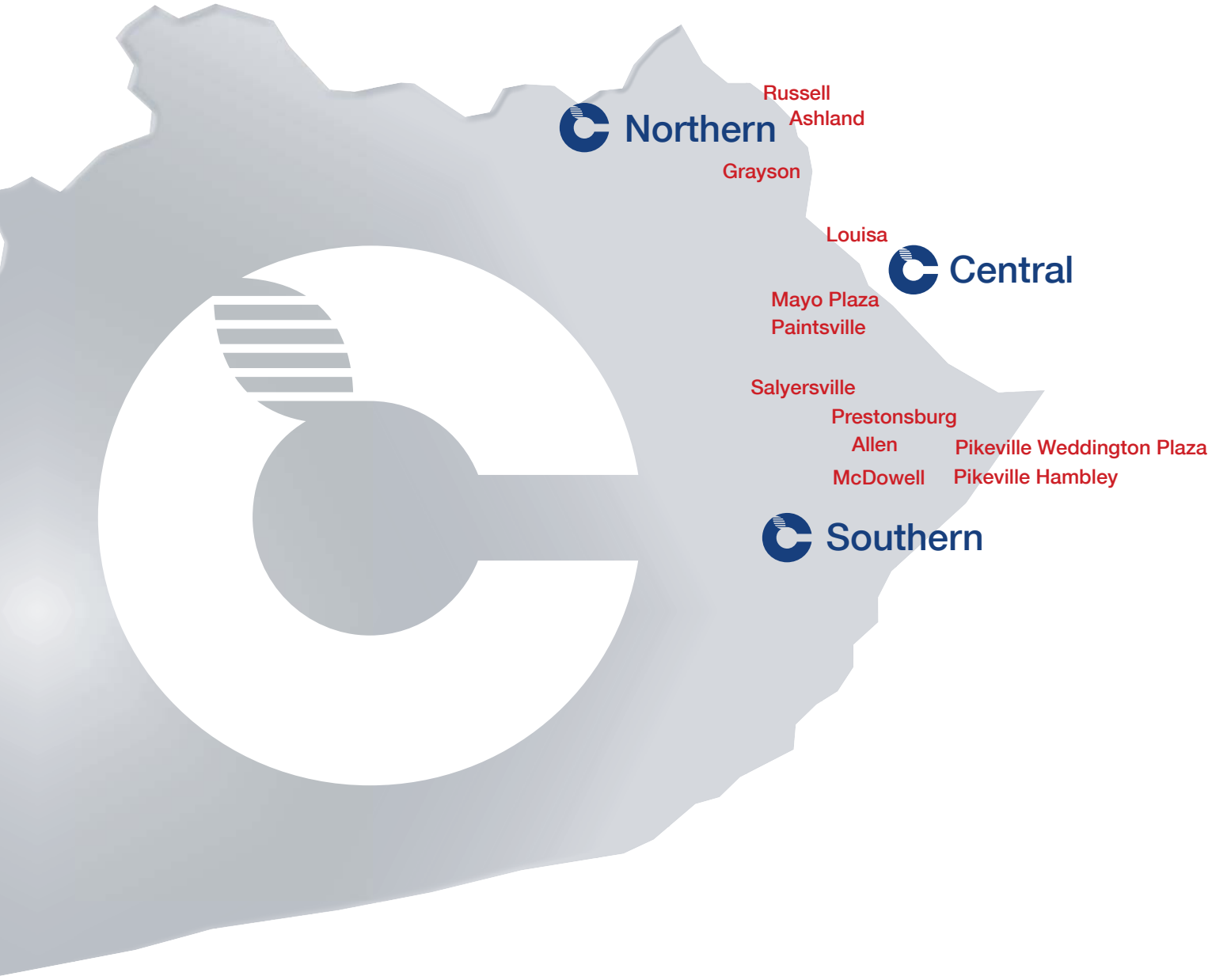
Citizens NATIONAL CORPORATION

Annual Report **2014**



Presence. Stability. Innovation.

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Our Vision & Philosophy

OUR VISION

Citizens National Bank will be the preferred, high performing, independent community bank in the markets we serve. We partner with growing businesses and consumers to build lasting and successful relationships. We do this by providing financial products and services valued by our customers and delivered by committed employees who really mean it.

OUR PHILOSOPHY

At Citizens National Bank, the customer experience is our first priority. We will provide convenient branch/ATM locations as well as maintain a wide range of systems and technology to meet customer needs. We will continue to offer our customers the latest in superior financial products and services. Citizens National Bank pledges to provide accurate, timely and personal service and when an error or problem does arise, we will work to resolve it to our customer's total satisfaction. We will strive to be responsive, thoughtful and friendly. Finally, we at Citizens National Bank promise that we will never lose sight of the fact that our customers are our greatest asset.

Letter to Shareholders

As you read our annual statement, you will see that 2014 has been a year of improvement for Citizens National Corporation and our subsidiary, Citizens National Bank.

Operationally, our subsidiary had an operating budget level performance of $3.9 million; however, through the acquisition of Peoples Security Bank of Louisa which was completed on December 22nd, we attained a subsidiary financial performance of $5.5 million.

Peoples Security Bancorp was purchased by Citizens National Corporation by investing cash in the amount of $3.240 million and notes payable in the amount of $3.239 million. Of the $3.240 million cash investment, $2.612 million was available from cash at Peoples Security Bancorp Inc. and the remaining cash came from Citizens National Corporation. As acquisition accounting requires all assets being purchased be booked at market value, we recognized $1.6 million in a "bargain gain on acquisition," which accounts for about 30% of our net performance at the subsidiary level of $5.5 million.

This year our subsidiary bank grew loans by approximately 4% organically and 7% by acquisition. Our loan portfolio is now over $300 million and we have a strong pipeline for continued growth in 2015.

Our Wealth Management department showed growth in excess of 28%, as trust and brokerage have combined assets in excess of $67 million. This level of assets produced a revenue growth of 75.7% over 2013, which further increases Wealth Management's impact on our bottom line.

With our organic performance and our acquisition, Citizens National Corporation closed 2014 with both share value and corporate income up over 2013 - Book Value by $7.02 or 14.9%; Tangible Book Value by $6.23 or 18.8%; and, corporate income by $1.784 million or 49.8%. Our capital is strong with Tier 1 at 10.85%, an improvement of 1.24% from 9.61% in 2013.

Our increased capital was utilized to return more to our shareholders. This was accomplished by implementing a stock repurchase plan of up to 100,000 (approximately 8.5%) shares in May 2014, followed by an increase in our dividend in the third quarter by 2 cents per quarter (12.5%). During 2014, we retired 22,542 shares and, with dividends, returned over $1.5 million to our shareholders. Our strong capital was also used to support our acquisition of Peoples Security Bancorp and subsidiary. This acquisition is a stimulus for growth, consolidating our footprint of contiguous counties along the US 23 corridor from Pikeville to Ashland.

We envision a future of growth. We shall continue to search for acquisition opportunities while expanding our delivery of products and services within our existing branch structure and will constantly strive to adhere to our Vision and Philosophy in order to show that *we take banking personally.*

V. Burton Bellamy

President/Chief Executive Officer

Shareholder Information

Annual Shareholders' Meeting

Citizens National Corporation
620 Broadway
Paintsville, KY 41240
Tuesday, April 21, 2015
11:30 a.m.

How to Buy Stock

Prospective investors, securities analysts, portfolio managers and representatives of financial institutions seeking information about the purchase of Citizens National Corporation stock may reference:

Citizens National Corporation stock is listed on the OTCQB under symbol CZNL.

Shareholder Inquiries

Communications regarding stock holdings, stock certificates, dividend payments, changes of address, transfer of ownership, or other stock matters may be directed to Citizens National Corporation.

Transfer Agent
Citizens National Corporation
620 Broadway
Paintsville, KY 41240
Telephone: 606.264.3026
Email: scollins@cnbonline.com

Investor Relations

Citizens National Corporation's Annual Report and current stock price information are available by contacting the company or visiting www.cnbonline.com. Prospective investors, securities analysts, portfolio managers and representatives of financial institutions seeking these reports or other information regarding the Company may contact:

Leisha Maynard, SVP & CFO
Citizens National Corporation
620 Broadway
Paintsville, KY 41240
Telephone: 606.264.3054
Fax: 606.789.4440
Email: leishamaynard@cnbonline.com

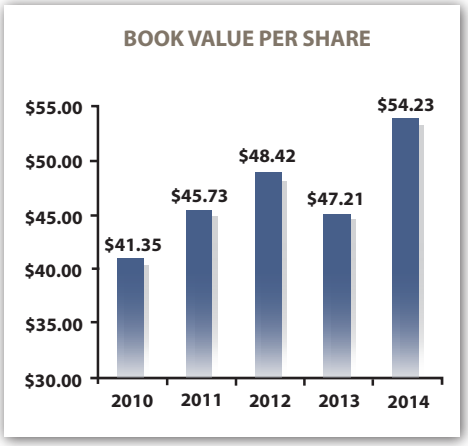
Common Stock

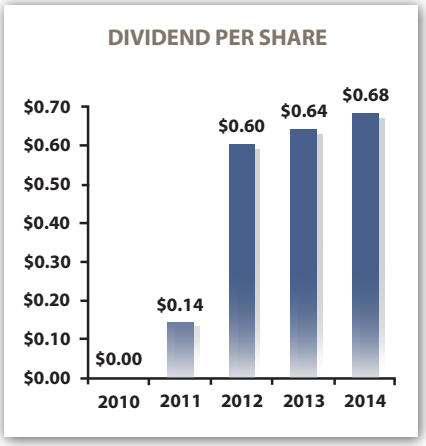
Citizens National Corporation has approximately 224 shareholders. Quarterly dividends on Citizens National Corporation common stock, when declared by the Board of Directors, are paid on or about March 31, June 30, September 30 and December 31. The Company does not currently offer a dividend reinvestment program.

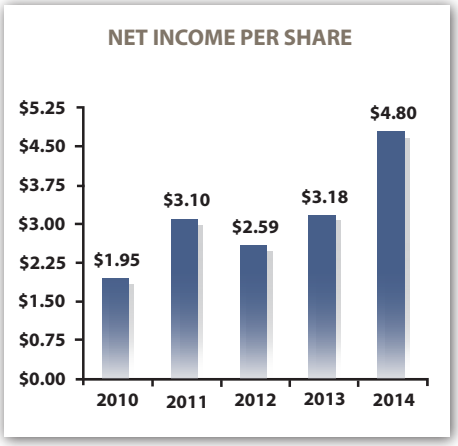
Financial Highlights

Year Ended December 31

	2014	2013	% Change
Net Income	$ 5,363,000	$ 3,579,000	49.8%
Net Interest Income	$ 15,694,000	$ 15,928,000	-1.5%
Net Overhead Expense	$ 9,853,000	$ 11,821,000	-16.6%
Common Dividends Paid	$ 757,000	$ 721,000	5.0%
Per Share			
Basic Earnings Per Common Share	$ 4.80	$ 3.18	50.9%
Dividend Per Common Share	$ 0.68	$ 0.64	6.3%
Book Value Per Common Share	$ 54.23	$ 47.21	14.9%
At Year End			
Total Assets	$ 568,523,000	$ 535,206,000	6.2%
Total Deposits	$ 456,413,000	$ 422,999,000	7.9%
Net Loans	$ 299,656,000	$ 270,719,000	10.7%
Stockholders' Equity	$ 59,809,000	$ 53,121,000	12.6%
Performance Ratios			
Return on Average Assets	1.02%	0.66%	
Return on Average Equity	9.51%	6.64%	
Capital Ratios			
Tier 1 Leverage Ratio	10.85%	9.61%	
Tier 1 Risk-Based	16.14%	15.85%	
Total Risk-Based	17.79%	18.09%	
Loan Loss Reserve to Loans	1.19%	1.40%	







Crowe Horwath®

Crowe Horwath LLP
Independent Member Crowe Horwath International

Independent Auditor's Report

Board of Directors and Shareholders
Citizens National Corporation
Paintsville, Kentucky

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying consolidated financial statements of Citizens National Corporation, which comprise the consolidated balance sheets as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income (loss), changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the 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 audits. We conducted our audits 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.

OPINION

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Citizens National Corporation as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Crowe Horwath LLP

Crowe Horwath LLP
Louisville, Kentucky
March 20, 2015

Consolidated Balance Sheets

December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

	2014	2013
ASSETS		
Cash and due from financial institutions	$ 17,343	$ 12,490
Federal funds sold	4,000	11,000
Cash and cash equivalents	21,343	23,490
Interest bearing deposits in other financial institutions	15,397	6,950
Securities available for sale	177,096	178,118
Loans held for sale	214	209
Loans, net	299,656	270,719
Restricted stock	4,060	3,887
Premises and equipment, net	11,966	10,465
Goodwill	15,605	15,605
Core deposit intangible	734	156
Bank owned life insurance	9,312	9,102
Prepaid expenses	4,848	5,825
Accrued interest receivable and other assets	8,292	10,680
	$ 568,523	$ 535,206
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits		
Non-interest bearing	$ 130,075	$ 110,990
Interest bearing	326,338	312,009
Total deposits	456,413	422,999
Repurchase agreements	7,698	18,383
Federal Home Loan Bank (FHLB) advances	16,711	16,500
Subordinated debentures	16,000	16,000
Notes payable	3,513	1,000
Deferred compensation plans	4,166	4,168
Accrued interest payable and other liabilities	4,213	3,035
Total liabilities	508,714	482,085
Shareholders' equity		
Common stock; 3,000,000 shares authorized; 1,102,767 and 1,125,309 issued and outstanding in 2014 and 2013	10,542	11,360
Retained earnings	47,200	42,594
Accumulated other comprehensive income (loss)	2,067	(833)
Total shareholders' equity	59,809	53,121
	$ 568,523	$ 535,206

See accompanying notes

Consolidated Statements of Income

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

	2014	2013
Interest income		
Loans, including fees	$ 14,232	$ 15,690
Taxable securities	3,052	2,774
Tax exempt securities	1,564	1,489
Federal funds sold and other	49	66
	18,897	20,019
Interest expense		
Deposits	2,042	2,501
Federal Home Loan Bank advance	752	950
Repurchase agreements and federal funds purchased	62	261
Subordinated debentures	304	311
Notes payable	43	68
	3,203	4,091
Net interest income	15,694	15,928
Provision for loan losses	-	100
Net interest income after provision for loan losses	15,694	15,828
Non-interest income		
Service charge on deposit accounts	4,095	4,358
Gain on sale of mortgage loans	92	189
Earnings on bank owned life insurance	210	210
Gains on sales of securities available for sale	141	133
Bargain purchase gain	1,880	-
Other	1,050	814
	7,468	5,704
Non-interest expense		
Salaries and employee benefits	7,863	7,864
Occupancy and equipment	2,074	2,126
Data processing	1,358	1,392
Core deposit amortization	156	311
Advertising	305	247
Net loss (gain) on sale of assets	(33)	472
Franchise and local deposit tax	891	854
FDIC insurance expense	359	374
Other	4,348	3,885
	17,321	17,525
Income before income taxes	5,841	4,007
Income tax expense	478	428
Net income	$ 5,363	$ 3,579
Basic earnings per share	$ 4.80	$ 3.18

See accompanying notes

Consolidated Statements of Comprehensive Income (Loss)

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands)

	2014	2013
Net income	$ 5,363	$ 3,579
Other comprehensive income:		
Unrealized gains (losses) on securities:		
Unrealized holding gains (losses) arising during the period	4,534	(6,303)
Reclassification adjustment for gain included in net income	(141)	(133)
Net unrealized gains (losses)	4,393	(6,436)
Tax effect	1,493	2,188
Total other comprehensive income (loss)	2,900	(4,248)
Comprehensive income (loss)	$ 2,463	$ (669)

See accompanying notes

Consolidated Statements of Changes in Shareholders' Equity

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands)

	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balances, January 1, 2013	$ 11,411	$ 39,736	$ 3,415	$ 54,562
Net income	-	3,579	-	3,579
Redemption of 1,460 shares of common stock	(51)	-	-	(51)
Change in net unrealized gain (loss) on securities available for sale, net of reclassification and tax effects	-	-	(4,248)	(4,248)
Cash dividends declared	-	(721)	-	(721)
Balances, December 31, 2013	11,360	42,594	(833)	53,121
Net income	-	5,363	-	5,363
Redemption of 22,542 shares of common stock	(818)	-	-	(818)
Change in net unrealized gain (loss) on securities available for sale, net of reclassification and tax effects	-	-	2,900	2,900
Cash dividends declared	-	(757)	-	(757)
Balances, December 31, 2014	$ 10,542	$ 47,200	$ 2,067	$ 59,809

See accompanying notes

Consolidated Statements of Cash Flows

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands)

	2014	2013
Cash flows from operating activities		
Net income	$ 5,363	$ 3,579
Adjustments to reconcile net income to net cash from operating activities		
Depreciation and amortization	2,573	901
Net amortization of securities	283	459
Intangible amortization	156	311
Provision for loan losses	-	100
Gain on sale of available for sale securities	(141)	(133)
Loss (gain) on sale of assets	(47)	(6)
Gain on sale of mortgage loans	(92)	(189)
Loss on other real estate owned	157	478
Bargain Purchase Gain	(1,880)	-
Earnings on bank owned life insurance	(210)	(210)
Net change in:		
Loans held for sale	87	(20)
Interest receivable and other assets	2,088	949
Interest payable and other liabilities	489	343
Net cash from operating activities	8,826	6,562
Cash flows from investing activities		
Net cash received in bank acquisition	9,011	-
Change in interest bearing deposits	(8,447)	9,751
Activity in available for sale securities:		
Purchases	(12,915)	(66,234)
Sales	15,289	14,022
Maturities, calls and principal reductions	19,093	30,695
Purchase of restricted stock	-	(163)
Proceeds from sale of other real estate owned	1,588	1,038
Proceeds from sale of property, plant and equipment	-	(25)
Loan originations and payments, net	(11,196)	25,880
Property and equipment expenditures, net	(2,324)	(561)
Net cash from investing activities	10,099	14,403
Cash flows from financing activities		
Net change in deposits	(8,086)	(12,993)
Net change in securities sold under agreements to repurchase	(10,685)	3,601
Net change in notes payable	(726)	(1,700)
Repayment of Federal Home Loan advances	-	(12,000)
Redemption of common stock	(818)	(51)
Common stock dividends paid	(757)	(721)
Net cash from financing activities	(21,072)	(23,864)
Net change in cash and cash equivalents	(2,147)	(2,899)
Beginning cash and cash equivalents	23,490	26,389
Ending cash and cash equivalents	$ 21,343	$ 23,490
Supplemental cash flow information		
Interest paid	$ 3,247	$ 4,179
Income taxes paid	413	178
Supplemental noncash disclosures		
Transfer from loans to other real estate	$ 1,268	$ 1,486

See accompanying notes

Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations and Principles of Consolidation: The consolidated financial statements include the accounts of Citizens National Corporation (Company) and its wholly owned subsidiary, Citizens National Bank (Bank). Citizens is a nationally chartered commercial bank. Intercompany transactions and balances have been eliminated in consolidation.

The Company, through its bank subsidiary, provides financial services through its offices in Eastern Kentucky. Its primary deposit products are checking, savings, and term certificate accounts, and its primary lending products are residential mortgage, commercial, and installment loans. Substantially all loans are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Commercial loans are expected to be repaid from cash flow from operations of businesses. There are no significant concentrations of loans to any one industry or customer. However, the customers' ability to repay their loans is dependent on the real estate and general economic conditions in the area.

Subsequent Events: The Company has evaluated subsequent events for recognition and disclosure through March 20, 2015, which is the date the financial statements were available to be issued.

Use of Estimates: To prepare financial statements in conformity with accounting principles generally accepted in the United States of America, management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and actual results could differ.

Cash Flows: Cash and cash equivalents include cash, deposits with other financial institutions under 90 days, and federal funds sold. Net cash flows are reported for customer loan and deposit transactions, interest bearing deposits in other financial institutions, federal funds purchased and securities sold under agreements to repurchase transactions.

Interest-Bearing Deposits in Other Financial Institutions: Interest-bearing deposits in other financial institutions with maturities typically exceeding 90 days.

Securities: Securities are classified as available for sale when they might be sold before maturity. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in accumulated other comprehensive income, net of tax.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments, except for mortgage-backed securities where prepayments are anticipated. Gains and losses on sales are recorded on the trade date and determined using the specific identification method.

Management evaluates securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) other-than-temporary impairment (OTTI) related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis.

Loans Held for Sale: Mortgage loans originated and intended for sale in the secondary market are carried at the lower of aggregated cost or fair value, as determined by outstanding commitments from investors. Net unrealized losses, if any, are recorded as a valuation allowance and charged to earnings. Mortgage loans held for sale are generally sold servicing released.

Continued on following page

Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Loans: Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, net of unearned interest, deferred loan fees and costs, and an allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level-yield method without anticipating prepayments.

Interest income on mortgage and commercial loans is discontinued at the time the loan is 90 days delinquent unless the loan is well-secured and in process of collection. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not received for loans placed on nonaccrual is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Purchased Credit Impaired Loans: The Company purchases individual loans and groups of loans, some of which have shown evidence of credit deterioration since origination. These purchased credit impaired loans are recorded at the amount paid, such that there is no carryover of the seller's allowance for loan losses. After acquisition, losses are recognized by an increase in the allowance for loan losses.

Such purchased credit impaired loans are accounted for individually. The Company estimates the amount and timing of expected cash flows for each loan, and the expected cash flows in excess of amount paid is recorded as interest income over the remaining life of the loan (accretable yield). The excess of the loan's contractual principal and interest over expected cash flows is not recorded (nonaccretable difference).

Over the life of the loan, expected cash flows continue to be estimated. If the present value of expected cash flows is less than the carrying amount, a loss is recorded as a provision for loan losses. If the present value of expected cash flows is greater than the carrying amount, it is recognized as part of future interest income.

Allowance for Loan Losses: The allowance for loan losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged-off.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired or loans otherwise classified as substandard or doubtful. The general component covers non-classified loans and is based on historical loss experience adjusted for current factors.

A loan is impaired when full payment under the loan terms is not expected. Commercial and commercial real estate loans are individually evaluated for impairment. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Large groups of smaller balance homogeneous loans, such as consumer and residential real estate loans are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosures. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructuring.

Continued on following page

Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Troubled debt restructurings are separately identified for impairment disclosures and are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a troubled debt restructuring is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. For troubled debt restructurings that subsequently default, the Company determines the amount of reserve in accordance with the accounting policy for the allowance for loan losses.

The general component covers non-impaired loans and is based on historical loss experience adjusted for current factors. The historical loss experience is determined by portfolio segment and is based on a 48 month migration analysis. This actual loss experience is supplemented with other economic factors based on the risks present for each portfolio segment. These economic factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; and effects of changes in credit concentrations. The following portfolio segments have been identified: commercial, real estate and consumer.

Loans secured by real estate make up the largest segment of the Company's loan portfolio. If a borrower fails to repay a loan secured by real estate, the Company may liquidate the collateral in order to satisfy the amount owed. The Company uses independent third party state-certified or licensed appraisers in accordance with its loan policy to mitigate risk when underwriting real estate loans. Cash flow analysis of the borrower, loan to value limits as adopted by loan policy and other customary underwriting standards are also in place which are designed to maximize credit quality and mitigate risks associated with real estate lending.

Commercial loans are made to businesses and are secured mainly by assets such as inventory, accounts receivable, machinery, fixtures and equipment, or any other asset of value that relates to business operations. Commercial lending involves significant risk, as loan repayments are more dependent on the successful operation or management of the business and its cash flows.

Consumer lending includes loans to individuals mainly for personal autos or a variety of other personal uses and may be secured or unsecured. Loan repayment associated with consumer loans is highly dependent upon the borrower's continuing financial stability, which is heavily influenced by local unemployment rates. The Company mitigates its risk exposure to each of its loan segments by analyzing the borrower's repayment capacity, imposing restrictions on the amount it will loan compared to estimated collateral values, limiting the payback periods, and following other customary underwriting practices as adopted in its loan policy.

Premises and Equipment: Land is carried at cost. Premises and equipment are reported at cost less accumulated depreciation. Depreciation is calculated on the straight-line and accelerated methods over asset useful lives.

Federal Home Loan Bank Stock (FHLB) and Federal Reserve Bank Stock (FRB): The Bank is a member of the FHLB system and Regional Federal Reserve Bank. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. FHLB and FRB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment. Because this stock is viewed as long term investment, impairment is based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

Continued on following page

Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Bank Owned Life Insurance: The Bank has purchased life insurance policies on certain key executives. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

Transfers of Financial Assets: Transfers of financial assets are accounted for as sales, when control over the assets has been relinquished. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Company, 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 the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Foreclosed Assets: Assets acquired through or instead of loan foreclosure are initially recorded at fair value less cost to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at the lower of cost or fair value less estimated cost to sell. If fair value declines subsequent to foreclosure, a valuation allowance is recorded through expense. Operating costs after acquisition are expensed. Other real estate owned was $2,217 and $2,029 at December 31, 2014 and 2013, respectively.

Goodwill and Other Intangible Assets: Goodwill resulting from business combinations prior to January 1, 2009 represents the excess of the purchase price over the fair value of the net assets of businesses acquired. Goodwill resulting from business combinations after January 1, 2009, is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but tested for impairment at least annually or more frequently if events and circumstances exists that indicate that a goodwill impairment test should be performed. The Company has selected December 31 as the date to perform the annual impairment test. Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill is the only intangible asset with an indefinite life on our balance sheet.

Other intangible assets consist of core deposit intangible assets arising from whole bank and branch acquisitions and are amortized on a straight-line basis over their estimated useful lives of 8 years.

Long-Term Assets: Premises and equipment, core deposit and other intangible assets and other long-term assets are reviewed for impairment when events indicate their carrying amount may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value.

Loan Commitments and Related Financial Instruments: Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial 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.

Repurchase Agreements: Substantially all repurchase agreement liabilities represent amounts advanced by various customers. Securities are pledged to cover these liabilities, which are not covered by federal deposit insurance.

Income Taxes: Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded.

The Company recognizes interest and/or penalties related to income tax matters in income tax expense.

Earnings Per Share: Basic earnings per common share is net income divided by the weighted average number of common shares outstanding during the period. The Company does not present diluted earnings per share because there are no potential dilutive common shares outstanding. Earnings per share are restated for all stock splits and dividends through the date of issue of the financial statements.

Fair Values of Financial Instruments: Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Comprehensive Income: Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale which is also recognized as a separate component of equity.

Loss Contingencies: Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there now are such matters that will have a material effect on the financial statements.

Retirement Plans: Employee 401(k) and profit sharing plan expense is the amount of matching contributions. Deferred compensation and supplemental retirement plan expense allocates the benefits over years of service.

Restrictions on Cash: Cash on hand or on deposit with the Federal Reserve Bank was required to meet regulatory reserve and clearing requirements.

Dividend Restriction: Banking regulations require maintaining certain capital levels and may limit the dividends paid by the Bank to the holding company or by the holding company to shareholders.

Reclassifications: Some items in the prior year consolidated financial statements were reclassified to conform with the current presentation. Reclassifications had no effect on prior year net income or shareholders' equity.

Adoption of New Accounting Standards and Newly Issued Not Yet Effective Accounting Standards:

The following provides a description of recently adopted or newly issued not yet effective accounting standards that could have a material effect on our financial statements:

ASU 2013-02, *Comprehensive Income (Topic 220) – Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* – In February 2013, the FASB amended existing guidance related to reporting amounts reclassified out of accumulated other comprehensive income. These amendments do not change the current requirements for reporting net income or other comprehensive income in financial statements. These amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional details about those amounts. These amendments are effective prospectively for fiscal years, and interim periods within those years, beginning December 15, 2013. The adoption of this standard did not have a material effect on the Company's operating results or financial condition. See footnote 17.

ASU 2013-12, *Definition of a Public Business Entity: An Addition to the Master Glossary* – In December 2013, the FASB amended the Glossary of the Codification to include a single definition of a public business entity for future use in U.S. GAAP. The definition of a public business entity will be used in considering the scope of new financial guidance and will identify whether the guidance does or does not apply to public business entities. The amendment does not affect existing requirements and there is no effective date. The Company is currently evaluating the impact of this amendment on the consolidated financial statements.

ASU 2014-02, *Intangibles – Goodwill and Other (Topic 350) – Accounting for Goodwill* – In January 2014, the FASB amended existing guidance to permit a private company to amortize goodwill on a straight-line basis over a period of ten years, or less if the company demonstrates that another useful life is more appropriate. It also permits a private company to apply a simplified impairment model to goodwill. Under the goodwill accounting alternative, goodwill should be tested for impairment when a triggering event occurs that indicates that the fair value of a company (or a reporting unit) may be below its carrying amount. A private company that elects the accounting alternative is further required to make an accounting policy election to test goodwill for impairment at either the company level or the reporting unit level. The accounting alternative, if elected, should be applied prospectively to goodwill existing as of the beginning of the period of adoption. If elected these amendments are effective for annual periods beginning after December 15, 2014 and interim periods within annual periods beginning after December 15, 2015. The adoption of this standard is not expected to have a material effect on the Company's operating results or financial condition.

ASU 2014-18, *Business Combinations (Topic 805): Accounting for Identifiable Intangible Assets in a Business Combination (a consensus of the Private Company Council)* – In December, the FASB provided an accounting alternative to reduce the cost and complexity associated with the measurement of certain identifiable intangible assets. The amendments permit a private company to elect an accounting alternative to no longer recognize separately from goodwill (1) customer-related intangible assets unless they are capable of being sold or licensed independently from the other assets of the business and (2) noncompetition agreements. Customer-related intangible assets that may meet that criterion for recognition include but are not limited to mortgage servicing rights and core deposits. For private entities electing this alternative, the amendments generally will result in those entities separately recognizing fewer intangible assets in a business combination when compared to entities that do not elect or are not eligible for this alternative.

A private company that elects this accounting alternative must adopt the accounting alternative for amortizing goodwill. If the accounting alternative for amortizing goodwill was not adopted previously, it should be adopted on a prospective basis as of the adoption of the accounting alternative.

The amendments are effective for the first transaction within the scope of the accounting alternative that occurs in fiscal years beginning after December 15, 2015 and for interim and annual periods thereafter. If the first transaction occurs in a fiscal year beginning after December 15, 2016, then this is effective for the interim period that includes the date of the transaction and for interim and annual periods thereafter. Early application is permitted for any interim and annual period before which financial statements are available to be issued. Existing customer-related intangible assets and noncompetition agreements shall continue to be measured in accordance with Topic 350 and are not to be subsumed into goodwill upon adoption. The company is currently evaluating the impact of this amendment on the consolidated financial statements.

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 2 – SECURITIES

The fair value of available for sale securities and the related gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
2014				
U.S. Government and federal agencies	$ 6,000	$ -	$ (106)	$ 5,894
States and municipals	57,404	2,194	(60)	59,538
U.S. Government sponsored entity mortgage backed securities: residential	108,069	1,818	(722)	109,165
Other securities	2,492	10	(3)	2,499
Total	$ 173,965	$ 4,022	$ (891)	$ 177,096
2013				
U.S. Government and federal agencies	$ 9,999	$ -	$ (482)	$ 9,517
States and municipals	50,576	1,045	(759)	50,862
U.S. Government sponsored entity mortgage backed securities: residential	116,325	925	(1,987)	115,263
Other securities	2,480	17	(21)	2,476
Total	$ 179,380	$ 1,987	$ (3,249)	$ 178,118

Proceeds from sales of available for sale securities were $15,289 with a gross gain of $141 and no gross losses in 2014. The tax effect related to this gain was $48. Proceeds from sales of available for sale securities were $14,022 with a gross gain of $133 and no gross losses in 2013. The tax effect related to this gain was $45.

The amortized cost and fair value of debt securities are shown by contractual maturity. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

	Amortized Cost	Fair Value
Due in one year or less	$ 665	$ 668
Due after one year through five years	10,273	10,344
Due after five years through ten years	24,676	25,395
Due after ten years	30,282	31,524
	65,896	67,931
U.S. Government sponsored entity mortgage backed securities: residential	108,069	109,165
	$ 173,965	$ 177,096

Securities with a carrying value of $74,231 and $79,625 at year-end 2014 and 2013 were pledged to secure public deposits, trust deposits, and for other purposes.

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 2 – SECURITIES (Continued)

Securities with unrealized losses at year-end 2014 and 2013 aggregated by investment category and length of time that individual security have been in a continuous unrealized loss position, are as follows:

	Less Than 12 Months		12 Months or More		Total	
Description	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
2014						
U.S. Government and federal agencies	$ 995	$ (5)	$ 4,899	$ (101)	$ 5,894	$ (106)
States and municipals	3,795	(13)	2,760	(47)	6,555	(60)
U.S. Government sponsored entity mortgage backed securities: residential	9,574	(61)	22,133	(661)	31,707	(722)
Other securities	-	-	497	(3)	497	(3)
Total temporarily impaired	$ 14,364	$ (79)	$ 30,289	$ (812)	$ 44,653	$ (891)

	Less Than 12 Months		12 Months or More		Total	
Description	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
2013						
U.S. Government and federal agencies	$ 9,517	$ (482)	$ -	$ -	$ 9,517	$ (482)
States and municipals	15,489	(717)	406	(42)	15,895	(759)
U.S. Government sponsored entity mortgage backed securities: residential	60,980	(1,987)	-	-	60,980	(1,987)
Other securities	1,479	(21)	-	-	1,479	(21)
Total temporarily impaired	$ 87,465	$ (3,207)	$ 406	$ (42)	$ 87,871	$ (3,249)

Unrealized losses on securities have not been recognized into income because the securities are of high credit quality at acquisition and as of December 31, 2014, management does not intend to sell or believe they will not be required to sell in the foreseeable future, and the decline in fair value is largely due to changes in interest rates and other market conditions. The fair value is expected to recover as the bonds approach their maturity and/or market conditions change.

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

NOTE 3 – LOANS

Loans at year-end were as follows:

	2014	2013
Commercial	$ 29,613	$ 27,420
Real estate:		
Commercial real estate	94,021	87,705
Construction and land development	16,791	7,109
Residential real estate	129,907	117,369
Consumer:		
Direct	6,355	4,592
Indirect	26,220	30,434
Other	765	378
Subtotal	303,672	275,007
Less: Allowance for loan losses	(3,616)	(3,848)
Net deferred loan fees	(400)	(440)
Loans, net	$ 299,656	$ 270,719

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

NOTE 3 – LOANS (Continued)

The following table presents the activity in the allowance for loan losses by class of loans for the years ended December 31, 2014 and 2013:

	Commercial	Commercial Real Estate	Construction and Land Development	Residential Real Estate	Consumer Direct	Consumer Indirect	Other/ Unallocated	Total
December 31, 2014								
Allowance for loan losses:								
Beginning balance	$ 439	$ 957	$ 82	$ 1,933	$ 53	$ 312	$ 72	$3,848
Provision for loan losses	(171)	598	104	(398)	130	(232)	(31)	-
Loans charged-off	(45)	-	-	(470)	(50)	(5)	(59)	(629)
Recoveries	206	57	-	109	7	-	18	397
Total ending allowance balance	$ 429	$1,612	$ 186	$ 1,174	$ 140	$ 75	$ -	$3,616
December 31, 2013								
Allowance for loan losses:								
Beginning balance	$ 504	$1,176	$ 77	$ 1,806	$ 59	$ 265	$227	$4,114
Provision for loan losses	(184)	(202)	3	475	11	94	(97)	100
Loans charged-off	(212)	(144)	-	(398)	(42)	(47)	(75)	(918)
Recoveries	331	127	2	50	25	-	17	552
Total ending allowance balance	$ 439	$ 957	$ 82	$ 1,933	$ 53	$ 312	$ 72	$3,848

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 3 – LOANS (Continued)

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio class and based on impairment method as of December 31, 2014 and 2013:

	Commercial	Commercial Real Estate	Construction and Land Development	Residential Real Estate	Consumer Direct	Consumer Indirect	Other/ Unallocated	Total
December 31, 2014								
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ 17	$ 138	$ -	$ 471	$ -	$ 3	$ -	$ 629
Collectively evaluated for impairment	412	1,474	186	703	140	72	-	2,987
Total ending allowance balance	$ 429	$ 1,612	$ 186	$ 1,174	$ 140	$ 75	$ -	$ 3,616
Loans:								
Loans individually evaluated for impairment	$ 313	$ 3,915	$ 261	$ 6,625	$ -	$ 88	$ -	$ 11,202
Loans collectively evaluated for impairment	29,300	90,106	16,530	123,282	6,355	26,132	765	292,470
Total ending loan balance	$ 29,613	$ 94,021	$ 16,791	$ 129,907	$ 6,355	$26,220	$ 765	$303,672
December 31, 2013								
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ 140	$ 20	$ -	$ 831	$ -	$ -	$ -	$ 991
Collectively evaluated for impairment	299	937	82	1,102	53	312	72	2,857
Total ending allowance balance	$ 439	$ 957	$ 82	$ 1,933	$ 53	$ 312	$ 72	$ 3,848
Loans:								
Loans individually evaluated for impairment	$ 521	$ 5,250	$ 281	$ 8,414	$ 7	$ -	$ -	$ 14,473
Loans collectively evaluated for impairment	26,899	82,455	6,828	108,955	4,585	30,434	378	260,534
Total ending loan balance	$ 27,420	$ 87,705	$ 7,109	$ 117,369	$ 4,592	$30,434	$ 378	$275,007

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

NOTE 3 – LOANS (Continued)

The following table presents information related to impaired loans by class of loans as of and for the year ended December 31, 2014:

	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
December 31, 2014						
With no related allowance recorded:						
Commercial	$ 205	$ 76	$ -	$ 63	$ 1	$ 1
Real estate:						
Commercial real estate	1,295	1,295	-	1,806	37	37
Construction and land development	261	261	-	268	-	-
Residential real estate	2,097	1,937	-	3,143	77	72
Consumer:						
Direct	-	-	-	-	-	-
Indirect	-	-	-	-	-	-
Subtotal	3,858	3,569	-	5,280	115	110
With an allowance recorded:						
Commercial	237	237	17	306	7	7
Real estate:						
Commercial real estate	2,620	2,620	138	1,856	107	107
Construction and land development	-	-	-	-	-	-
Residential real estate	4,744	4,688	471	3,507	185	185
Consumer						
Direct	-	-	-	1	-	-
Indirect	91	88	3	32	8	8
Subtotal	7,691	7,633	629	5,702	307	307
Total	$ 11,549	$ 11,202	$ 629	$10,982	$ 422	$ 417

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 3 – LOANS (Continued)

The following table presents information related to impaired loans by class of loans as of and for the year ended December 31, 2013:

	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
December 31, 2013						
With no related allowance recorded:						
Commercial	$ 25	$ 25	$ -	$ 13	$ 1	$ 1
Real estate:						
Commercial real estate	3,626	3,447	-	2,920	157	147
Construction and land development	391	281	-	331	14	14
Residential real estate	4,168	3,991	-	2,668	188	188
Consumer:						
Direct	7	7	-	8	-	-
Indirect	-	-	-	5	-	-
Subtotal	8,217	7,751	-	5,945	360	350
With an allowance recorded:						
Commercial	496	496	140	1,340	18	18
Real estate:						
Commercial real estate	1,803	1,803	20	2,491	91	91
Construction and land development	-	-	-	89	-	-
Residential real estate	4,470	4,423	831	6,048	194	194
Subtotal	6,769	6,722	991	9,968	303	303
Total	$14,986	$ 14,473	$ 991	$ 15,913	$ 663	$ 653

The recorded investment in loans excludes accrued interest receivable and loan origination fees, net, due to immateriality. Management has evaluated the significance of deferred fees and costs and accrued interest receivable relative to the loan portfolio. Deferred fees and costs total $400 and $440 and accrued interest receivable total $832 and $907 at year end 2014 and 2013, respectively. Given the insignificance to the total loan portfolio, amounts are reported at unpaid principal balance.

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 3 – LOANS (Continued)

The following table presents the recorded investment in nonaccrual and loans past due over 90 days still on accrual by class of loans as of December 31, 2014 and 2013:

	Nonaccrual		Loans Past Due Over 90 Days Still Accruing	
	2014	2013	2014	2013
Commercial	$ 157	$ 302	$ -	$ -
Real estate				
Commercial real estate	928	3,146	-	-
Construction and land development	261	276	-	-
Residential real estate	3,995	2,067	85	215
Consumer				
Direct	-	-	-	-
Indirect	71	-	27	154
Other	-	-	-	-
	$ 5,412	$ 5,791	$ 112	$ 369

The following table presents the aging of the recorded investment in past due loans as of December 31, 2014 and 2013:

	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 days Past Due	Nonaccrual Loans	Total Past Due	Loans Not Past Due	Total
December 31, 2014							
Commercial	$ 14	$ -	$ -	$ 157	$ 171	$ 29,442	$ 29,613
Real estate:							
Commercial real estate	34	-	-	928	962	93,059	94,021
Construction and land development	-	-	-	261	261	16,530	16,791
Residential real estate	1,487	421	85	3,995	5,988	123,919	129,907
Consumer:							
Direct	28	-	-	-	28	6,327	6,355
Indirect	1,148	600	27	71	1,846	24,374	26,220
Other	9	1	-	-	10	755	765
Total	$ 2,720	$ 1,022	$ 112	$ 5,412	$ 9,266	$ 294,406	$ 303,672
December 31, 2013							
Commercial	$ -	$ -	$ -	$ 302	$ 302	$ 27,118	$ 27,420
Real estate:							
Commercial real estate	-	-	-	3,146	3,146	84,559	87,705
Construction and land development	233	-	-	276	509	6,600	7,109
Residential real estate	978	210	215	2,067	3,470	113,899	117,369
Consumer:							
Direct	35	1	-	-	36	4,556	4,592
Indirect	1,018	1,128	154	-	2,300	28,134	30,434
Other	11	1	-	-	12	366	378
Total	$ 2,275	$ 1,340	$ 369	$ 5,791	$ 9,775	$ 265,232	$ 275,007

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 3 – LOANS (Continued)

As of December 31, 2014 and 2013, the Company has a recorded investment in troubled debt restructurings of $6,169 and $5,300. The Company has allocated $307 and $783 of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of December 31, 2014 and 2013. The Company has not committed to lend additional amounts as of December 31, 2014 and 2013 to customers with outstanding loans that are classified as troubled debt restructurings.

During the years ended December 31, 2014 and 2013, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included one or a combination of the following: capitalization of interest on the loan; an adjustment of the maturity date; or a delay in payment of principal. Four and two loans were modified as a troubled debt restructuring in 2014 and 2013.

The following tables present loans by class modified as troubled debt restructurings that occurred during the years ended December 31, 2014 and 2013:

	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
December 31, 2014			
Troubled debt restructurings:			
Real estate:			
Commercial real estate	1	$ 1,118	$ 1,118
Construction and land development	1	280	280
Residential real estate	2	1,217	1,217
Total	4	$ 2,615	$ 2,615

The troubled debt restructurings described above increased the allowance for loan losses by $77 and resulted in no charge-offs during the year ended December 31, 2014.

	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
December 31, 2013			
Troubled debt restructurings:			
Real estate:			
Residential real estate	2	$ 2,497	$ 2,496
Total	2	$ 2,497	$ 2,496

The troubled debt restructurings described above increased the allowance for loan losses by $221 and resulted in no charge-offs during the year ended December 31, 2013.

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 3 – LOANS (Continued)

The following tables present loans by class modified as troubled debt restructurings for which there was a payment default within twelve months following the modification during the years ended December 31, 2014 and 2013:

	Number Loans	Recorded Investment
December 31, 2014		
Troubled debt restructurings that subsequently defaulted:		
Real estate:		
Commercial real estate	1	$ 472
Residential real estate	1	1,338
Total	2	$ 1,810
December 31, 2013		
Troubled debt restructurings that subsequently defaulted:		
Real estate:		
Residential real estate	2	$ 2,410
Total	2	$ 2,410

A loan is considered to be in payment default once it is 30 days contractually past due under the modified terms. The troubled debt restructurings that subsequently defaulted described above did not increase the allowance for loan losses and resulted in no charge-offs during the year ended December 31, 2014.

In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the company's internal underwriting policy.

Credit Quality Indicators:

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis includes non-homogeneous loans, such as commercial and commercial real estate, and groups of homogeneous loans. This analysis is performed on a quarterly basis. The Company uses the following definitions for the risk ratings:

Weak Pass: This grade is given to loans that show signs of weakness in either adequate sources of repayment or collateral but have demonstrated mitigating factors that minimize the risk of delinquency of loss.

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NOTE 3 – LOANS (Continued)

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

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

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

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. As of December 31, 2014 and 2013, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

	Pass	Weak Pass	Special Mention	Substandard	Doubtful
December 31, 2014					
Commercial	$ 16,958	$ 10,855	$ 1,507	$ 293	$ -
Commercial real estate	38,722	46,188	6,162	2,949	-
Construction and land development	13,638	2,892	-	261	-
Total	$ 69,318	$ 59,935	$ 7,669	$ 3,503	$ -
December 31, 2013					
Commercial	$ 19,453	$ 5,878	$ 1,593	$ 496	$ -
Commercial real estate	49,499	31,080	2,946	4,180	-
Construction and land development	5,264	1,565	-	280	-
Total	$ 74,216	$ 38,523	$ 4,539	$ 4,956	$ -

The Company considers the performance of the loan portfolio and its impact on the allowance for loan losses. For residential and consumer loan segments, the Company also evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. The following table presents the recorded investment in residential and consumer loans based on payment activity as of December 31, 2014 and 2013:

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
(Dollar amounts in thousands, except per share amounts)

NOTE 3 – LOANS (Continued)

December 31, 2014	Residential	Consumer Direct	Consumer Indirect	Other
Performing	$ 125,827	$ 6,355	$ 26,122	$ 765
Nonperforming	4,080	-	98	-
Total	$ 129,907	$ 6,355	$ 26,220	$ 765

December 31, 2013	Residential	Consumer Direct	Consumer Indirect	Other
Performing	$ 115,087	$ 4,592	$ 30,280	$ 378
Nonperforming	2,282	-	154	-
Total	$ 117,369	$ 4,592	$ 30,434	$ 378

Loans to executive officers and directors, including loans to affiliated companies of these individuals, totaled approximately $9 and $16 at year-end 2014 and 2013.

NOTE 4 – PURCHASED CREDIT IMPAIRED LOANS

In 2014, the Company has purchased loans, for which there was, at acquisition, evidence of deterioration of credit quality since origination and it was probable, at acquisition, that all contractually required payments would not be collected. The carrying amount of those loans is as follows for 2014:

	2014
Commercial	$ 923
Mortgage	224
Outstanding balance	$ 1,147
Carrying amount, net of allowance of $0	$ 1,147
Cash flows expected to be collected at acquisition	$ 1,350
Fair value of acquired loans at acquisition	$ 1,147

For those purchased credit impaired loans disclosed above, the Company did not increase the allowance for loan losses during 2014. No allowances for loan losses were reversed during 2014.

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 5 – PREMISES AND EQUIPMENT

Year-end premises and equipment were as follows:

	2014	2013
Land	$ 2,311	$ 2,311
Buildings and improvements	16,205	12,970
Furniture and equipment	11,480	9,422
	29,996	24,703
Less: Accumulated depreciation	(18,030)	(14,238)
	$ 11,966	$ 10,465

Depreciation expense was $825 and $901 for the years ended 2014 and 2013.

Operating Leases: The Company leases certain branch properties and equipment under operating leases. Rent expense was $258 and $273 for 2014 and 2013. Rent commitments, before considering renewal options that generally are present, were as follows:

2015	$ 247
2016	241
2017	202
2018	139
2019	7

NOTE 6 – INTANGIBLE ASSETS

Acquired Intangible Assets

Acquired intangible assets were as follows at year end:

	2014		2013	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets:				
Core deposit intangibles	$ 4,927	$ 4,194	$ 4,194	$ 4,038

Aggregate amortization expense was $156 and $311 for 2014 and 2013.

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 6 – INTANGIBLE ASSETS (Continued)

Estimated amortization expense for each of the next five years:

2015	$ 92
2016	92
2017	92
2018	92
2019	92

NOTE 7 – TIME DEPOSITS AND TERM REPURCHASE AGREEMENTS

Time deposits of $250 or more were $22,516 and $18,699 at year-end 2014 and 2013.

Scheduled maturities of time deposits and term repurchase agreements for the next five years were as follows:

2015	$ 68,355
2016	42,911
2017	12,115
2018	2,777
2019	12,194
	$ 138,352

Deposits from executive officers, directors, and their affiliates at year-end 2014 and 2013 were $2,753 and $2,962.

NOTE 8 – FEDERAL HOME LOAN BANK ADVANCES

At year-end, advances from the Federal Home Loan Bank were as follows:

	2014	2013
Maturities from June 2015 through May 2023, fixed rates at rates from 2.35% to 5.12%, averaging 4.55%.	$16,711	$ -
Maturities from June 2015 through March 2018, fixed rates at rates from 2.35% to 5.12%, averaging 4.60%.	-	16,500

Each advance is payable at its maturity date, with a prepayment penalty for fixed rate advances. The advances are collateralized by $87,413 and $74,685 of first mortgage loans under a blanket lien arrangement at year end 2014 and 2013. Based on this collateral and the Company's holdings of FHLB stock, the Company is eligible to borrow up to a total of $34,366 at year end 2014.

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NOTE 8 – FEDERAL HOME LOAN BANK ADVANCES (Continued)

Repayments over the next five years are as follows:

2015	5,051
2016	4,048
2017	5,048
2018	2,535
2019	12

NOTE 9 – SUBORDINATED DEBENTURES AND NOTES PAYABLE

In June 2006 and 2007, CZNL Statutory Trust I and Trust II, trusts formed by the Company, closed a pooled private offering of 6,000 and 10,000 trust preferred securities with a liquidation amount of $1 per security. The Company issued $6,186 and $10,310 of subordinated debentures to the trusts in exchange for ownership of all of the common security of the trusts and the proceeds of the preferred securities sold by the trusts. The trusts are not consolidated with the Company's financial statements, but rather the subordinated debentures are shown as a liability.

The Company may redeem the subordinated debentures, in whole or in part, in a principal amount with integral multiples of $1, on or after June 2011 for Trust I and June 2012 for Trust II at 100% of the principal amount, plus accrued and unpaid interest. The subordinated debentures mature on June 2036 for Trust I and June 2037 for Trust II. The subordinated debentures are also redeemable in whole or in part from time to time, upon the occurrence of specific events defined within the trust indentures. The Company has the option to defer interest payments on the subordinated debentures from time to time for a period not to exceed five consecutive years for Trust I and Trust II.

The subordinated debentures may be included in Tier I capital (with certain limitations applicable) under current regulatory guidelines and interpretations. The subordinated debentures for Trust I have a variable rate of interest equal to the three month London Interbank Offered Rate (LIBOR) plus 1.50%, which was 1.74% at year-end 2014 and 2013. The subordinated debentures for Trust II have a variable rate of LIBOR plus 1.63%, which was 1.87% at year-end 2014 and 2013.

As of year-end 2014, the Company has multiple notes payable. The outstanding balance for one note payable was $274 as of year-end 2014. The outstanding balance accrues interest at 3.50%. Interest is due quarterly and the loan matures June 30, 2016. The loan is secured by stock of the Bank. The company has three additional loans to the major shareholders from the acquisition of Peoples Security Bank. The outstanding balance for these loans was $3,239 as of year-end 2014. The outstanding balance accrues interest at 3.25%. Principal and interest is due quarterly and the loans mature March 31, 2019. The principal payments for these loans will be $762 in 2015, 2016, 2017, and 2018 and $191 in 2019. The loans are secured by a letter of credit for $3,239 with another financial institution with an interest rate of 3.50%. These notes were issued in 2014.

As of year-end 2013, the Company had a note payable with an outstanding balance of $1,000. The outstanding balance accrued interest at prime (3.25% rate at December 31, 2013). This note was paid off during 2014.

NOTE 10 – EMPLOYEE BENEFIT PLANS

Citizens National Bank provides a 401(k) retirement plan for its employees which matches employee contributions at 100% for the first 1% then at 50% for the next 5% up to a maximum of 6% of salary. Expense for the 401(k) plan was $198 and $186 for 2014 and 2013.

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 10 – EMPLOYEE BENEFIT PLANS (Continued)

Deferred Compensation Plans: The Company maintains a deferred compensation plan for its directors and executive officers. Under the director plan, the directors may elect to defer their compensation until termination of service. The fees deferred are invested by the Bank at the discretion of the director. Upon termination of service, the director or their beneficiary is paid the amount deferred (plus or minus accumulated earnings or losses) over 10 years. The expense incurred for the director plan was $51 and $48 for 2014 and 2013, and resulted in deferred compensation assets and liabilities of $817 and $777 as of year-end 2014 and 2013. The executive plan covers four executives and provides for a retirement benefit for periods ranging from 15-20 years following their retirement. The expense incurred for the executive plan for each of the last two years was $177 and $373 and resulted in a liability of $3,349 and $3,391 as of year-end 2014 and 2013.

NOTE 11 – INCOME TAXES

The income tax expense (benefit) was as follows:

	2014	2013
Current	$ 263	$ 376
Valuation allowance	(6)	(25)
Deferred	221	77
Total	$ 478	$ 428

Effective tax rates differ from federal statutory rate of 34% applied to income before income taxes due to the following:

	2014	2013
Federal statutory rate times financial statement income	34%	34%
Effect of:		
Tax-exempt income	(9.92)	(13.41)
State taxes, net of federal benefit	.24	.53
Earnings from company owned life insurance	(1.22)	(1.78)
Bargain purchase gain	(10.94)	-
Deferred compensation benefit with split dollar life insurance	(.22)	(2.61)
General Business Credits	(4.40)	(6.41)
Change in valuation allowance	(.10)	(.05)
Other, net	.74	.40
Total	8.18 %	10.67%

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Notes to Consolidated Financial Statements

Years ended December 31, 2014 and 2013
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NOTE 11 – INCOME TAXES (Continued)

Deferred tax assets and liabilities at year-end consist of:

	2014	2013
Deferred tax assets:		
Loan loss provisions	$ 1,229	$ 1,308
Core deposit intangible and other purchase accounting adjustments	-	204
Deferred compensation	1,385	1,401
Net operating loss carryforward	1,055	1,034
Nonaccrual loan interest	85	120
Accrued expenses	166	89
Other real estate owned	85	119
Capital loss carryforward	10	16
Credit carryforward	362	362
Unrealized loss on available for sale securities	-	429
Other	4	1
	4,381	5,083
Deferred tax liabilities:		
Depreciation	(273)	(333)
Core deposit intangible and other purchase accounting adjustments	(342)	-
Accretion on securities	(18)	(16)
Federal Home Loan Bank stock dividends	(327)	(291)
Unrealized gain on available for sale securities	(1,052)	-
Other	(125)	(73)
	(2,137)	(713)
Valuation allowance	(10)	(16)
Net deferred tax asset	$ 2,234	$ 4,354

The Company recorded a valuation allowance on the deferred tax asset related to capital losses that are not more likely than not to be realized. No valuation allowance for any remaining deferred tax assets is considered necessary. At year end 2014 and 2013, the Company had net operating loss carryovers from previous and current year acquisitions of approximately $3,104 and $3,043 which expires beginning in 2023. The utilization of the net operating loss carryforward is limited to $435 annually under code section 382. The portion of the net operating loss carryforward that will expire before utilization is not carried as a deferred tax asset.

The Company has no unrecognized tax benefits as of December 31, 2014. The Company does not expect the total amount of unrecognized tax benefits to significantly increase in the next twelve months. Should the accrual of any interest or penalties relative to unrecognized tax benefits be necessary, it is the Company's policy to record such accruals in its income tax expense accounts; no such accruals existed as of December 31, 2014. The Company and its subsidiaries file a U.S. Corporation federal income tax return, a West Virginia Corporation income tax return, and a Kentucky Corporation income tax return. These returns are subject to examination by taxing authorities for all years after 2009.

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Notes to Consolidated Financial Statements

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NOTE 12 – LOAN COMMITMENTS AND OTHER RELATED ACTIVITIES

Some financial instruments, such as loan commitments, credit lines, letters of credit, and overdraft protection, are issued to meet customer-financing needs. These are agreements to provide credit or to support the credit of others, as long as conditions established in the contract are met, and usually have expiration dates. Commitments may expire without being used. Off-balance-sheet risk to credit loss exists up to the face amount of these instruments, although material losses are not anticipated. The same credit policies are used to make such commitments as are used for loans, including obtaining collateral at exercise of the commitment.

Letters of credit are financial instruments considered financial guarantees under accounting guidance.

The contractual amount of financial instruments with off-balance-sheet risk was as follows at year-end:

	2014	2013
Commitments to make loans	$ 32,320	$ 21,088
Unused lines of credit	16,623	13,500
Letters of credit	5,400	5,538

At year-end 2014 and 2013, reserves of $8,429 and $8,740 were required as deposits with the Federal Reserve or as cash on hand.

NOTE 13 – EARNINGS PER SHARE

Basic earnings per share was computed as follows.

	2014	2013
Net income	$ 5,363	$ 3,579
Average common shares outstanding (in thousands)	1,117	1,126
Basic earnings per share	$ 4.80	$ 3.18

NOTE 14 – CAPITAL REQUIREMENTS AND RESTRICTIONS ON RETAINED EARNINGS

Banks and bank holding companies are subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. Management believes as of December 31, 2014, the Company and Bank meet all capital adequacy requirements to which they are subject.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At year-end 2014 and 2013, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt

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NOTE 14 – CAPITAL REQUIREMENTS AND RESTRICTIONS ON RETAINED EARNINGS (Continued)

corrective action. There are no conditions or events since that notification that management believes have changed the institution's category.

Actual and required capital amounts (in millions) and ratios are presented below at year-end.

	Actual		Required For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Regulation	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
2014						
Total capital to risk weighted assets						
Consolidated	$ 60.2	17.8%	$ 27.1	8.0%	N/A	N/A
Bank	62.3	18.5	27.0	8.0	$ 33.8	10.0%
Tier 1 (core) capital to risk weighted assets						
Consolidated	$ 54.6	16.1%	$ 13.5	4.0%	N/A	N/A
Bank	58.7	17.4	13.5	4.0	$ 20.3	6.0%
Tier 1 (core) capital to average assets						
Consolidated	$ 54.6	10.8%	$ 20.1	4.0%	N/A	N/A
Bank	58.7	11.7	20.1	4.0	$ 25.1	5.0%
2013						
Total capital to risk weighted assets						
Consolidated	$ 57.1	18.1%	$ 25.3	8.0%	N/A	N/A
Bank	55.7	17.7	25.2	8.0	$ 31.5	10.0%
Tier 1 (core) capital to risk weighted assets						
Consolidated	$ 50.0	15.8%	$ 12.6	4.0%	N/A	N/A
Bank	51.8	16.5	12.6	4.0	$ 18.9	6.0%
Tier 1 (core) capital to average assets						
Consolidated	$ 50.0	9.6%	$ 20.8	4.0%	N/A	N/A
Bank	51.8	10.0	20.8	4.0	$ 26.0	5.0%

Dividends Restrictions – The Company's principal source of funds for dividend payments is dividends received from the Bank. Banking regulations limit the amount of dividends that may be paid without prior approval of regulatory agencies. Under these regulations, the amount of dividends that may be paid in any calendar year is limited to the current year's net profits, combined with the retained net profits of the preceding two years, subject to the capital requirements described above. During 2015, the Bank could, without prior approval, declare dividends of approximately $2,667 plus any 2015 net profits retained to date of the dividend declaration.

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NOTE 15 – DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

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

> Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.
>
> Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
>
> Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Securities: The fair values of securities available for sale are determined by obtaining matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs).

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

Other Real Estate Owned: Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

Appraisals for both collateral-dependent impaired loans and other real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Company. Once received, a credit review specialist reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics.

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NOTE 15 – DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Assets and Liabilities Measured on a Recurring Basis

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

	Fair Value Measurements at December 31 Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
2014			
Assets:			
Available for sale securities:			
U.S. Government and federal agencies	$ -	$ 5,894	$ -
States and municipals	-	59,538	-
U.S. Government sponsored entity mortgage backed securities: residential	-	109,165	-
Other securities	-	2,499	-
Total	$ -	$ 177,096	$ -
2013			
Assets:			
Available for sale securities:			
U.S. Government and federal agencies	$ -	$ 9,517	$ -
States and municipals	-	50,862	-
U.S. Government sponsored entity mortgage backed securities: residential	-	115,263	-
Other securities	-	2,476	-
Total	$ -	$ 178,118	$ -

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NOTE 15 – DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Assets measured at fair value on a non-recurring basis are summarized below:

	Fair Value Measurements at December 31, Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
2014			
Impaired loans:			
Commercial	$ -	$ -	$ -
Real estate:			
Residential real estate	-	-	214
OREO:			
Real estate:			
Commercial real estate	$ -	$ -	$ 427
Construction and land development	-	-	5
Residential real estate	-	-	1,275
2013			
Impaired loans:			
Commercial	$ -	$ -	$ 62
Real Estate:			
Residential real estate	-	-	1,397
OREO:			
Real estate:			
Commercial real estate	$ -	$ -	$ 692
Residential real estate	-	-	1,270

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a carrying amount of $521, with a valuation allowance of $307 at December 31, 2014, resulting in an additional provision for loan losses of $86 for the year ended December 31, 2014. Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a carrying amount of $2,415, with a valuation allowance of $956 at December 31, 2013, resulting in an additional provision for loan losses of $173 for the year ended December 31, 2013.

Other real estate owned measured at fair value less costs to sell, had a net carrying amount of $1,707, which is made up of the outstanding balance of $1,908, net of a valuation allowance of $201 at December 31, 2014, resulting in a charge of $145 for the year ended December 31, 2014. Other real estate owned measured at fair value less costs to sell, had a net carrying amount of $1,962, which is made up of the outstanding balance of $2,281, net of a valuation allowance of $319 at December 31, 2013, resulting in a charge of $223 for the year ended December 31, 2013.

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NOTE 15 – DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Carrying amount and estimated fair values of financial instruments were as follows at year-end:

	2014		2013	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets:				
Cash and due from financial institutions	$ 17,343	$ 17,343	$ 12,490	$ 12,490
Federal Funds Sold	4,000	4,000	11,000	11,000
Interest bearing deposits in Other financial institutions	15,397	15,397	6,950	6,950
Securities available for sale	177,096	177,096	178,118	178,118
Loans held for sale	214	221	209	212
Loans, net	299,656	302,433	270,719	269,652
Restricted securities	4,060	N/A	3,887	N/A
Accrued interest receivable	1,604	1,604	1,621	1,621
Financial liabilities:				
Deposits	$ 456,413	$ 457,448	$ 422,999	$ 424,989
Federal funds purchased, repurchase agreement and note payable	11,211	11,211	19,383	19,433
FHLB advances	16,711	17,740	16,500	18,120
Subordinated debentures	16,000	7,689	16,000	7,523
Accrued interest payable	263	263	307	307

The methods and assumptions used to estimate fair values are described as follows. The carrying value is considered to estimate fair value for cash and cash equivalents, accrued interest receivable and payable, demand and savings deposits, short-term borrowings and variable rate loans and deposits that reprice fully and frequently. It is not practicable to determine the fair value of FHLB and FRB stock due to restrictions placed on its transferability. The fair value for loans and certificates of deposits are based on estimates of discounted cash flow analysis using current market rates for the estimated life and credit risk. The fair value of debt is based on current rates for similar financing. The fair value of off balance sheet items is not considered material.

NOTE 16 – BUSINESS COMBINATION

On December 22, 2014, the Company acquired 100% of the outstanding common shares of Peoples Security Bancorp ("PSBI") in exchange for cash of $3,240 and notes payable of $3,239. Bank results of operations were included in the Company's results beginning December 23, 2014. The company acquired PSBI to strengthen and expand its market presence in Lawrence County, Kentucky. Acquisition-related costs of $173 are included in other in the Company's income statement for the year ended December 31, 2014.

The following table summarizes the consideration paid for Peoples Security Bancorp, Inc. and the amounts of assets acquired and liabilities assumed recognized at the acquisition date:

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NOTE 16 – BUSINESS COMBINATION (Continued)

Consideration	
Cash	$ 3,240
Notes Payable	3,239
Fair value of total consideration transferred	$ 6,479
Recognized amounts of identifiable assets acquired and liabilities assumed	
Cash and cash equivalents	$ 12,251
Securities	16,194
Federal Home Loan Bank Stock	173
Loans	19,009
Premises and equipment	1,750
Core deposit intangibles	734
Real estate owned	358
Other assets	288
Total assets acquired	50,757
Deposits	41,500
Federal Home Loan Bank advances	211
Other liabilities	687
Total liabilities assumed	42,398
Total identifiable net assets (liabilities)	8,359
Bargain Purchase Gain	$ (1,880)

The fair value of net assets acquired includes fair value adjustments to certain receivables that were not considered impaired as of the acquisition date. The fair value adjustments were determined using discounted contractual cash flows. However, the Company believes that all contractual cash flows related to these financial instruments will be collected. As such, these receivables were not considered impaired at the acquisition date and were not subject to the guidance relating to purchased credit impaired loans, which have shown evidence of credit deterioration since origination. Receivables acquired that were not subject to these requirements include non-impaired loans and customer receivables with a fair value and gross contractual amounts receivable of $17,863 and $18,131 on the date of acquisition.

NOTE 17 – ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following is changes in accumulated other comprehensive income (loss) by component, net of tax, for the years ending December 31, 2014 and 2013:

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NOTE 17 – ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS) (Continued)

	Unrealized Gains And Losses on Available-For-Sale Securities December 31, 2014	Unrealized Gains and Losses on Available-For-Sale Securities December 31, 2013
Beginning balance	$ (833)	$ 3,415
Other comprehensive income Before reclassification	2,993	(4,160)
Amounts reclassified from accumulated other comprehensive income	(93)	(88)
Net current period other comprehensive income	2,900	(4,248)
Ending balance	$ 2,067	(833)

The following is significant amounts reclassified out of each component of accumulated other comprehensive income (loss) for the year ending December 31, 2014:

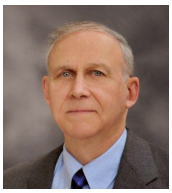
Details about Accumulated Other Comprehensive Income Components	Amount Reclassified From Accumulated Other Comprehensive Income	Affected Line Item in the Statement Where Net Income is Presented
Unrealized gains and losses on securities available for sale	$ 141	Net gain (losses) on sale of securities
	(48)	Tax (expense) or benefit
	$ 93	Net of tax

The following is significant amounts reclassified out of each component of accumulated other comprehensive income (loss) for the year ending December 31, 2013:

Details about Accumulated Other Comprehensive Income Components	Amount Reclassified From Accumulated Other Comprehensive Income	Affected Line Item in the Statement Where Net Income is Presented
Unrealized gains and losses on securities available for sale	$ 133	Net gain (losses) on sale of securities
	(45)	Tax(expense) or benefit
	$ 88	Net of tax

Board of Directors

Gregory Meade

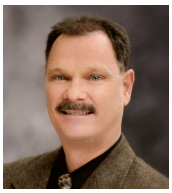


Chairman of the Board. Elected to the CNC Board on April 15, 1991, Meade is President of Gregory J Meade Insurance, Inc., of Paintsville. He is the Chairman of the Johnson County Soil Conservation District, Chairman of the Johnson County Extension Council, Secretary and Treasurer of the Johnson County Farm Bureau, and past member of the Paintsville/Prestonsburg Airport Board.

V. Burton Bellamy

A board member since the fall of 2013, Bellamy has been a community banker in eastern Kentucky since 1979, serving at the Executive level for over 30 years; having previously served as a director for three banks and two holding companies accumulating over 25 years at the Director Level. Prior to his banking career he served in the Air Force and Army. A graduate of Eastern Kentucky University's College of Law Enforcement and receiving his MBA degree from Morehead State University. Bellamy serves on boards or steering committees of Johnson-Paintsville Chamber of Commerce, Mountain Comprehensive Care Corporation, and Johnson County Community of Hope. A native of Breathitt County, he and his wife, Linda Kaye, reside in Paintsville and are members of the First Baptist Church.

Paul David Brown, Jr.

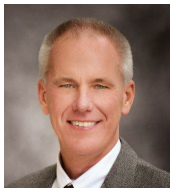


Elected to the Board of Directors in 2008, Paul David is the CEO, Pres., of Redd, Brown & Williams Real Estate Services where he has been employed since 1980. He is married to Cathy Thomas Brown and they have two children, Jennifer Brown of Pikeville, KY & Rachael Melvin of Paintsville, KY. Paul David is a Certified General Appraiser, Principle Real Estate Broker, and Principle Auctioneer. He is also a Nationally Certified AQB Uniform Standards of Professional Appraisal Practice Instructor and has earned the GAA, IFAS, CERS professional designations. He also is a certified real estate and appraisal instructor, has a BBA from Eastern Kentucky University where he was also a four year baseball letterman. Paul David is a member of St Michael's Catholic Church where he serves as an Ordained Permanent Deacon as well as serving on Finance Council, Building & Grounds Committee and other committees.

Larry Conley

A CNC Board member since August 1992, Conley has been a sports announcer for various stations including CBS, NBC, ABC, Fox Television and ESPN. He was also a former manager for both General Electric Credit and Converse Rubber Co. He played basketball for the University of Kentucky Basketball program and played professionally for the Kentucky Colonels.

Robin Cooper



A member of the CNC Board since April 1983, Robin is a former Mayor of the City of Paintsville. During his tenure he was elected President of the Kentucky League of Cities and served as Chairman of the Kentucky Law Enforcement Council for several years. He retired from the periodical and newspaper business in 1998 and is currently employed as the Chief Member Services Officer for the Kentucky League of Cities.

Barrett Frederick

A member of the CNC Board since April 1986, Frederick is President of Rifle Coal Company, a highway contracting company. He holds a Juris Doctorate degree from the University of Louisville and practiced law from 1974 until 1980 in the West Liberty area. He is a member of the Morgan County ARH Advisory Committee. Also, he is a managing partner of Winwoods Farm in Georgetown, a thoroughbred horse breeding operation.

Bob Hutchison

A Board Member since April 1991. Hutchison currently co-owns 14 McDonald's restaurants throughout East Kentucky. He is President/CEO of Hutch Chevy-Buick-GMC dealership and Hutch Chrysler-Dodge-Jeep-Ram dealership in Paintsville. He received his Bachelor of Science degree in Business and is a member of the First United Methodist Church in Paintsville. He is a Board Member of Christian Appalachian Project, Chairman of the Johnson County School System, a Trustee of Midway College, a Trustee of The University of Pikeville, and a member of Leadership Kentucky. He is also President of Rock house Volunteer Fire Department, an Executive Board Member of The Bluegrass Council for Boy Scouts of America, and serves on the Board of Commercial Bank of West Liberty.

Lisa M. Johnson

Lisa is the newest member of the Board being elected in April 2014. She is a graduate of the University of Pikeville with a Bachelor of Business Administration with emphasis in Accounting. She is married to attorney, Michael Fleet Johnson, of Pikeville. She owns rental properties and does the accounting for several personal businesses. She is a long-time member of the First Baptist Church of Pikeville where she serves on the New Building and College committees among others.

Lynn Dorton Mullins

Board Member since April 1994. Mullins recently retired as owner and service provider of Lynn Mullins Speech Therapy Services. She received her BA and MA from the University of Kentucky in Speech Pathology. She is a member of the American Speech and Hearing Association and the Kentucky Speech-Language Hearing Association. Mullins is a member of the First United Methodist Church in Paintsville where she serves on the board and is a trustee and a member of the Wesleyan Service Guild. She is also a member of Beta Sigma Phi Service Sorority and Paintsville High School Alumni Association (PHSAA).

Marvin Butch Walker

A CNC Board Member since the fall of 2005, Walker has been a licensed practicing attorney in the Eastern District of Kentucky for more than 30 years. He is a graduate of the University of Kentucky Colleges of Engineering and Law. For several years, a significant part of his law practice has included serving as a consultant to his wife, Kathy E. Walker, the President and CEO of Elm Street Resources, Inc. Formerly, Walker was associated with the Paintsville law firm of Wells, Porter, Schmitt, and Walker (now Porter, Schmitt, Banks, and Baldwin). He remains a long-standing member of the Paintsville Independent Board of Education.

Senior Management Team & Executive Committee

V. Burton Bellamy
President/CEO

Lee Wilson
Executive Vice President/CCO

Ben D. Tackett, Jr.
Executive Vice President/CLO

Darren Gillespie
SVP/Business Banking

Pam Butcher
SVP/Retail Banking

Jim Hobbs
SVP/Market President

Kathy M. Kinner
SVP/Human Resources

Leisha Maynard
SVP/CFO

Jason Suman
SVP/Market President

Rose M. Wheeler
SVP/Information Systems Operations Manager

Chase Caudill
VP/Wealth Management

SENIOR MANAGEMENT TEAM

Jim Hobbs, Leisha Maynard, Darren Gillespie, Rose Wheeler, Lee Wilson, V. Burton Bellamy, Ben D. Tackett, Jr., Pam Butcher, Chase Caudill, Kathy Kinner, Jason Suman

Directors Emeriti

Paul D. Brown
was elected to the Board of Directors April 1970, where he served for 38 years before retiring in April 2008.

Citizens National Bank Market Advisory Boards

Southern

Kenny Blackburn

Gary Branham

Randy Clark

Paul Preston

Officers, Citizens National Corporation

Gregory Meade
Chairman of the Board

V. Burton Bellamy
President/CEO

Leisha Maynard, CPA
SVP/CFO/Treasurer

Sharon Collins
Corporate Secretary

Executive Officers, Citizens National Bank

V. Burton Bellamy
President/CEO

Lee Wilson
Executive Vice President/CCO

Ben D. Tackett, Jr.
Executive Vice President/CLO

Officers

Pam Butcher
SVP /Retail Banking

Darren Gillespie
SVP/Business Banking

Jim Hobbs
SVP/ Market President

Kathy Kinner
SVP/Human Resources

Leisha Maynard
SVP/CFO

Jason Suman
SVP/ Market President

Rose M. Wheeler
SVP/Information Systems/Operations Manager

Patty Adams
VP/Branch Operations

Chase Caudill, CTFA, CFB
CTFA, CFP - VP/Wealth Management and Trust

Paula Chandler
VP/Senior Compliance Officer

Todd Dials
VP/AOC Manager

Debra Fazenbaker
VP/ Business Development/Branch Support

Judy Frazier
VP/Branch Manager

Johnene Holbrook
VP/Auditor

Joyce Lemaster
VP/Branch Manager

Amy Lyons
VP/Senior Credit Analyst

Rita Parker
VP/Branch Manager

Michelle Powers
VP/Credit Operations Supervisor

Dave Simpson
VP/Security Officer/BSA Officer

Grady Underwood
VP/Mortgage Originator

Joyce Castle
AVP/Treasurer

Donna Cassell
AVP/Human Resources Specialist

Melissa A. Castle
AVP/Assistant Branch Manager

Sharon Collins
AVP/Executive Administrative Assistant/ Insurance Administrator

Daniel Cornette
AVP/Mortgage Originator

Tyler Crum
AVP/Business Banking Officer

April Damron
AVP/Branch Manager

Beverly Gibbs
AVP/Branch Manager

Jim Moore
AVP/Financial Consultant

John Moore
AVP/Information Systems Manager

Cody Prater
AVP/Branch Manager

George Prater
AVP/Branch Manager

Jon Rose
AVP/Loan Compliance/ CRA Officer

Stephanie Salyer
AVP/Problem Resolution/Training Manager

Carolyn Sisco
AVP/AOC Assistant Manager

Joey Stambaugh
AVP/Special Assets Officer

Misty Jenkins
AVP/Branch Manager

Brandi Vanhoose
AVP /Controller

Jarrod Adkins
Branch Manager

Brandon Feltner
Business Banking Officer

Mitzie Heaberlin
Branch Manager

Focus on Communities

Citizens continues to honor its responsibility to the communities we serve. Whether donating time, money or both, Citizens National Bank and its employees contribute to the well being of the people of the eight counties we serve. Citizens National Bank supports a variety of organizations in education, historical preservation, the arts, our youth, health care and economic development. Here are some that have benefited from our contributions.

History & the Arts

Jenny Wiley Theatre
Kentucky Historical Society
Mountain Arts Center
Paramount Arts Center
Paramount Women's Association

Youth & Education

Ashland Community and Technical College
Big Brothers & Big Sisters of the Tri-State
Boy Scouts of America
East Kentucky Science Center
4-H
Girl Scouts of America
Kentucky Christian University
Kentucky Governor's Scholars
Leadership East Kentucky
Leadership Kentucky
Morehead State University Small Business Awards
Morehead State University Women's Symposium
Paul B. Hall Scholarship Fund
Pikeville College Scholarship
Project Proms
School Sports Sponsorships
UNITE Program
University of Kentucky
University of Kentucky Robinson Scholar
University of Pikeville

Economic Development

Ashland Alliance
Big Sandy Area Development District
Floyd County Chamber of Commerce
Grayson Chamber of Commerce
Main Street Associations
Paintsville/Johnson County Chamber of Commerce
Southeast Kentucky Chamber of Commerce

Community & Health

American Cancer Society
Ashland Community Kitchen
CAReS
CASA
Christian Appalachian Project
Clean Start
For Jamie's Sake
Habitat for Humanity
Highlands Center for Autism
Highlands Foundation
Highlands Museum and Discovery Center
Hope in the Mountains
Hope's Place
Judi's Place for Kids
Kentucky Apple Festival
Kiwanis
Mountain Comprehensive Care
Our Lady of Bellefonte Hospital Foundation
Pathways
Pike County Humane Society
Pike County YMCA
Red Cross
River Cities Harvest
Rotary
Safe Harbor
Special Olympics
Summer Motion Ashland
United Way

Fight against Polio

Judi's Place Event

Main Office and Wealth Management staff a.k.a. Smurf Village showing the customers and the community fun in October 2014

Jarrod Adkins was fourth in the 5K Run and first in his age division

God's Pantry donation

Southern Region Relay for Life

CNB H.O.M.E.S. Team

Read to Children Day at WR Castle Elementary Caroleene Gambill , Assistant Branch Manager Mayo Plaza

Carolyn and Sandra Baldridge Shareholders Meeting 2014

Ashland Business After Hours 2014

Citizens NATIONAL CORPORATION

Citizens
NATIONAL CORPORATION

620 Broadway
Paintsville, Kentucky 41240
cnbonline.com