015 and 2014 measured for impairment using the fair value of the collateral for collateral dependent loans, had a carrying value of approximately $1.3 million after a specific allowance allocation of $98,000 and $0 after a specific allowance allocation of approximately $1.4 million, respectively, resulted in no additional provision for loan losses for the years then ended. During 2015, approximately $1.3 million of a specific allowance allocation on an impaired collateral dependent loan at December 31, 2014 was credited to the provision for loan losses following resolution of outstanding environmental matters and pursuant to regulatory approval.

Other real estate owned as of December 31, 2015 carried at a fair value of $505,000, net of a valuation allowance of $74,000, resulted in write-downs of $74,000 during the year. There were no other real estate properties measured at fair value on a non-recurring basis which required a valuation allowance at December 31, 2014.

As discussed previously, the fair values of impaired loans and other real estate owned carried at fair value are determined by third party appraisals. Management makes adjustments to these appraised values based on the age of the appraisal and the type of the property. The following table presents quantitative information about level 3 fair value measurements for the larger classes of financial instruments measured at fair value on a non-recurring basis at December 31, 2015 and 2014, respectively:

2015		Fair Value	Valuation Techniques	Unobservable Inputs	Range (Weighted Average)
Impaired loans					
Commercial real estate	$	1,251	Sales comparison approach	Management discount for property type and recent market volatility	7% (7%)
Other real estate owned - Commercial		505	Sales comparison approach	Management discount for property type and recent market volatility	9% - 19% (13%)
2014					
Impaired loans					
Commercial real estate	$	-	Sales comparison approach	Management discount for property type and recent market volatility	100% (100%)

21. Fair Value of Financial Instruments

Fair value disclosures require fair-value information about financial instruments for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair-value estimates cannot be substantiated by comparison to independent markets and, in many cases, cannot be realized in immediate settlement of the instrument.

Fair-value methods and assumptions for the Corporation’s financial instruments are as follows:

Cash and cash equivalents – The carrying amounts reported in the consolidated balance sheets for cash, due from banks and short-term investments reasonably approximate those assets’ fair values.

Interest-bearing time deposits with other financial institutions – The carrying amount of interest-bearing time deposits with other financial institutions is based on current rates for similar certificates of deposit.

Investment securities available for sale – Fair values for investment securities available for sale are determined as discussed above.

FHLBI and FRB stock – It is not practicable to determine the fair value of Federal Home Loan Bank Stock of Indianapolis and Federal Reserve Bank Stock due to restrictions placed on their transferability.

Loans held for investment – For variable-rate loans that reprice frequently, fair values are generally based on carrying values, adjusted for credit risk. The fair value of fixed-rate loans is estimated by discounting future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Accrued interest receivable – The carrying amount of accrued interest receivable is a reasonable estimate of fair value.

Deposits – The fair value of deposits with no stated maturity, such as demand deposit, NOW, savings, and money market accounts, is equal to the amount payable on demand. The fair value of time deposits is estimated using rates currently offered for wholesale funds with similar remaining maturities.

Accrued interest payable – The carrying amount of accrued interest payable is a reasonable estimate of fair value.

Off-balance-sheet instruments – The fair value of commitments to extend credit is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of commitments to extend credit, including letters of credit, is estimated to approximate their aggregate book balance and is not considered material and therefore not included in the following table.

	December 31, 2015		December 31, 2014	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(in thousands)			
Financial assets:				
Cash and cash equivalents	$ 29,685	$ 29,685	$ 26,336	$ 26,336
Interest-bearing time deposits with other financial institutions	941	941	-	-
Investment securities available for sale	141,522	141,522	132,175	132,175
FHLBI and FRB stock	1,065	N/A	1,140	N/A
Loans, net	165,108	165,124	152,937	153,284
Accrued interest receivable	851	851	683	683
Financial liabilities:				
Deposits	$ 313,066	$ 313,011	$ 290,379	$ 290,521
Accrued interest payable	52	52	59	59

Limitations

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

22. New Accounting Standards

FASB issued Accounting Standards Update ("ASU") 2014-04, *Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure*. The amendments in this ASU clarify that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. This amendment is effective for fiscal years, and interim periods within those years, beginning after December 15, 2014. The impact of adoption of this ASU by the Corporation in 2015 was not material.

FASB issued ASU 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 205): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity.* The amendments in the Update change the requirements for reporting discontinued operations. A discontinued operation may include a component of an entity or a group of components of an entity, or a business or nonprofit activity. A disposal of a component of an entity or a group of components of an entity is required to be reported in discontinued operation if the disposal represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results. The amendments in this Update require an entity to present for each comparative period, the assets and liabilities of a disposal group that included a discontinued operation separately in the asset and liability sections, respectively, of the statement of financial position. This Update also requires additional disclosures about discontinued operations including pretax profit or loss, and any ongoing involvement with the discontinued operation. The amendments are effective for the annual periods and interim periods within those annual periods beginning December 15, 2014. The impact of adoption of this ASU by the Corporation in 2015 was not material.

FASB issued ASU 2014-14, *Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure.* This update requires creditors to reclassify loans that are within the scope of the ASU to "other receivables" upon foreclosure, rather than reclassifying them to other real estate owned. The separate other receivable recorded upon foreclosure is to be measured based on the amount of the loan balance (principal and interest) the creditor expects to recover from the guarantor. The new guidance is effective for the public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. The impact of the adoption of the ASU by the Corporation in 2015 was not material.

FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606).* This ASU supersedes and replaces nearly all existing revenue recognition guidance, including industry-specific guidance, establishes a new control-based revenue recognition model, changes the basis for deciding when revenue is recognized over time or at a point in time, provides new and more detailed guidance on specific topics and expands and improves disclosures about revenue. In addition, this ASU specifies the accounting for some costs to obtain or fulfill a contract with a customer. The new guidance does not apply to certain contracts within the scope of other ASC Topics, such as lease contracts, insurance contracts, financing arrangements, financial instruments, guarantees other than product or service warranties, and nonmonetary exchanges between entities in the same line of business to facilitate sales to customers. The amendments are effective for annual periods and interim periods within those annual periods beginning after December 15, 2016. In August 2015, FASB issued ASU 2015-14, *Revenue from Contracts with Customers (Topic 606) – Deferral of the Effective Date,* to delay the implementation requirement by one year. The impact of adoption of this ASU by the Corporation is not expected to be material.

FASB issued ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10) – Recognition and Measurement of Financial Assets and Financial Liabilities*. This ASU amends existing guidance related to the accounting for certain financial assets and liabilities. These amendments, among other

things, require equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income, require public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, require separate presentation of financial assets and financial liabilities by measurement category and form of financial asset and eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The new standard is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Management is currently assessing the impact to the Corporation's consolidated financial statements.