LCNB CORP
Form 10-K
March 09, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)
x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2015
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ______________________ to _____________________

Commission File Number 000-26121

LCNB Corp.

(Exact name of registrant as specified in its charter)

Ohio	31-1626393
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

2 North Broadway, Lebanon, Ohio 45036
(Address of principal executive offices, including Zip Code)

(513) 932-1414
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Exchange Act:

Title of Each Class	Name of each exchange on which registered
None	None

Securities registered pursuant to 12(g) of the Exchange Act:

COMMON STOCK, NO PAR VALUE
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
o Yes x No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
o Yes x No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes o No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
x Yes o No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

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

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

The aggregate market value of the registrant's outstanding voting common stock held by nonaffiliates on June 30, 2015, determined using a per share closing price on that date of $16.20 as quoted on the NASDAQ Capital Market, was $154,224,000.

As of March 8, 2016, 9,905,147 common shares were issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement included in the Notice of Annual Meeting of Shareholders to be held April 26, 2016, which Proxy Statement will be mailed to shareholders within 120 days from the end of the fiscal year ended December 31, 2015 are incorporated by reference into Part III.

LCNB CORP.
For the Year Ended December 31, 2015

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PART I

Item 1. Business

FORWARD-LOOKING STATEMENTS

Certain statements made in this document regarding LCNB's financial condition, results of operations, plans, objectives, future performance and business, are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995. These forward-looking statements are identified by the fact they are not historical facts and include words such as "anticipate", "could", "may", "feel", "expect", "believe", "plan", and similar express

These forward-looking statements reflect management's current expectations based on all information available to management and its knowledge of LCNB's business and operations. Additionally, LCNB's financial condition, results of operations, plans, objectives, future performance and business are subject to risks and uncertainties that may cause actual results to differ materially. These factors include, but are not limited to:

1. the success, impact, and timing of the implementation of LCNB's business strategies, including the successful integration of recently completed and pending acquisitions;
2. LCNB may incur increased charge-offs in the future;
3. LCNB may face competitive loss of customers;
4. changes in the interest rate environment may have results on LCNB's operations materially different from those anticipated by LCNB's market risk management functions;
5. changes in general economic conditions and increased competition could adversely affect LCNB's operating results;
6. changes in other regulations and government policies affecting bank holding companies and their subsidiaries, including changes in monetary policies, could negatively impact LCNB's operating results;
7. LCNB may experience difficulties growing loan and deposit balances;
8. the current economic environment poses significant challenges for us and could adversely affect our financial condition and results of operations;
9. deterioration in the financial condition of the U.S. banking system may impact the valuations of investments LCNB has made in the securities of other financial institutions resulting in either actual losses or other than temporary impairments on such investments; and
10. the effects of the Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and the regulations promulgated and to be promulgated thereunder, which may subject LCNB and its subsidiaries to a variety of new and more stringent legal and regulatory requirements which adversely affect their respective businesses.

Forward-looking statements made herein reflect management's expectations as of the date such statements are made. Such information is provided to assist shareholders and potential investors in understanding current and anticipated financial operations of LCNB and is included pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. LCNB undertakes no obligation to update any forward-looking statement to reflect events or circumstances that arise after the date such statements are made.

DESCRIPTION OF LCNB CORP.'S BUSINESS

General Description

LCNB Corp., an Ohio corporation formed in December 1998, is a financial holding company headquartered in Lebanon, Ohio. Substantially all of the assets, liabilities and operations of LCNB Corp. are attributable to its wholly-owned subsidiary, LCNB National Bank (the "Bank"). LCNB Corp. and its subsidiary are herein collectively referred to as "LCNB." The predecessor of LCNB Corp., the Bank, was formed as a national banking association in 1877. On May 19, 1999, the Bank became a wholly-owned subsidiary of LCNB Corp.

On January 11, 2013, LCNB consummated a merger with First Capital Bancshares, Inc. (“First Capital”) in a stock and cash transaction valued at approximately $20.2 million. Immediately following the merger of First Capital into LCNB, Citizens National Bank (“Citizens National”), a wholly-owned subsidiary of First Capital, was merged into LCNB National Bank. At that time, Citizens National’s six full–service offices became offices of LCNB. Three of these offices are located in Chillicothe, Ohio and one office is located in each of Frankfort, Ohio, Clarksburg, Ohio, and Washington Court House, Ohio.

On January 24, 2014, LCNB purchased all of the outstanding stock of Eaton National Bank & Trust Co. ("Eaton National") from its holding company, Colonial Banc Corp., in a cash transaction totaling $24.75 million. Upon consummation of the transaction, Eaton National was merged into the Bank and its five offices became offices of the Bank. Two of these offices are located in Eaton, Ohio and one office is located in each of New Paris, Ohio, Lewisburg, Ohio, and West Alexandria, Ohio.

On April 30, 2015, LCNB consummated a merger with BNB Bancorp, Inc. (“BNB”) in a stock and cash transaction valued at approximately $13.5 million. Immediately following the merger of BNB into LCNB, Brookville National Bank ("Brookville National"), a wholly-owned subsidiary of BNB, was merged into LCNB National Bank. At that time, Brookville National's two offices, both located in Brookville, Ohio, became offices of LCNB.

At February 29, 2016, the Bank had 36 offices, including a main office in Warren County, Ohio and branch offices in Warren, Butler, Clinton, Clermont, Hamilton, Montgomery, Preble, Ross, and Fayette Counties, Ohio, and 40 automated teller machines ("ATMs").

The Bank is a full service community bank offering a wide range of commercial and personal banking services. Deposit services include checking accounts, NOW accounts, savings accounts, Christmas and vacation club accounts, money market deposit accounts, Lifetime Checking accounts (a senior citizen program), individual retirement accounts, and certificates of deposit. Additional supportive services include online banking, bill pay, mobile banking and telephone banking. Commercial customers also have both cash management and remote deposit capture products as potential options. Deposits of the Bank are insured up to applicable limits by the Deposit Insurance Fund, which is administered by the Federal Deposit Insurance Corporation (the “FDIC”).

Loan products offered include commercial and industrial loans, commercial and residential real estate loans, agricultural loans, construction loans, various types of consumer loans, and Small Business Administration loans. The Bank's residential mortgage lending activities consist primarily of loans for purchasing or refinancing personal residences, home equity lines of credit, and loans for commercial or consumer purposes secured by residential mortgages. Most fixed-rate residential real estate loans are sold to the Federal Home Loan Mortgage Corporation with servicing retained. Consumer lending activities include automobile, boat, home improvement and personal loans. The Bank also offers indirect financing through various automotive, boat, and lawn and garden dealers.

The Trust and Investment Management Division of the Bank performs complete trust administrative functions and offers agency and trust services, retirement savings products, and mutual fund investment products to individuals, partnerships, corporations, institutions and municipalities.

Security brokerage services are offered by the Bank through arrangements with LPL Financial LLC, a registered broker/dealer. Licensed brokers offer a full range of investment services and products, including financial needs analysis, mutual funds, securities trading, annuities, and life insurance.

Other services offered include safe deposit boxes, night depositories, cashier's checks, bank-by-mail, ATMs, cash and transaction services, debit cards, wire transfers, electronic funds transfer, utility bill collections, notary public service, personal computer-based cash management services, 24 hour telephone banking, PC Internet banking, mobile banking, and other services tailored for both individuals and businesses.

The Bank is not dependent upon any one significant customer or specific industry. Business is not seasonal to any material degree.

The address of the main office of the Bank is 2 North Broadway, Lebanon, Ohio 45036; telephone (513) 932-1414.

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LCNB CORP. AND SUBSIDIARIES

Market Area

LCNB's primary market area consists of Warren, Butler, Clinton, Preble, Ross, and Fayette Counties and portions of Hamilton, Clermont, and Montgomery Counties in Southwestern and South Central Ohio. Certain demographic information is as follows:

	Warren	Butler	Clinton	Preble	Ross	Fayette	Hamilton	Montgomery
Population:								
2000 census	158,383	332,807	40,543	42,337	73,345	28,433	845,303	559,062
2010 census	212,693	368,130	42,040	42,270	78,064	29,030	802,374	535,153
Percentage increase/decrease in population	34.3%	10.6%	3.0%	(0.2)%	6.4%	2.1%	(5.1)%	(4.3)%
Estimated percentage of persons below poverty level	5.9%	12.8%	14.0%	10.7%	17.5%	18.5%	15.4%	15.7%
Estimated median household income	$71,274	$54,788	$46,261	$48,899	$42,626	$39,599	$48,234	$43,965
Median age	37.0	35.7	37.7	41.0	39.5	39.3	36.9	38.7
Unemployment rate:								
December 2015	3.9%	4.2%	5.7%	4.6%	5.4%	4.7%	4.1%	4.7%
December 2014	3.9%	4.3%	6.3%	4.5%	5.4%	4.5%	4.3%	4.8%
December 2013	5.5%	6.2%	8.8%	6.4%	7.6%	5.9%	6.0%	7.0%

Once primarily a rural county (its population according to the 1950 census was only 38,505), Warren County experienced significant growth during the latter half of the twentieth century and into the twenty-first century. Many people who now live in Warren County are employed by companies located in the Cincinnati and Dayton metropolitan areas. A sizable tourist industry that includes King's Island, the Beach Waterpark, and the Ohio Renaissance Festival provides a number of temporary summer jobs. Not including local government entities and school districts, which are significant sources of employment, the top five major employers in Warren County are Macy's Credit and Customer Service, Procter & Gamble's Mason Business Center, Atrium Health Center Mason, WellPoint (health insurance), and Luxottica.

Butler County was historically a rural area with the exception of three urban centers. Hamilton and Middletown were both manufacturing centers. As is true with many manufacturing communities in the Midwest, many of the manufacturing companies in Hamilton and Middletown have either closed or greatly diminished their workforces and these jobs have been largely replaced with lower-paying service oriented jobs. Oxford is the home of Miami University and Oxford's businesses primarily serve the college students.

Most of the growth in Butler County has occurred in West Chester, Liberty, and Fairfield Townships. Many of the people living in these townships are employed by companies located in the Cincinnati metropolitan area. Not including local government entities and school districts, the top five major employers in Butler County are Miami University, AK Steel, Cincinnati Financial Corp. (insurance), GE Aviation, and Liberty Mutual Group (insurance). Fort Hamilton Hospital, Mercy Hospital Fairfield, McCullough-Hyde Memorial Hospital, West Chester Hospital, Cincinnati Children's Hospital Liberty Campus, Cincinnati Children's Hospital Fairfield, and Bethesda Butler Hospital are located in Butler County and collectively are a significant source of health-related employment.

Clinton County remains mostly rural. Wilmington, with a 2010 census population of 12,520, is the largest city. The next largest is Blanchester, with a 2010 census population of 4,243. The unemployment rates for December 2013 through December 2015 are unusually high because of the loss of a dominant employer. DHL, an overnight shipping company, owned the Wilmington Air Park, a decommissioned air force base, and maintained hub operations at this location. In 2008, Wilmington Air Park discontinued operations, resulting in the direct loss of approximately 8,000 jobs, not including job losses sustained by other businesses dependent on the air park operations. Certain services subcontracted to ABX Air and ASTAR Air Cargo continue, but with greatly diminished work forces.

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Preble County is mostly rural. Eaton, with a 2010 census population of 8,407, is the only city in the county. Major employers are Neaton Auto Products Manufacturing Inc., Henny Penny Corporation, Parker-Hannifin Corporation, SILFEX, a division of Lam Research Corp., and Wal-Mart.

Ross and Fayette Counties are both primarily rural. Chillicothe, with a 2010 census population of 21,901, is the largest city in Ross County and Washington Court House, with a 2010 census population of 14,192, is the largest city in Fayette County. Not including local government entities and school districts, major employers in Ross County include Adena Regional Medical Center, Kenworth Truck Company (assembler of heavy trucks), Veterans Affairs Medical Center, P.H. Glatfelter Company (formerly Mead Corp.), the Ross Correctional Institution, and the Chillicothe Correctional Institution.

Hamilton County’s economics are dominated by Cincinnati. Fortune 500 companies with their headquarters in Hamilton County include American Financial Group, Macy's, Inc., Fifth Third Bank, The Kroger Company, The Procter & Gamble Company, and Western & Southern Financial Group. The five largest employers are The Kroger Company, The University of Cincinnati, The Procter & Gamble Company, Cincinnati Children’s Hospital Medical Center, and TriHealth Inc.

LCNB’s four offices in Montgomery County are located in the communities of Oakwood, Centerville and Brookville. Similar to Cincinnati and Hamilton County, Dayton is the largest city in Montgomery County and dominates the economic demographics of the county. The largest employer of Montgomery County residents is Wright Patterson Air Force Base, which is actually located in Greene County. Large employers located in Montgomery County include Premier Health Partners, Kettering Health Network, The Kroger Company, LexisNexis, and Sinclair Community College.

LCNB’s market area includes a portion of Clermont County primarily because of a branch office located in Goshen, Ohio. Goshen is a suburb of Cincinnati and many of its residents work in Hamilton County. Goshen’s economic demographics are similar to Hamilton County’s demographics.

Competition

The Bank faces strong competition both in making loans and attracting deposits. The deregulation of the banking industry and the wide spread enactment of state laws that permit multi-bank holding companies as well as the availability of nationwide interstate banking has created a highly competitive environment for financial services providers. The Bank competes with other national and state banks, savings and loan associations, credit unions, finance companies, mortgage brokerage firms, realty companies with captive mortgage brokerage firms, mutual funds, insurance companies, brokerage and investment banking companies, and other financial intermediaries operating in its market and elsewhere, many of whom have substantially larger financial and managerial resources.

The Bank seeks to minimize the competitive effect of other financial institutions through a community banking approach that emphasizes direct customer access to the Bank's President and other officers in an environment conducive to friendly, informed, and courteous personal services. Management believes that the Bank is well positioned to compete successfully in its primary market area. Competition among financial institutions is based upon interest rates offered on deposit accounts, interest rates charged on loans and other credit and service charges, the quality and scope of the services rendered, the convenience of the banking facilities, and, in the case of loans to commercial borrowers, relative lending limits.

Management believes the commitment of the Bank to personal service, innovation, and involvement in the communities and primary market areas it serves, as well as its commitment to quality community banking service, are factors that contribute to its competitive advantage.

Supervision and Regulation

LCNB Corp., as a financial holding company, is regulated under the Bank Holding Company Act of 1956, as amended (the "Act"), and is subject to the supervision and examination of the Board of Governors of the Federal Reserve System (the "Federal Reserve Board").

The Bank is subject to the provisions of the National Bank Act. The Bank is subject to primary supervision, regulation and examination by the Office of the Comptroller of the Currency (the "OCC"). The Bank is also subject to the rules and regulations of the Board of Governors of the Federal Reserve System and the FDIC.

LCNB Corp. and the Bank are subject to an extensive array of banking laws and regulations that are intended primarily for the protection of the customers and depositors of LCNB's subsidiary. These laws and regulations govern such areas as permissible activities, loans and investments, and rates of interest that can be charged on loans and reserves. LCNB and the Bank also are subject to general U.S. federal laws and regulations and to the laws and regulations of the State of Ohio. Set forth below are brief descriptions of selected laws and regulations applicable to LCNB and the Bank.

The Financial Reform, Recovery and Enforcement Act of 1989 ("FIRREA") provides that a holding company and its controlled insured depository institutions are liable for any loss incurred by the FDIC in connection with the default of any FDIC assisted transaction involving an affiliated insured bank or savings association.

The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") substantially revised the bank regulatory and funding provisions of the Federal Deposit Insurance Act and several other federal banking statutes. Among its many reforms, FDICIA, as amended:

1. Required regulatory agencies to take "prompt corrective action" with financial institutions that do not meet minimum capital requirements;

2. Established five capital tiers: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized;

3. Imposed significant restrictions on the operations of a financial institution that is not rated well-capitalized or adequately capitalized;

4. Prohibited a depository institution from making any capital distributions, including payments of dividends or paying any management fee to its holding company, if the institution would be undercapitalized as a result;

5. Implemented a risk-based premium system;

6. Required an audit committee to be comprised of outside directors;

7. Required a financial institution with more than $1 billion in total assets to issue annual, audited financial statements prepared in conformity with U.S. generally accepted accounting principles; and

8. Required a financial institution with more than $1 billion in total assets to document, evaluate, and report on the effectiveness of the entity's internal control system and required an independent public accountant to attest to management's assertions concerning the bank's internal control system.

The members of an audit committee for banks with more than $1 billion in total assets must be independent of management. Only a majority, rather than all, of the members of an audit committee for banks with total assets between $500 million and $1 billion must be independent. FDICIA does not relieve financial institutions that are public companies, such as LCNB, from internal control reporting and attestation requirements or audit committee independence requirements prescribed by the Sarbanes-Oxley Act of 2002 (see below).
The Gramm-Leach-Bliley Act, which amended the Bank Holding Company Act of 1956 and other banking related laws, was signed into law on November 12, 1999. The Gramm-Leach-Bliley Act repealed certain sections of the

Glass-Steagall Act and substantially eliminated the barriers separating the banking, insurance, and securities industries. Effective March 11, 2000, qualifying bank holding companies could elect to become financial holding companies. Financial holding companies have expanded investment powers, including affiliating with securities and insurance firms and engaging in other activities that are "financial in nature or incidental to such financial activity," as defined in the act, or "complementary to a financial activity."

The Sarbanes-Oxley Act of 2002 ("SOX") became effective on July 30, 2002. The purpose of SOX is to strengthen accounting oversight and corporate accountability by enhancing disclosure requirements, increasing accounting and auditor regulation, creating new federal crimes, and increasing penalties for existing federal crimes. SOX directly impacts publicly traded companies, certified public accounting firms auditing public companies, attorneys who work for public companies or have public companies as clients, brokerage firms, investment bankers, and financial analysts who work for brokerage firms or investment bankers. Key provisions affecting LCNB include:

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1. Certification of financial reports by the chief executive officer ("CEO") and the chief financial officer ("CFO"), who are responsible for designing and monitoring internal controls to ensure that material information relating to the issuer and its consolidated subsidiaries is made known to the certifying officers by others within the company;
2. Inclusion of an internal control report in annual reports that include management's assessment of the effectiveness of a company's internal control over financial reporting and a report by the company's independent registered public accounting firm attesting to the effectiveness of internal control over financial reporting;
3. Accelerated reporting of stock trades on Form 4 by directors and executive officers;
4. Disgorgement requirements of incentive pay or stock-based compensation profits received within twelve months of the release of financial statements if the company is later required to restate those financial statements due to material noncompliance with any financial reporting requirement that resulted from misconduct;
5. Disclosure in a company's periodic reports stating if it has adopted a code of ethics for its CFO and principal accounting officer or controller and, if such code of ethics has been implemented, immediate disclosure of any change in or waiver of the code of ethics;
6. Disclosure in a company's periodic reports stating if at least one member of the audit committee is a "financial expert," as that term is defined by the Securities and Exchange Commission (the "SEC"); and
7. Implementation of new duties and responsibilities for a company's audit committee, including independence requirements, the direct responsibility to appoint the outside auditing firm and to provide oversight of the auditing firm's work, and a requirement to establish procedures for the receipt, retention, and treatment of complaints from a company's employees regarding questionable accounting, internal control, or auditing matters.

In addition, the SEC adopted final rules on September 5, 2002, which rules were amended in December, 2005, requiring accelerated filing of quarterly and annual reports. Under the amended rules, “large accelerated filers” includes companies with a market capitalization of $700 million or more and “accelerated filers” includes companies with a market capitalization between $75 million and $700 million. Large accelerated filers are required to file their annual reports within 60 days of year-end and quarterly reports within 40 days. Accelerated filers are required to file their annual and quarterly reports within 75 days and 40 days, respectively. These new accelerated filing deadlines were effective for fiscal years ending on or after December 15, 2005. Under the amended rules, LCNB is considered an accelerated filer.

The Federal Deposit Insurance Reform Act of 2005 and the Federal Deposit Insurance Reform Conforming Amendments Act of 2005 (collectively, the “Deposit Insurance Reform Acts”) were both signed into law during February, 2006. The provisions of the Deposit Insurance Reform Acts included:

1. Merging the Bank Insurance Fund and the Savings Association Insurance Fund into a new fund called the Deposit Insurance Fund, effective March 31, 2006;
2. Increasing insurance coverage for retirement accounts from $100,000 to $250,000, effective April 1, 2006; and
3.

Eliminating a 1.25% hard target Designated Reserve Ratio, as defined, and giving the FDIC discretion to set the Designated Reserve Ratio within a range of 1.15% to 1.50% for any given year.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") became effective on July 21, 2010. The Dodd-Frank Act includes provisions that specifically affect financial institutions and other entities providing financial services and other corporate governance and compensation provisions that will affect most public companies.

The Dodd-Frank Act established a new independent regulatory body within the Federal Reserve System known as the Bureau of Consumer Financial Protection (the "Bureau"). The Bureau has assumed responsibility for most consumer protection laws and has broad authority, with certain exceptions, to regulate financial products offered by banks and non-banks. The Bureau has authority to supervise, examine, and take enforcement actions with respect to depository institutions with more than $10 billion in assets, non-bank mortgage industry participants, and other Bureau-designated non-bank providers of consumer financial services. The primary regulator for depository institutions with $10 billion or less in assets will continue to have primary examination and enforcement authority for these institutions. The regulations enforced, however, will be the regulations written by the Bureau.

The Dodd-Frank Act directs federal bank regulators to develop new capital requirements for holding companies and depository institutions that address activities that pose risk to the financial system, such as significant activities in higher risk areas, or concentrations in assets whose reported values are based on models.

The Dodd-Frank Act permanently raised the FDIC maximum deposit insurance amount to $250,000. In addition, the Dodd-Frank Act places a floor on the FDIC's reserve ratio at 1.35% of estimated insured deposits or the comparable percentage of the assessment base.

General corporate governance provisions included in the Dodd-Frank Act include expanding executive compensation disclosures to be included in the annual proxy statement, requiring non-binding shareholder advisory votes on executive compensation at annual meetings, enhancing independence requirements for compensation committee members and any advisers used by the compensation committee, and requiring the adoption of certain compensation policies including the recovery of executive compensation in the event of a financial statement restatement.
Noncompliance with laws and regulations by bank holding companies and banks can lead to monetary penalties and/or an increased level of supervision or a combination of these two items. Management is not aware of any current significant instances of noncompliance with laws and regulations and does not anticipate any problems maintaining compliance on a prospective basis. Recent regulatory inspections and examinations of LCNB and the Bank have not disclosed any significant instances of noncompliance.
The earnings and growth of LCNB are affected not only by general economic conditions, but also by the fiscal and monetary policies of the federal government and its agencies, particularly the Federal Reserve Board. Its policies influence the amount of bank loans and deposits and the interest rates charged and paid thereon and thus have an effect on earnings. The nature of future monetary policies and the effect of such policies on the future business and earnings of LCNB and the Bank cannot be predicted.

A substantial portion of LCNB's cash revenues is derived from dividends paid by the Bank. These dividends are subject to various legal and regulatory restrictions. Generally, dividends are limited to the aggregate of current year retained net income, as defined, plus the retained net income of the two prior years. In addition, dividend payments may not reduce capital levels below minimum regulatory guidelines.

Employees

As of December 31, 2015, LCNB employed 280 full-time equivalent employees. LCNB is not a party to any collective bargaining agreement. Management considers its relationship with its employees to be very good. Employee benefit programs are considered by management to be competitive with benefit programs provided by other financial institutions and major employers within LCNB's market area.

Divestitures

In March 2011, LCNB Corp. sold Dakin Insurance Agency Inc. (“Dakin”) to an independent insurance agency and therefore its financial results are reported in the income statements as income from discontinued operations, net of tax.

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Availability of Financial Information

LCNB files unaudited quarterly financial reports on Form 10-Q, annual financial reports on Form 10-K, current reports on Form 8-K, and amendments to these reports are filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 with the SEC. Copies of these reports are available free of charge in the shareholder information section of the Bank's website, www.lcnb.com, as soon as reasonably practicable after they are electronically filed or furnished to the SEC, or by writing to:

Robert C. Haines II
Executive Vice President, CFO
LCNB Corp.
2 N. Broadway
P.O. Box 59
Lebanon, Ohio 45036

Financial reports and other materials filed by LCNB with the SEC may also be read and copied at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Information on the operation of the Public Reference Room may be obtained from the SEC by calling 1-800-SEC-0330. The SEC also maintains an internet site (www.sec.gov) that contains reports, proxy and information statements, and other information regarding registrants that file reports electronically, as LCNB does.

FINANCIAL INFORMATION ABOUT FOREIGN AND DOMESTIC OPERATIONS AND EXPORT SALES

LCNB and its subsidiary do not have any offices located in foreign countries and have no foreign assets, liabilities or related income and expense for the years presented.

STATISTICAL INFORMATION

The following tables and certain tables appearing in Item 7, Management's Discussion and Analysis present additional statistical information about LCNB Corp. and its operations and financial condition. They should be read in conjunction with the consolidated financial statements and related notes and the discussion included in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, and Item 7A, Quantitative and Qualitative Disclosures about Market Risk.

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

The table presenting an average balance sheet, interest income and expense, and the resultant average yield for average interest-earning assets and average interest-bearing liabilities is included in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

The table analyzing changes in interest income and expense by volume and rate is included in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

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Investment Portfolio

The following table presents the carrying values of securities for the years indicated:

	At December 31,		
	2015	2014	2013
	(Dollars in thousands)		
Securities available-for-sale:			
U.S. Treasury notes	$72,846	62,560	12,894
U.S. Agency notes	139,889	83,637	106,675
U.S. Agency mortgage-backed securities	29,378	38,032	40,309
Certificates of deposit	249	3,086	1,501
Municipal securities	132,420	93,790	92,642
Mutual funds	2,466	2,461	2,380
Trust preferred securities	50	50	147
Equity securities	680	1,749	1,693
Total securities available-for-sale	377,978	285,365	258,241
Securities held-to-maturity:			
Municipal securities	22,633	22,725	16,323
Federal Reserve Bank stock	2,732	2,346	1,603
Federal Home Loan Bank stock	3,638	3,638	2,854
Total securities	$406,981	314,074	279,021

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Contractual maturities of securities at December 31, 2015, were as follows. Actual maturities may differ from contractual maturities when issuers have the right to call or prepay obligations.

	Available-for-Sale				Held-to-Maturity			
	Amortized Cost	Fair Value	Yield		Amortized Cost	Fair Value	Yield	
	(Dollars in thousands)							
U.S. Treasury notes:								
Within one year	$9,091	9,081	0.67	%	$—	—	—	%
One to five years	36,725	36,923	1.60	%	—	—	—	%
Five to ten years	26,856	26,842	1.94	%	—	—	—	%
After ten years	—	—	—	%	—	—	—	%
Total U.S. Treasury notes	72,672	72,846	1.61	%	—	—	—	%
U.S. Agency notes:								
Within one year	—	—	—	%	—	—	—	%
One to five years	83,404	83,085	1.48	%	—	—	—	%
Five to ten years	57,472	56,804	2.06	%	—	—	—	%
After ten years	—	—	—	%	—	—	—	%
Total U.S. Agency notes	140,876	139,889	1.72	%	—	—	—	%
Certificates of deposit								
Within one year	248	249	1.16	%	—	—	—	%
One to five years	—	—	—	%	—	—	—	%
Five to ten years	—	—	—	%	—	—	—	%
After ten years	—	—	—	%	—	—	—	%
Total certificates of deposit	248	249	1.16	%	—	—	—	%
Municipal securities (1):								
Within one year	13,672	13,829	3.28	%	3,819	3,831	2.43	%
One to five years	62,645	63,589	3.03	%	3,904	3,882	3.04	%
Five to ten years	54,321	55,002	3.26	%	3,168	3,107	3.40	%
After ten years	—	—	—	%	11,742	11,810	6.31	%
Total Municipal securities	130,638	132,420	3.15	%	22,633	22,630	4.68	%
U.S. Agency mortgage-backed securities	29,608	29,378	2.39	%	—	—	—	%
Mutual funds	2,517	2,466	1.92	%	—	—	—	%
Trust preferred securities	49	50	7.78	%	—	—	—	%
Equity securities	659	680	4.57	%	—	—	—	%
Totals	$377,267	377,978	2.25	%	22,633	22,630	4.68	%

(1) Yields on tax-exempt obligations are computed on a taxable-equivalent basis based upon a 34% statutory Federal income tax rate.

Excluding holdings in U.S. Treasury securities and U.S. Government Agencies, there were no investments in securities of any issuer that exceeded 10% of LCNB's consolidated shareholders' equity at December 31, 2015.

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LCNB CORP. AND SUBSIDIARIES

Loan Portfolio

Administration of the lending function is the responsibility of the Chief Lending Officer and certain senior lenders. Lenders perform their duties subject to oversight and policy direction from the Board of Directors and the Loan Committee. The Loan Committee consists of LCNB's Chief Executive Officer, President, Chief Financial Officer, Cashier, Chief Lending Officer, Chief Credit Officer, Loan Operations Officer, Loan Review Officer, Credit Analysis Officer, and the officers in charge of commercial, consumer, and real estate loans.

Employees authorized to accept loan applications have various, designated lending limits for the approval of loans. A loan application for an amount outside a particular employee's lending limit needs to be approved by an employee with a lending limit sufficient for that loan. Residential and commercial real estate loans of any amount require the approval of two of the following designated officers: Chief Executive Officer, President, Chief Lending Officer, Chief Credit Officer, and the officers in charge of commercial, real estate, and consumer lending. Any loan in excess of $3.0 million or with policy exceptions needs the approval of the Board of Directors.

Interest rates charged by LCNB vary with degree of risk, type of loan, amount, complexity, repricing frequency and other relevant factors associated with the loan.

The following table summarizes the distribution of the loan portfolio for the years indicated:

	At December 31,														
	2015			2014			2013			2012			2011		
	Amount	%		Amount	%		Amount	%		Amount	%		Amount	%	
	(Dollars in thousands)														
Commercial and industrial	$45,275	5.9	%	$35,424	5.1	%	$29,337	5.1	%	$26,236	5.8	%	$30,990	6.7	%
Commercial, secured by real estate	419,633	54.5	%	379,141	54.3	%	314,252	54.7	%	230,256	50.7	%	219,188	47.6	%
Residential real estate	273,139	35.4	%	254,087	36.4	%	215,587	37.6	%	183,132	40.4	%	186,904	40.5	%
Consumer	18,510	2.4	%	18,006	2.5	%	12,643	2.2	%	10,554	2.3	%	14,562	3.2	%
Agricultural	13,479	1.7	%	11,472	1.6	%	2,472	0.4	%	1,668	0.4	%	2,835	0.6	%
Other loans, including deposit overdrafts	665	0.1	%	680	0.1	%	91	—	%	1,875	0.4	%	6,554	1.4	%
	770,701	100.0	%	698,810	100.0	%	574,382	100.0	%	453,721	100.0	%	461,033	100.0	%
Deferred origination costs (fees), net	237			146			(28	)		62			229		
Total loans	770,938			698,956			574,354			453,783			461,262		
Less allowance for loan losses	3,129			3,121			3,588			3,437			2,931		
Loans, net	$767,809			$695,835			$570,766			$450,346			$458,331		

As of December 31, 2015, there were no concentrations of loans exceeding 10% of total loans that are not already disclosed as a category of loans in the above table.

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LCNB CORP. AND SUBSIDIARIES

The following table summarizes the commercial and agricultural loan maturities and sensitivities to interest rate change at December 31, 2015:

	(In thousands)
Maturing in one year or less	$33,115
Maturing after one year, but within five years	63,883
Maturing beyond five years	381,389
Total commercial and agricultural loans	$478,387
Loans maturing beyond one year:	
Fixed rate	$155,886
Variable rate	289,386
Total	$445,272

Risk Elements

The following table summarizes non-accrual, past-due, and accruing restructured loans for the dates indicated:

	At December 31,				
	2015	2014	2013	2012	2011
	(Dollars in thousands)				
Non-accrual loans	$1,723	5,599	2,961	2,283	3,668
Past-due 90 days or more and still accruing	559	203	250	128	39
Accruing restructured loans	13,723	14,269	15,151	13,343	14,739
Total	$16,005	20,071	18,362	15,754	18,446
Percent to total loans	2.08 %	2.87 %	3.20 %	3.47 %	4.00 %

LCNB is not committed to lend additional funds to debtors whose loans have been modified to provide a reduction or deferral of principal or interest because of deterioration in the financial position of the borrower.

At December 31, 2015, there were no material additional loans not classified as acquired credit impaired or already disclosed as non-accrual, accruing restructured, or accruing past due 90 days or more where known information about possible credit problems of the borrowers causes management to have serious doubts as to the ability of such borrowers to comply with present loan repayment terms.

Summary of Loan Loss Experience

The table summarizing the activity related to the allowance for loan losses is included in Item 7, Management’s Discussion and Analysis of Financial Condition and Results of Operations.

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LCNB CORP. AND SUBSIDIARIES

Allocation of the Allowance for Loan Losses

The following table presents the allocation of the allowance for loan loss:

	At December 31, 2015			2014			2013			2012			2011		
	Amount	Percent of Loans in Each Category to Total Loans		Amount	Percent of Loans in Each Category to Total Loans		Amount	Percent of Loans in Each Category to Total Loans		Amount	Percent of Loans in Each Category to Total Loans		Amount	Percent of Loans in Each Category to Total Loans	
	(Dollars in thousands)														
Commercial and industrial	$244	5.9	%	$129	5.1	%	$175	5.1	%	$320	5.8	%	$162	6.7	%
Commercial, secured by real estate	1,908	54.5	%	1,990	54.3	%	2,520	54.7	%	2,296	50.7	%	1,941	47.6	%
Residential real estate	854	35.4	%	926	36.4	%	826	37.6	%	712	40.4	%	656	40.5	%
Consumer	54	2.4	%	63	2.5	%	66	2.2	%	108	2.3	%	166	3.2	%
Agricultural	66	1.7	%	11	1.6	%	—	0.4	%	—	0.4	%	—	0.6	%
Other loans, including deposit overdrafts	3	0.1	%	2	0.1	%	1	—	%	1	0.4	%	6	1.4	%
Unallocated	—	—		—	—		—	—		—	—		—	—	
Total	$3,129	100.0	%	$3,121	100.0	%	$3,588	100.0	%	$3,437	100.0	%	$2,931	100.0	%

Deposits

The statistical information regarding average amounts and average rates paid for the deposit categories is included in the "Distribution of Assets, Liabilities and Shareholders' Equity" table included in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following table presents the contractual maturity of time deposits of $100,000 or more at December 31, 2015:

	(In thousands)
Maturity within 3 months	$7,297
After 3 but within 6 months	5,137
After 6 but within 12 months	11,265
After 12 months	50,356
	$74,055

Return on Equity and Assets

The statistical information regarding the return on assets, return on equity, dividend payout ratio, and equity to assets ratio is presented in Item 6, Selected Financial Data.

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Item 1A. Risk Factors

There are risks inherent in LCNB's operations, many beyond management's control, which may adversely affect its financial condition and results from operations and should be considered in evaluating the Company. Credit, market, operational, liquidity, interest rate and other risks are described elsewhere in this report. Other risk factors may include the items described below.

New capital requirements could adversely affect LCNB's capital ratios
On July 2, 2013, the Federal Reserve Board approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for U.S. bank holding companies as well as state banks that are members of the Federal Reserve System and savings and loan holding companies (commonly known as Basel III). On July 9, 2013, the OCC adopted the same rules for national banks and federal savings associations, and the FDIC approved the same provisions, as an interim final rule, for state nonmember banks and state savings associations.

Under the final rules, minimum requirements will increase for both the quantity and quality of capital held by banks and savings associations. The rules include a new common equity Tier 1 capital to risk-weighted assets ratio of 4.5% and a common equity Tier 1 capital conservation buffer of 2.5% of risk-weighted assets. The final rules also raise the minimum ratio of Tier 1 capital to risk-weighted assets from 4.0% to 6.0% and require a minimum leverage ratio of 4.0%.

The phase-in period for the final rules began for LCNB on January 1, 2015, with full compliance with all of the final rules' requirements phased in over a multi-year schedule. While management expects that LCNB's capital ratios under Basel III will continue to exceed the well capitalized minimum capital requirements, there can be no assurance that such will be the case. If LCNB is unable to meet or exceed the applicable minimum capital requirements, it may become subject to supervisory actions ranging in severity from losing its financial holding company status, to being precluded from making acquisitions or engaging in new activities or becoming subject to informal or formal regulatory enforcement actions.

LCNB's earnings are significantly affected by market interest rates.
Fluctuations in interest rates may negatively impact LCNB's profitability. A primary source of income from operations is net interest income, which is equal to the difference between interest income earned on loans and investment securities and the interest paid for deposits and other borrowings. These rates are highly sensitive to many factors beyond LCNB's control, including general economic conditions, the slope of the yield curve (that is, the relationship between short and long-term interest rates), and the monetary and fiscal policies of the United States Federal government. LCNB expects the current level of interest rates and the current slope of the yield curve will cause further downward pressure on its net interest margin.

Increases in general interest rates could have a negative impact on LCNB's results of operations by reducing the ability of borrowers to repay their current loan obligations. Some residential real estate mortgage loans, most home equity line of credit loans, and many of LCNB's commercial loans have adjustable rates. Borrower inability to make scheduled loan payments due to a higher loan cost could result in increased loan defaults, foreclosures, and write-offs and may necessitate additions to the allowance for loan losses. In addition, increases in the general level of interest rates may decrease the demand for new consumer and commercial loans, thus limiting LCNB's growth and profitability. A general increase in interest rates may also result in deposit disintermediation, which is the flow of deposits away from banks and other depository institutions into direct investments that have the potential for higher rates of return, such as stocks, bonds, and mutual funds. If this occurs, LCNB may have to rely more heavily on borrowings as a source of funds in the future, which could negatively impact its net interest margin.

Gains from sales of mortgage loans may experience significant volatility.

Gains from sales of mortgage loans are highly influenced by the level and direction of mortgage interest rates, real estate activity, and refinancing activity. Current historically low market interest rates created a refinancing demand for residential fixed-rate mortgage loans. The increased volume of refinancing activity increased gains from sales of mortgage loans as LCNB sold most of these loans to the Federal Home Loan Mortgage Corporation. An increase in market interest rates may decrease the demand for refinanced loans and decrease the gains from sales of mortgage loans recognized in LCNB's consolidated statements of income. Gains from sales of mortgage loans may also be impacted by changes in LCNB's strategy to manage its residential mortgage portfolio. For example, LCNB may occasionally change the proportion of loan originations that are sold in the secondary market and instead add a greater proportion to its loan portfolio.

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Banking competition in Southwestern and South Central Ohio is intense.
LCNB faces strong competition for deposits, loans, trust accounts, and other services from other banks, savings banks, credit unions, mortgage brokers, and other financial institutions. Many of LCNB’s competitors include major financial institutions that have been in business for many years and have established customer bases, numerous branches, and substantially higher regulatory lending limits. Competitors in the Southwestern Ohio area include U.S. Bank, PNC Bank, Fifth Third Bank, Chase, KeyBank, Park National Bank, Huntington National Bank, and First Financial Bank. In addition, credit unions are growing larger due to more flexible membership requirement regulations and are offering more financial services than they legally could in the past.

LCNB also competes with numerous real estate brokerage firms, some owned by realty companies, for residential real estate mortgage loans. Incentives offered by captive finance companies owned by the major automobile companies have limited the banking industry’s opportunities for growth in the new automobile loan market. The banking industry now competes with brokerage firms and mutual fund companies for funds that would have historically been held as bank deposits. Technology has lowered barriers to entry and made it possible for non-banks to offer products and services traditionally provided by banks, such as automatic transfer and automatic payment systems. Many of these competitors have fewer regulatory constraints and may have lower cost structures.

If LCNB is unable to attract and retain loan, deposit, brokerage, and trust customers, its growth and profitability levels may be negatively impacted.

Economic conditions in Southwestern and South Central Ohio could adversely affect LCNB’s financial condition and results of operations.
LCNB conducts its operations from offices that are located in nine Southwestern and South Central Ohio counties, from which substantially all of its customer base is drawn. Because of this geographic concentration of operations and customer base, LCNB's financial performance is heavily influenced by economic conditions in these areas. LCNB's financial performance could be negatively affected to the extent that business and economic conditions in these areas do not continue to recover from the recent recession. Any material deterioration in economic conditions in these markets could have material direct or indirect adverse impacts on LCNB's customers and on LCNB. Such deterioration could increase the number of customers experiencing financial distress, negatively impacting their ability to obtain new loans or to repay existing loans. As a result, LCNB may experience increases in the levels of impaired loans, increased charge-offs, and increased provisions for loan losses. Deteriorating economic conditions may also effect the ability of depositors to maintain or add to deposit balances and may effect the demand for loans, trust, brokerage, and other products and services offered by LCNB. Such losses and decreased demand could have material adverse effects on LCNB's financial position, results of operations, and cash flows.

The allowance for loan losses may be inadequate.
The provision for loan losses is determined by management based upon its evaluation of the amount needed to maintain the allowance for loan losses at a level considered appropriate in relation to the estimated risk of losses inherent in the portfolio. In addition to historic charge-off percentages, factors taken into consideration to determine the adequacy of the allowance for loan losses include the nature, volume, and consistency of the loan portfolio, overall portfolio quality, a review of specific problem loans, the fair value of any underlying collateral, borrowers’ cash flows, and current economic conditions that may affect borrowers’ ability to make payments. Increases in the allowance result in an expense for the period. By its nature, the evaluation is imprecise and requires significant judgment. Actual results may vary significantly from management’s assumptions. If, as a result of general economic conditions or a decrease in asset quality, management determines that additional increases in the allowance for loan

losses are necessary, LCNB will incur additional expenses.

LCNB's loan portfolio includes a substantial amount of commercial and industrial loans and commercial real estate loans, which may have more risks than residential or consumer loans.

LCNB's commercial and industrial and commercial real estate loans comprise a substantial portion of its total loan portfolio. These loans generally carry larger loan balances and involve a greater degree of financial and credit risk than home equity, residential mortgage, or consumer loans. The increased financial and credit risk associated with these types of loans is a result of several factors, including the concentration of principal in a limited number of loans, the size of loan balances, the effects of general economic conditions on income-producing properties, and the increased difficulty of evaluating and monitoring these types of loans.

The repayment of loans secured by commercial real estate is often dependent upon the successful operation, development, or sale of the related real estate or commercial business and may, therefore, be subject to adverse conditions in the real estate market or economy. If the cash flow from operations is reduced, the borrower's ability to repay the loan may be impaired. In such cases, LCNB may take one or more actions to protect its financial interest in the loan. Such actions may include foreclosure on the real estate securing the loan, taking possession of other collateral that may have been pledged as security for the loan, or modifying the terms of the loan. If foreclosed on, commercial real estate is often unique and may not be as salable as a residential home.

The fair value of LCNB's investments could decline.

Most of LCNB's investment securities portfolio is designated as available-for-sale. Accordingly, unrealized gains and losses, net of tax, in the estimated fair value of the available-for-sale portfolio is recorded as other comprehensive income, a separate component of shareholders' equity. The fair value of LCNB's investment portfolio may decline, causing a corresponding decline in shareholders' equity. Management believes that several factors will affect the fair values of the investment portfolio including, but not limited to, changes in interest rates or expectations of changes, the degree of volatility in the securities markets, inflation rates or expectations of inflation, and the slope of the interest rate yield curve. These and other factors may impact specific categories of the portfolio differently and the effect any of these factors may have on any specific category of the portfolio cannot be predicted.

Many state and local governmental authorities have experienced deterioration of financial condition in recent years due to declining tax revenues, increased demand for services, and various other factors. To the extent LCNB has any municipal securities in its portfolio from issuers who are experiencing deterioration of financial condition or who may experience future deterioration of financial condition, the value of such securities may decline and could result in other-than-temporary impairment charges, which could have an adverse effect on LCNB's financial condition and results of operations. Additionally, a general, industry-wide decline in the fair value of municipal securities could significantly affect LCNB's financial condition and results of operations.

Changes in income tax laws or interpretations or in accounting standards could materially affect LCNB's financial condition or results of operations.

Changes in income tax laws could be enacted, or interpretations of existing income tax laws could change, causing an adverse effect to LCNB's financial condition or results of operations. Similarly, new accounting standards may be issued by the Financial Accounting Standards Board (the "FASB") or existing standards revised, changing the methods for preparing financial statements. These changes are not within LCNB's control and may significantly impact its reported financial condition and results of operations. FASB is currently working on various projects, including accounting for impaired financial instruments and accounting for leases.

LCNB is subject to environmental liability risk associated with lending activities.

A significant portion of the Bank's loan portfolio is secured by real property. During the ordinary course of business, the Bank may foreclose on and take title to properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on these properties. If hazardous or toxic substances are found, the Bank may be liable for remediation costs, as well as for personal injury and property damage. Environmental laws may require the Bank to incur substantial expenses and may materially reduce the affected property's value or limit the Bank's ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase the Bank's exposure to environmental liability. Although the Bank has policies and procedures to perform an environmental review before initiating any foreclosure action on real property, these reviews may not be sufficient to detect all potential environmental hazards. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on LCNB's financial condition and results of operations.

The banking industry is highly regulated.

LCNB is subject to regulation, supervision, and examination by the Federal Reserve Board and the Bank is subject to regulation, supervision, and examination by the OCC. LCNB and the Bank are also subject to regulation and examination by the FDIC as the deposit insurer. The Bureau of Consumer Financial Protection is responsible for most consumer protection laws and has broad authority, with certain exceptions, to regulate financial products offered by banks. Federal and state laws and regulations govern numerous matters including, but not limited to, changes in the ownership or control of banks, maintenance of adequate capital, permissible business operations, maintenance of deposit insurance, protection of customer financial privacy, the level of reserves held against deposits, restrictions on dividend payments, the making of loans, and the acceptance of deposits. See the previous section titled “Supervision and Regulation” for more information on this subject.

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LCNB CORP. AND SUBSIDIARIES

Federal regulators may initiate various enforcement actions against a financial institution that violates laws or regulations or that operates in an unsafe or unsound manner. These enforcement actions may include, but are not limited to, the assessment of civil money penalties, the issuance of cease-and-desist or removal orders, and the imposition of written agreements.

Proposals to change the laws governing financial institutions are periodically introduced in Congress and proposals to change regulations are periodically considered by the regulatory bodies. Such future legislation and/or changes in regulations could increase or decrease the cost of doing business, limit or expand permissible activities, or affect the competitive balance among banks, savings associations, credit unions, and other financial institutions. The likelihood of any major changes in the future and their effects are impossible to predict.

FDIC deposit insurance assessments may materially increase in the future.
Deposits of LCNB are insured up to statutory limits by the Federal Deposit Insurance Corporation (FDIC) and, accordingly, LCNB and other banks and financial institutions pay quarterly premiums to the FDIC to maintain the Deposit Insurance Fund. The likelihood and extent of future rate increases are indeterminable.

Future growth and expansion opportunities may contain risks.
From time to time LCNB may seek to acquire other financial institutions or parts of those institutions or may engage in de novo branch expansion. It may also consider and enter into new lines of business or offer new products or services. Such activities involve a number of risks, which may include potential inaccuracies in estimates and judgments used to evaluate the expansion opportunity, diversion of management and employee attention, lack of experience in a new market or product or service, and difficulties in integrating a future acquisition or introducing a new product or service. There is no assurance that such growth or expansion activities will be successful or that they will achieve desired profitability levels.

LCNB’s controls and procedures may fail or be circumvented.
Management regularly reviews and updates LCNB’s internal controls, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of LCNB’s controls and procedures or failure to comply with regulations related to its controls and procedures could have a material adverse effect on LCNB’s business, results of operations, and financial condition.

LCNB’s information systems may experience an interruption or breach in security.
LCNB relies heavily on communications and information systems to conduct its business. Any failure, interruption, or breach in security of these systems could result in failures or disruptions in LCNB’s customer relationship management, general ledger, deposit, loan, and other systems. While LCNB has policies and procedures designed to prevent or limit the effect of the failure, interruption, or security breach of its information systems, there can be no assurance that any such occurrences will not occur or, if they do occur, that they will be adequately addressed. The occurrence of any failures, interruptions, or security breaches of LCNB’s information systems could damage LCNB’s reputation, result in a loss of customer business, subject LCNB to additional regulatory scrutiny, or expose LCNB to civil litigation and possible financial liability, any of which could have a material adverse effect on its financial condition and results of operations.

LCNB continually encounters technological change.

The financial services industry is continually undergoing rapid technological change with frequent introductions of new technology-driven products and services. LCNB's future success depends, in part, upon its ability to address customer needs by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in LCNB's operations. LCNB may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to its customers. Failure to successfully keep pace with technological change affecting the financial services industry could negatively affect LCNB's growth, revenue and profit.

Risk factors related to LCNB's trust business.
Competition for trust business is intense. Competitors include other commercial bank and trust companies, brokerage firms, investment advisory firms, mutual fund companies, accountants, and attorneys.

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LCNB's trust business is directly affected by conditions in the debt and equity securities markets. The debt and equity securities markets are affected by, among other factors, domestic and foreign economic conditions and the monetary and fiscal policies of the United States Federal government, all of which are beyond LCNB's control. Changes in economic conditions may directly affect the economic performance of the trust accounts in which clients' assets are invested. A decline in the fair value of the trust accounts caused by a decline in general economic conditions directly affects LCNB's trust fee income because such fees are primarily based on the fair value of the trust accounts. In addition, a sustained decrease in the performance of the trust accounts or a lack of sustained growth may encourage clients to seek alternative investment options.

The management of trust accounts is subject to the risk of mistaken distributions, poor investment choices, and miscellaneous other incorrect decisions. Such mistakes may give rise to surcharge actions by beneficiaries, with damages substantially in excess of the fees earned from management of the accounts.

LCNB's ability to pay cash dividends is limited.
LCNB is dependent upon the earnings of the Bank for funds to pay dividends on its common shares. The payment of dividends by LCNB and the Bank is subject to certain regulatory restrictions. As a result, any payment of dividends in the future will be dependent, in large part, on the ability of LCNB and the Bank to satisfy these regulatory restrictions and on the Bank's earnings, capital levels, financial condition, and other factors. Although LCNB's financial earnings and financial condition have allowed it to declare and pay periodic cash dividends to shareholders, there can be no assurance that the current dividend policy or the amount of dividend distributions will continue in the future.

Item 1B. Unresolved Staff Comments

Not applicable

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LCNB CORP. AND SUBSIDIARIES

Item 2. Properties

The Bank conducts its business from the following offices:

	Name of Office	Address	
1.	Main Office	2 North Broadway Lebanon, Ohio 45036	Owned
2.	Auto Bank	Silver and Mechanic Streets Lebanon, Ohio 45036	Owned
3.	Barron Street Office	1697 North Barron Street Eaton, Ohio 45320	Leased
4.	Bridge Street Office	1240 North Bridge Street Chillicothe, Ohio 45601	Owned
5.	Brookville Office	225 West Upper Lewisburg Salem Road Brookville, Ohio 45309	Owned
6.	Centerville Office	9605 Dayton-Lebanon Pike Centerville, Ohio 45458	Owned
7.	Chillicothe Office	33 West Main Street Chillicothe, Ohio 45601	Owned
8.	Clarksburg Office	10820 Main Street Clarksburg, Ohio 43115	Owned
9.	Colerain Township Office	3209 West Galbraith Road Cincinnati, Ohio 45239	Owned
10.	Columbus Avenue Office	730 Columbus Avenue Lebanon, Ohio 45036	Owned
11.	Eaton Office	110 West Main Street Eaton, Ohio 45320	Owned
12.	Fairfield Office	765 Nilles Road Fairfield, Ohio 45014	Leased
13.	Frankfort Office	Springfield and Main Streets Frankfort, Ohio 45628	Owned
14.	Goshen Office	6726 Dick Flynn Blvd.	Owned

		Goshen, Ohio 45122	
15.	Hamilton Office	794 NW Washington Blvd. Hamilton, Ohio 45013	Owned
16.	Hay Avenue Office	121 Hay Avenue Brookville, Ohio 45309	Owned
17.	Hunter Office	3878 State Route 122 Franklin, Ohio 45005	Owned
18.	Lewisburg Office	522 South Commerce Street Lewisburg, Ohio 45338	Owned

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	Name of Office	Address	
19.	Loveland Office	500 Loveland-Madeira Road Loveland, OH 45140	Owned
20.	Maineville Office	7795 South State Route 48 Maineville, Ohio 45039	Owned
21.	Mason/West Chester Office	1050 Reading Road Mason, Ohio 45040	Owned
22.	Middletown Office	4441 Marie Drive Middletown, Ohio 45044	Owned
23.	Monroe Office	101 Clarence F. Warner Drive Monroe, Ohio 45050	Owned
24.	New Paris Office	201 South Washington Street New Paris, Ohio 45347	Owned
25.	Oakwood Office	2705 Far Hills Avenue Oakwood, Ohio 45419	(2)
26.	Okeana Office (closed February 12, 2016)	6225 Cincinnati-Brookville Road Okeana, Ohio 45053	Owned
27.	Otterbein Office	Otterbein Retirement Community State Route 741 Lebanon, Ohio 45036	Leased
28.	Oxford Office (1)	30 West Park Place Oxford, Ohio 45056	(2)
29.	Rochester/Morrow Office	Route 22-3 at 123 Morrow, Ohio 45152	Owned
30.	South Lebanon Office	603 Corwin Nixon Blvd. South Lebanon, Ohio 45065	Owned
31.	Springboro/Franklin Office	525 West Central Avenue Springboro, Ohio 45066	Owned
32.	Warrior Office	Lebanon High School 1916 Drake Road Lebanon, Ohio 45036	Leased

33.	Washington Court House Office	100 Crossings Drive Washington Court House, Ohio 43160	Owned
34.	Waynesville Office	9 North Main Street Waynesville, Ohio 45068	Owned
35.	West Alexandria Office	55 East Dayton Street West Alexandria, Ohio 45381	Owned
36.	Western Avenue Office	1006 Western Avenue Chillicothe, Ohio 45601	Owned

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	Name of Office	Address	
37.	Wilmington Office	1243 Rombach Avenue Wilmington, Ohio 45177	Owned
38.	Operations Center (under construction)	105 North Broadway Lebanon, Ohio 45036	Owned

(1) Excess space in this office is leased to third parties.
(2) The Bank owns the Oakwood and Oxford office buildings and leases the land.

Item 3. Legal Proceedings

Except for routine litigation incidental to its businesses, LCNB is not a party to any material pending legal proceedings and none of its property is the subject of any such proceedings.

Item 4. Mine Safety Disclosures

Not Applicable

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LCNB CORP. AND SUBSIDIARIES

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities.

LCNB had approximately 1,026 registered holders of its common stock as of December 31, 2015. The number of shareholders includes banks and brokers who act as nominees, each of whom may represent more than one shareholder. LCNB's stock trades on the NASDAQ Capital Market exchange under the symbol "LCNB."

Trade prices for shares of LCNB Common Stock and cash dividends per share declared and paid are set forth below. The trade prices shown below are interdealer without retail markups, markdowns, or commissions.

	2015			2014		
	High	Low	Dividends Declared	High	Low	Dividends Declared
First Quarter	$16.40	13.95	0.16	18.24	17.25	0.16
Second Quarter	17.88	15.01	0.16	18.89	14.67	0.16
Third Quarter	16.40	15.26	0.16	17.14	14.84	0.16
Fourth Quarter	17.18	15.07	0.16	15.43	13.83	0.16
Total dividends declared			0.64			0.64

It is expected that LCNB will continue to pay dividends on a similar schedule, to the extent permitted by business and potential factors beyond management's control.

LCNB depends on dividends from the Bank for the majority of its liquid assets, including the cash needed to pay dividends to its shareholders. National banking law limits the amount of dividends the Bank may pay to the sum of retained net income, as defined, for the current year plus retained net income for the previous two years. Prior approval from the OCC, the Bank's primary regulator, would be necessary for the Bank to pay dividends in excess of this amount. In addition, dividend payments may not reduce capital levels below minimum regulatory guidelines. Management believes the Bank will be able to pay anticipated ordinary dividends to LCNB without needing to request approval.

During the period of this report, LCNB did not sell any of its securities that were not registered under the Securities Act.

On April 17, 2001, LCNB's Board of Directors authorized three separate stock repurchase programs, two of which continue to be in effect – the "Market Repurchase Program and the "Private Sale Repurchase Program." Any shares purchased will be held for future corporate purposes.

Under the Market Repurchase Program, LCNB was originally authorized to purchase up to 200,000 shares of its stock through market transactions with a selected stockbroker. On November 14, 2005, the Board of Directors extended the Market Repurchase Program by increasing the shares authorized for repurchase to 400,000 total shares. Through December 31, 2015, 290,444 shares have been purchased under this program. No shares were purchased under the Market Repurchase Program during 2015.

The Private Sale Repurchase Program is available to shareholders who wish to sell large blocks of stock at one time. Because LCNB's stock is not widely traded, a shareholder releasing large blocks may not be able to readily sell all shares through normal procedures. Purchases of blocks will be considered on a case-by-case basis and will be made at prevailing market prices. There is no limit to the number of shares that may be purchased under this program. A total of 466,018 shares have been purchased under this program since its inception through December 31, 2015. No shares were purchased under the Private Sale Repurchase Program during 2015.

LCNB established an Ownership Incentive Plan (the "2002 Plan") during 2002 that allowed for the issuance of up to 200,000 shares of stock-based awards to eligible employees, as determined by the Board of Directors. The awards could be in the form of stock options, share awards, and/or appreciation rights. The 2002 Plan expired on April 16, 2012. Outstanding, unexercised options continue to be exercisable in accordance with their terms.

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The 2015 Ownership Incentive Plan (the "2015 Plan") was approved by LCNB's shareholders at the annual meeting on April 28, 2015 and allows for stock-based awards to eligible employees, as determined by the Compensation Committee of the Board of Directors. Awards may be made in the form of stock options, appreciation rights, restricted shares, and/or restricted share units. This plan provides for the issuance of up to 450,000 shares and will terminate on April 28, 2025, unless earlier terminated by the Compensation Committee.

The following table shows information relating to stock options outstanding under the 2002 Plan and 2015 Plan at December 31, 2015:

Plan Category	Number of Securities to be Issued upon Exercise of Outstanding Options	Weighted Average Exercise Price of Outstanding Options	Number of Securities Remaining Available for Future Issuance
Equity compensation plans approved by security holders	83,861	$12.39	433,962
Equity compensation plans not approved by security holders	—	—	—
Total	83,861	$12.39	433,962

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The graph below provides an indicator of cumulative total shareholder returns for LCNB as compared with the NASDAQ Composite, the SNL Midwest OTC-BB and Pink Sheet Banks, and the SNL Midwest Bank indexes. This graph covers the period from December 31, 2010 through December 31, 2015. The cumulative total shareholder returns included in the graph reflect the returns for the shares of common stock of LCNB. The information provided in the graph assumes that $100 was invested on December 31, 2010 in LCNB common stock, the NASDAQ Composite, and the SNL Midwest Bank Index and that all dividends were reinvested.

	Period Ending					
Index	12/31/2010	12/31/2011	12/31/2012	12/31/2013	12/31/2014	12/31/2015
LCNB Corp.	$100.00	114.16	126.65	171.16	150.37	169.90
NASDAQ Composite	$100.00	99.21	116.82	163.75	188.03	201.40
SNL Midwest Bank index	$100.00	94.46	113.69	155.65	169.21	171.78

Source : SNL Financial LC, Charlottesville, VA

www.snl.com

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LCNB CORP. AND SUBSIDIARIES

Item 6. Selected Financial Data

The following represents selected consolidated financial data of LCNB for the years ended December 31, 2011 through 2015 and are derived from LCNB's consolidated financial statements. Certain prior year data presented in this table have been reclassified to conform with the current year presentation. This data should be read in conjunction with the consolidated financial statements and the notes thereto included in Item 8 of this Form 10-K and Management's Discussion and Analysis of Financial Condition and Results of Operations and Quantitative and Qualitative Disclosures about Market Risk included in Items 7 and 7A, respectively, of this Form 10-K, and are qualified in their entirety thereby and by other detailed information elsewhere in this Form 10-K.

	For the Years Ended December 31,				
	2015	2014	2013	2012	2011
	(Dollars in thousands, except ratios and per share data)				
Income Statement:					
Interest income	$42,659	39,477	33,497	29,938	32,093
Interest expense	3,328	3,590	4,065	4,889	6,387
Net interest income	39,331	35,887	29,432	25,049	25,706
Provision for loan losses	1,366	930	588	1,351	2,089
Net interest income after provision for loan losses	37,965	34,957	28,844	23,698	23,617
Non-interest income	10,123	9,142	9,090	9,049	7,764
Non-interest expenses	32,392	30,844	26,212	21,682	21,849
Income before income taxes	15,696	13,255	11,722	11,065	9,532
Provision for income taxes	4,222	3,386	2,942	2,795	2,210
Net income from continuing operations	11,474	9,869	8,780	8,270	7,322
Income from discontinued operations, net of tax	—	—	—	—	793
Net income	$11,474	9,869	8,780	8,270	8,115
Dividends per common share	$0.64	0.64	0.64	0.64	0.64
Basic earnings per common share:					
Continuing operations	1.18	1.06	1.12	1.23	1.09
Discontinued operations	—	—	—	—	0.12
Diluted earnings per common share:					
Continuing operations	1.17	1.05	1.10	1.22	1.08
Discontinued operations	—	—	—	—	0.12
Balance Sheet:					
Securities	$406,981	314,074	279,021	276,970	267,771
Loans, net	767,809	695,835	570,766	450,346	458,331
Total assets	1,280,531	1,108,066	932,338	788,637	791,570
Total deposits	1,087,160	946,205	785,761	671,471	663,562
Short-term borrowings	37,387	16,645	8,655	13,756	21,596
Long-term debt	5,947	11,357	12,102	13,705	21,373
Total shareholders' equity	140,108	125,695	118,873	82,006	77,960

Selected Financial Ratios and Other Data:

Return on average assets	0.94	%	0.88	%	0.93	%	1.02	%	1.02	%
Return on average equity	8.43	%	8.04	%	9.02	%	10.22	%	10.89	%
Equity-to-assets ratio	10.94	%	11.34	%	12.75	%	10.40	%	9.85	%
Dividend payout ratio	54.24	%	60.38	%	57.14	%	52.03	%	52.89	%
Net interest margin, fully taxable equivalent	3.64	%	3.66	%	3.57	%	3.52	%	3.70	%

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LCNB CORP. AND SUBSIDIARIES

Dakin Insurance Agency, Inc. ("Dakin") was sold during the first quarter 2011 and therefore the net gain on the sale and Dakin’s financial operating results are reported in the income statements as income from discontinued operations, net of tax.
First Capital merged with and into LCNB as of the close of business on January 11, 2013. As of the date of the merger, LCNB recorded additional loans of $98.9 million and additional deposits of $136.8 million.
An underwritten public offering of common stock was conducted during the fourth quarter 2013. The offering increased shareholders' equity by $26.9 million, which was the net proceeds LCNB received after deducting offering expenses. The proceeds were used to fund the acquisition of Eaton National on January 24, 2014 and the remainder was used for general corporate purposes.
Eaton National merged with and into LCNB as of the close of business on January 24, 2014. As of the date of the merger, LCNB recorded additional loans of $115.9 million and additional deposits of $165.3 million.
BNB merged with and into LCNB as of the close of business on April 30, 2015. As of the date of the merger, LCNB recorded additional loans of $34.7 million and additional deposits of $99.1 million.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Introduction

The following is management's discussion and analysis of the consolidated financial condition and consolidated results of operations of LCNB. It is intended to amplify certain financial information regarding LCNB and should be read in conjunction with the Consolidated Financial Statements and related Notes and the Financial Highlights contained in the 2015 Annual Report to Shareholders.

Forward-Looking Statements

Certain statements made in this document regarding LCNB's financial condition, results of operations, plans, objectives, future performance and business, are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995. These forward-looking statements are identified by the fact they are not historical facts and include words such as "anticipate", "could", "may", "feel", "expect", "believe", "plan", and similar express

These forward-looking statements reflect management's current expectations based on all information available to management and its knowledge of LCNB's business and operations. Additionally, LCNB's financial condition, results of operations, plans, objectives, future performance and business are subject to risks and uncertainties that may cause actual results to differ materially. These factors include, but are not limited to:

1. the success, impact, and timing of the implementation of LCNB's business strategies, including the successful integration of recently completed acquisitions;
2. LCNB may incur increased charge-offs in the future;
3. LCNB may face competitive loss of customers;
4. changes in the interest rate environment may have results on LCNB's operations materially different from those anticipated by LCNB's market risk management functions;
5. changes in general economic conditions and increased competition could adversely affect LCNB's operating results;
6. changes in other regulations and government policies affecting bank holding companies and their subsidiaries, including changes in monetary policies, could negatively impact LCNB's operating results;
7. LCNB may experience difficulties growing loan and deposit balances;
8. the current economic environment poses significant challenges for us and could adversely affect our financial condition and results of operations;
9. deterioration in the financial condition of the U.S. banking system may impact the valuations of investments LCNB has made in the securities of other financial institutions resulting in either actual losses or other than temporary impairments on such investments; and
10. the effects of the Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and the regulations promulgated and to be promulgated thereunder, which may subject LCNB and its subsidiaries to a variety of new and more stringent legal and regulatory requirements which adversely affect their respective businesses.

Forward-looking statements made herein reflect management's expectations as of the date such statements are made. Such information is provided to assist shareholders and potential investors in understanding current and anticipated financial operations of LCNB and is included pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. LCNB undertakes no obligation to update any forward-looking statement to reflect events or circumstances that arise after the date such statements are made.

Overview

Net income for 2015 was $11,474,000 (basic and diluted earnings per share of $1.18 and $1.17, respectively), compared to $9,869,000 (basic and diluted earnings per share of $1.06 and $1.05) in 2014 and $8,780,000 (total basic and diluted earnings per share of $1.12 and $1.10) in 2013.

The following items significantly affected earnings for the years indicated:

1. The completion of a merger with BNB Bancorp, Inc. on April 30, 2015.
2. The completion of a merger with Eaton National Bank & Trust Co. on January 24, 2014.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

3. The completion of a merger with First Capital Bancshares, Inc. and its subsidiary, Citizens National Bank of Chillicothe, on January 11, 2013.
4. Net gains on sales of securities were significantly greater in 2013 when compared to 2015 and 2014.
5. Other real estate owned expense was significantly less in 2013 as compared to 2015 and 2014 because of decreases in valuation write-downs and a gain recognized during the first quarter 2013 on the sale of commercial real estate property.
6. Impaired loans with a carrying value of approximately $4.5 million were sold during the second second quarter 2015, significantly improving LCNB's loan quality metrics.

Net Interest Income

LCNB's primary source of earnings is net interest income, which is the difference between earnings from loans and other investments and interest paid on deposits and other liabilities. The following table presents, for the years indicated, average balances for interest-earning assets and interest-bearing liabilities, the income or expense related to each item, and the resulting average yields earned or rates paid.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

	Years ended December 31,								
	2015			2014			2013		
	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Paid	Average Yield/ Rate
	(Dollars in thousands)								
Loans (1)	$740,626	35,285	4.76%	$679,223	32,706	4.82%	$555,602	27,325	4.92%
Federal funds sold	452	1	0.22%	—	—	— %	768	1	0.13%
Interest-bearing demand deposits	12,245	30	0.24%	12,450	29	0.23%	9,908	24	0.24%
Federal Reserve Bank stock	2,495	152	6.09%	2,100	126	6.00%	1,436	86	5.99%
Federal Home Loan Bank stock	3,638	146	4.01%	3,571	146	4.09%	2,826	119	4.21%
Investment securities:									
Taxable	245,410	4,197	1.71%	219,131	3,757	1.71%	192,983	3,369	1.75%
Non-taxable (2)	115,215	4,315	3.75%	102,902	4,111	4.00%	98,567	3,898	3.95%
Total earning assets	1,120,081	44,126	3.94%	1,019,377	40,875	4.01%	862,090	34,822	4.04%
Non-earning assets	107,919			104,413			85,970		
Allowance for loan losses	(2,888)			(3,275)			(3,401)		
Total assets	$1,225,112			$1,120,515			$944,659		
Savings deposits	$608,925	545	0.09%	$544,698	474	0.09%	$454,265	407	0.09%
IRA and time certificates	219,562	2,464	1.12%	223,555	2,687	1.20%	197,302	3,195	1.62%
Short-term borrowings	15,105	24	0.16%	14,820	22	0.15%	16,912	25	0.15%
Long-term debt	6,177	295	4.78%	11,546	407	3.53%	12,768	438	3.43%
Total interest-bearing liabilities	849,769	3,328	0.39%	794,619	3,590	0.45%	681,247	4,065	0.60%
Demand deposits	230,608			196,273			160,470		
Other liabilities	8,590			6,908			5,593		
Capital	136,145			122,716			97,349		
Total liabilities and capital	$1,225,112			$1,120,516			$944,659		
Net interest rate spread (3)			3.55%			3.56%			3.44%
Net interest income and net interest margin on a tax equivalent basis (4)		40,798	3.64%		37,285	3.66%		30,757	3.57%
Ratio of interest-earning assets to interest-bearing liabilities	131.81%			128.29%			126.55%		

(1) Includes non-accrual loans if any.
(2) Income from tax-exempt securities is included in interest income on a taxable-equivalent basis. Interest income has been divided by a factor comprised of the complement of the incremental tax rate of 34%.
(3) The net interest spread is the difference between the average rate on total interest-earning assets and interest-bearing liabilities.
(4) The net interest margin is the taxable-equivalent net interest income divided by average interest-earning assets.

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LCNB CORP. AND SUBSIDIARIES

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

The following table presents the changes in interest income and expense for each major category of interest-earning assets and interest-bearing liabilities and the amount of change attributable to volume and rate changes for the years indicated. Changes not solely attributable to rate or volume have been allocated to volume and rate changes in proportion to the relationship of absolute dollar amounts of the changes in each.

	For the years ended December 31,					
	2015 vs. 2014			2014 vs. 2013		
	Increase (decrease) due to			Increase (decrease) due to		
	Volume	Rate	Total	Volume	Rate	Total
	(In thousands)					
Interest income attributable to:						
Loans (1)	$2,929	(350)	2,579	5,964	(583)	5,381
Federal funds sold	1	—	1	(1)	—	(1)
Interest-bearing demand deposits	—	1	1	6	(1)	5
Federal Reserve Bank stock	24	2	26	40	—	40
Federal Home Loan Bank stock	3	(3)	—	31	(4)	27
Investment securities:						
Taxable	449	(9)	440	449	(61)	388
Non-taxable (2)	472	(268)	204	173	40	213
Total interest income	3,878	(627)	3,251	6,662	(609)	6,053
Interest expense attributable to:						
Savings deposits	57	14	71	80	(13)	67
IRA and time certificates	(47)	(176)	(223)	388	(896)	(508)
Short-term borrowings	—	2	2	(3)	—	(3)
Long-term debt	(227)	115	(112)	(43)	12	(31)
Total interest expense	(217)	(45)	(262)	422	(897)	(475)
Net interest income	$4,095	(582)	3,513	6,240	288	6,528

(1) Non-accrual loans, if any, are included in average loan balances.
(2) Change in interest income from non-taxable investment securities is computed based on interest income determined on a taxable-equivalent yield basis. Interest income has been divided by a factor comprised of the complement of the incremental tax rate of 34%.

2015 vs. 2014. Net interest income on a fully tax-equivalent basis for 2015 totaled $40,798,000, an increase of $3,513,000 from 2014. The increase resulted from an increase in total taxable-equivalent interest income of $3,251,000 and a decrease in total interest expense of $262,000.

The increase in taxable-equivalent interest income was due to a $100.7 million increase in total average interest-earning assets, slightly offset by a 7 basis point (a basis point equals 0.01%) decrease in the average rate earned on interest-earning assets. The increase in total average interest-earning assets reflects an increase of $61.4 million in average loans, partially from the BNB merger and partially from organic growth, and a $38.6 million increase in investment securities. The decrease in the average rate earned was primarily due to general decreases in market rates.

Interest expense decreased primarily due to a $5.4 million decrease in average long term debt, primarily due the payment in full of a $5.0 million advance from the Federal Home Loan Bank of Cincinnati during the first quarter 2015, and to a 1 basis point decrease in the average rate paid on total interest-bearing liabilities.

2014 vs. 2013. Net interest income on a fully tax-equivalent basis for 2014 totaled $37,285,000, an increase of $6,528,000 from 2013. The increase resulted from an increase in total taxable-equivalent interest income of $6,053,000 and a decrease in total interest expense of $475,000.

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The increase in taxable-equivalent interest income was due to a $157.3 million increase in total average interest-earning assets, slightly offset by a 3 basis point decrease in the average rate earned on interest-earning assets. The increase in total average interest-earning assets reflects an increase of $123.6 million in average loans, primarily from the Eaton National merger, and a $30.5 million increase in investment securities. The decrease in the average rate earned was primarily due to general decreases in market rates.

Interest expense decreased primarily due to a 15 basis point decrease in the average rate paid on interest-bearing liabilities, partially offset by a $113.4 million increase in total average interest-bearing liabilities. Deposit accounts (savings deposits, NOW and money fund deposits, and IRA and time certificates) grew a combined total of $116.7 million on an average basis, while average short-term borrowings decreased $2.1 million, while average long-term debt decreased $1.2 million. The growth in deposits was primarily due to the Eaton National merger. The decrease in average rates paid was primarily due to general decreases in market rates.

The net interest margin, on a taxable-equivalent basis, increased from 3.57% for 2013 to 3.66% for 2014, the net effect of declines in both yields on earning assets and rates paid on liabilities, as indicated above.

Provisions and Allowance for Loan Losses

The following table presents the total loan loss provision and the other changes in the allowance for loan losses for the years 2011 through 2015:

	2015	2014	2013	2012	2011
	(Dollars in thousands)				
Balance – Beginning of year	$3,121	3,588	3,437	2,931	2,641
Loans charged off:					
Commercial and industrial	100	261	119	159	581
Commercial, secured by real estate	1,133	573	58	234	598
Residential real estate	304	652	244	486	512
Consumer	52	129	181	134	252
Agricultural	67	—	—	—	—
Other loans, including deposit overdrafts	74	79	67	85	127
Total loans charged off	1,730	1,694	669	1,098	2,070
Recoveries:					
Commercial and industrial	7	42	4	—	—
Commercial, secured by real estate	96	63	26	71	30
Residential real estate	107	40	31	7	31
Consumer	60	108	127	123	122
Agricultural	67	—	—	—	—
Other loans, including deposit overdrafts	35	44	44	52	88
Total recoveries	372	297	232	253	271
Net charge offs	1,358	1,397	437	845	1,799
Provision charged to operations	1,366	930	588	1,351	2,089
Balance - End of year	$3,129	3,121	3,588	3,437	2,931
Ratio of net charge-offs during the period to average loans outstanding	0.18 %	0.21 %	0.08 %	0.18 %	0.39 %
Ratio of allowance for loan losses to total loans at year-end	0.41 %	0.45 %	0.62 %	0.76 %	0.64 %

Charge-offs for the commercial, secured by real estate category had an elevated balance during 2015 due to the sale of impaired loans. Charge-offs for the commercial and industrial loan category for 2014 included a charge-off of $222,000 on one loan and charge-offs in the commercial, secured by real estate category for the same year included charge-offs totaling $469,000 on three loans. The $581,000 of charge-offs in the commercial and industrial loan category for 2011 is comprised of a $251,000 charge-off connected to a retail business that ceased operations during that year and the remaining $330,000 is due to one borrower. Commercial real estate charge-offs for 2011 consisted of loans to five different borrowers.

Charge-offs and recoveries classified as “Other” represent charge-offs and recoveries on checking and NOW account overdrafts. LCNB charges off such overdrafts when considered uncollectible, but no later than 60 days from the date first overdrawn.

LCNB continuously reviews the loan portfolio for credit risk through the use of its lending and loan review functions. Independent loan reviews analyze specific loans, providing validation that credit risks are appropriately identified and reported to the Loan Committee and Board of Directors. In addition, the Board of Directors' Audit Committee receives loan review reports throughout each year. New credits meeting specific criteria are analyzed prior to origination and are reviewed by the Loan Committee and Board of Directors.
Inputs from all of the Bank's credit risk identification processes are used by management to analyze and validate the adequacy and methodology of the allowance quarterly. The analysis includes two basic components: specific allocations for individual loans and general loss allocations for pools of loans based on average historic loss ratios for the thirty-six preceding months adjusted for identified economic and other risk factors. Due to the number, size, and complexity of loans within the loan portfolio, there is always a possibility of inherent undetected losses.

The following table presents the components of the allowance for loan losses on the dates specified:

	At December 31,								
	2015			2014			2013		
	Amount	Percent		Amount	Percent		Amount	Percent	
	(Dollars in thousands)								
Specific allocations	$363	11.6	%	$817	26.2	%	$1,032	28.8	%
General allocations:									
Historical loss	1,044	33.4	%	943	30.2	%	982	27.4	%
Adjustments to historical loss	1,722	55.0	%	1,361	43.6	%	1,574	43.8	%
Total	$3,129	100.0	%	$3,121	100.0	%	$3,588	100.0	%

Non-Interest Income

2015 vs. 2014. Total non-interest income for 2015 was $981,000 greater than for 2014 primarily due to increases in trust income, net gains on sales of securities, and gains from sales of mortgage loans. Trust income increased $359,000 primarily due to an increase in the fair value of trust assets and brokerage accounts managed. Net gains from sales of securities increased $346,000 and gains from sales of mortgage loans increased $196,000 primarily due to higher sales volumes.

2014 vs. 2013. Total non-interest income for 2014 was $52,000 greater than for 2013 primarily due to increases in trust income, service charges and fees on deposit accounts, and other operating income. Trust income increased $385,000 primarily due to an increase in the fair value of trust assets and brokerage accounts managed along with fee adjustments that became effective July 1, 2013. Service charges and fees on deposit accounts increased $683,000 primarily due to a greater number of deposit accounts resulting from the merger with Eaton National. Contributing to the increase in other operating income was a $78,000 increase in fee income from loans serviced for others, primarily due to increases in the servicing portfolio from the merger with Eaton National. These favorable increases were largely offset by a $911,000 decrease in net gains from sales of securities and a $192,000 decrease in gains from sales of mortgage loans primarily due to lower volumes of sales.

Non-Interest Expense

2015 vs. 2014. Total non-interest expense was $1,548,000 greater in 2015 than in 2014 primarily due to a $1,831,000 increase in salaries and employee benefits, partially offset by a $757,000 decrease in merger related expenses (consisting primarily of professional fees, data system conversion costs, and employee severance payments). Salaries and employee benefits and occupancy expenses increased due to salary and wage increases, employees retained from the BNB and Eaton National acquisitions, an increase in the number of employees outside of the acquisitions, and increased retirement plan expenses. Costs related to the acquisition of BNB in April 2015 were less than the costs associated with the acquisition of Eaton National in January 2014.

Amortization of intangibles increased $126,000 due to amortization of BNB's core deposit intangible. Other real estate owned expenses increased $204,000 primarily due to impairment charges recognized on a commercial property.

2014 vs. 2013. Total non-interest expense was $4,632,000 greater in 2014 than in 2013 largely due to a $2,275,000 increase in salaries and employee benefits and smaller increases in other line items. Salaries and employee benefits, as well as a variety of other expense items, increased due to the increased number of employees and offices resulting from the Eaton National merger. Occupancy expenses increased $190,000 due to increased real estate taxes, utilities, rental, and maintenance and repair costs, primarily reflecting costs required by the additional offices from the Eaton National merger. Marketing costs increased $142,000 primarily due to greater usage of television and print advertising during 2014. Amortization of intangibles increased $240,000 due to amortization of Eaton National's core deposit intangible, partially offset by the amortization in full of Sycamore National Bank's ("Sycamore") core deposit intangible during 2013. Other real estate owned expenses increased $315,000 primarily due to the absence of a gain recognized on the sale of commercial property during the first quarter 2013.

Income Taxes

LCNB's effective tax rates for the years ended December 31, 2015, 2014, and 2013 were 26.9%, 25.5%, and 25.1%, respectively. The difference between the statutory rate of 34.0% and the effective tax rate is primarily due to tax-exempt interest income and tax-exempt earnings from bank owned life insurance.

Assets

The carrying values of loans, premises and equipment, and deposits were greatly influenced by the merger with BNB. See Note 2 - Acquisition to the Consolidated Financial Statements for a description of the merger and a summary of the fair values of BNB's assets and liabilities added to LCNB's consolidated balance sheet.

Available-for-sale investment securities increased $92.6 million during 2015. Included in the increase were $58.2 million in investment securities obtained through the acquisition of BNB. During 2015, LCNB purchased $163.9 million in new securities. These additions were partially offset by sales, maturities, and calls of investment securities.

Net loans increased $72.0 million during 2015. The BNB merger added $34.7 million of net loans to LCNB's loan portfolio as of the merger date. The remainder of the net increase was due to new loan origination. The increase in the loan portfolio does not reflect $7.7 million of residential fixed-rate real estate loans that were originated and sold to the Federal Home Loan Mortgage Corporation during 2015.

Deposits

Total deposits at December 31, 2015 were $141.0 million greater than at December 31, 2014, including $99.1 million of new deposits obtained through the BNB acquisition and and a $24.0 million increase in public fund deposits by local government entities. Public fund deposits can be relatively volatile due to seasonal tax collections and the financial needs of the local entities.

Liquidity

Liquidity is the ability to have funds available at all times to meet the commitments of LCNB. These commitments may include paying dividends to shareholders, funding new loans for borrowers, funding withdrawals by depositors, paying general and administrative expenses, and funding capital expenditures. Sources of liquidity include growth in deposits, principal payments received on loans, proceeds from the sale of loans, the sale or maturation of investment securities, cash generated by operating activities, and the ability to borrow funds. Management closely monitors the level of liquid assets available to meet ongoing funding requirements. It is management's intent to maintain adequate liquidity so that sufficient funds are readily available at a reasonable cost. LCNB experienced no liquidity or operational problems during the past year as a result of current liquidity levels.

The liquidity of LCNB is enhanced by the fact that 84.3% of total deposits at December 31, 2015 were "core" deposits. Core deposits, for this purpose, are defined as total deposits less public funds and certificates of deposit greater than $100,000.

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LCNB CORP. AND SUBSIDIARIES

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

Liquid assets include cash and cash equivalents, federal funds sold and securities available-for-sale. Except for investments in the stock of the Federal Reserve Bank and the Federal Home Loan Bank of Cincinnati (“FHLB”) and certain local municipal securities, all of LCNB's investment portfolio is classified as "available-for-sale" and can be readily sold to meet liquidity needs, subject to certain pledging commitments for public funds, repurchase agreements, and other requirements. At December 31, 2015, LCNB's liquid assets amounted to $393.0 million or 30.7% of total assets, compared to $301.2 million or 27.2% of total assets at December 31, 2014. The ratio for 2015 is larger because of an increase in securities available-for-sale.

An additional source of funding is borrowings from the FHLB. Long-term advances totaling $5.9 million were outstanding at December 31, 2015. LCNB is approved to borrow up to $55.3 million in short-term advances through the FHLB’s Cash Management Advance program. Total remaining available borrowing capacity, including short-term advances, with the FHLB at December 31, 2015 was approximately $99.6 million. One of the factors limiting availability of FHLB borrowings is a bank’s ownership of FHLB stock. LCNB could increase its available borrowing capacity by purchasing more FHLB stock.

Besides short-term FHLB advances, short-term borrowings may include repurchase agreements, federal funds purchased, and advances from a line of credit with another financial institution. At December 31, 2015, LCNB could borrow up to $20 million through the line of credit and up to $17 million under federal funds arrangements with two other financial institutions.

Commitments to extend credit at December 31, 2015 totaled $118.9 million, including standby letters of credit totaling $0.5 million, and are more fully described in Note 14 - Commitments and Contingent Liabilities to LCNB's Financial Statements. Since many commitments to extend credit may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

The following table provides information concerning LCNB's contractual obligations at December 31, 2015:

	Payments due by period				
	Total	1 year or less	Over 1 through 3 years	Over 3 through 5 years	More than 5 years
	(In thousands)				
Short-term borrowings	$37,387	37,387	—	—	—
Long-term debt obligations	5,947	349	5,543	55	—
Operating lease obligations	5,206	479	634	259	3,834
Estimated pension plan contribution for 2016	200	200	—	—	—
Commitment to purchase municipal security when issued	7,630	7,630	—	—	—
Funding commitment for affordable housing tax credit limited partnership	907	291	326	91	199
Estimated capital expenditure obligations	11,026	11,026	—	—	—
Certificates of deposit:					
$100,000 and over	74,055	23,699	20,578	28,042	1,736
Other time certificates	143,900	62,205	36,914	42,275	2,506
Total	$286,258	143,266	63,995	70,722	8,275

During January 2016, LCNB prepaid in full a $5.0 million advance from the FHLB, which is included in the table above in the long-term debt obligations line, over 1 through 3 years. Since the prepaid advance had an interest rate of 5.25%, the average rate on remaining advances will decrease significantly.

The following table provides information concerning LCNB's commitments at December 31, 2015:

		Amount of Commitment Expiration Per Period			
	Total Amounts Committed	1 year or less	Over 1 through 3 years	Over 3 through 5 years	More than 5 years
	(In thousands)				
Commitments to extend credit	$11,815	11,815	—	—	—
Unused lines of credit	106,588	52,035	22,312	19,462	12,779
Standby letters of credit	457	453	4	—	—
Total	$118,860	64,303	22,316	19,462	12,779

Capital Resources

LCNB and the Bank are required by banking regulators to meet certain minimum levels of capital adequacy. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a material effect on LCNB's and the Bank's financial statements. These minimum levels are expressed in the form of certain ratios. Capital is separated into Tier 1 capital (essentially shareholders' equity less goodwill and other intangibles) and Tier 2 capital (essentially the allowance for loan losses limited to 1.25% of risk-weighted assets). Common Equity Tier 1 Capital is the sum of common stock, related surplus, and retained earnings, net of treasury stock, accumulated other comprehensive income, and other adjustments. The first three ratios, which are based on the degree of credit risk in the Bank's assets, provide for weighting assets based on assigned risk factors and include off-balance sheet items such as loan commitments and stand-by letters of credit. The ratio of Common Equity Tier 1 Capital to risk weighted assets must be at least 4.50%. The ratio of Tier 1 capital to risk-weighted assets must be at least 6.00% and the ratio of total capital (Tier 1 capital plus Tier 2 capital) to risk-weighted assets must be at least 8.00%. The capital leverage ratio supplements the risk-based capital guidelines. Banks are required to maintain a minimum ratio of Tier 1 capital to adjusted quarterly average total assets of 4.00%. A table summarizing the regulatory capital of LCNB and the Bank at December 31, 2015 and 2014 is included in Note 15 - Regulatory Matters of the consolidated financial statements.

The FDIC, the insurer of deposits in financial institutions, has adopted a risk-based insurance premium system based in part on an institution's capital adequacy. Under this system, a depository institution is required to pay successively higher premiums depending on its capital levels and its supervisory rating by its primary regulator. It is management's intention to maintain sufficient capital to permit the Bank to maintain a "well capitalized" designation (the FDIC's highest rating).

On April 17, 2001, LCNB's Board of Directors authorized three separate stock repurchase programs, two of which continue to be in effect – the “Market Repurchase Program” and the “Private Sale Repurchase Program.” Any shares purchased will be held for future corporate purposes.

Under the Market Repurchase Program, LCNB was originally authorized to purchase up to 200,000 shares of its stock, as restated for a 100% stock dividend issued in May, 2007, through market transactions with a selected stockbroker. On November 14, 2005, the Board of Directors extended the Market Repurchase Program by increasing the shares authorized for repurchase to 400,000 total shares, as restated for a stock dividend. Through December 31, 2015, 290,444 shares, as restated for the stock dividend, had been purchased under this program. No shares were purchased under this program during 2015.

The Private Sale Repurchase Program is available to shareholders who wish to sell large blocks of stock at one time. Because LCNB's stock is not widely traded, a shareholder releasing large blocks may not be able to readily sell all shares through normal procedures. Purchases of blocks will be considered on a case-by-case basis and will be made at prevailing market prices. A total of 466,018 shares, as restated for the stock dividend, had been purchased under this program at December 31, 2015. No shares were purchased under this program during 2015.

LCNB established an Ownership Incentive Plan during 2002 that allowed for stock-based awards to eligible employees. Under the plan, awards could be in the form of stock options, share awards, and/or appreciation rights. The plan provided for the issuance of up to 200,000 shares, as restated for a stock dividend. The plan expired on April 16, 2012. Any outstanding unexercized options, however, continue to be exercisable in accordance with their terms.

On January 9, 2009, LCNB issued 13,400 shares of Fixed Rate Cumulative Preferred Stock, Series A and a warrant for the purchase of 217,063 common shares of LCNB stock at an exercise price of $9.26 per share to the U.S. Treasury Department. LCNB allocated $583,000 of the proceeds from the preferred stock issuance to the warrant. The warrant carries a ten year term and was 100% vested at grant. On October 21, 2009, LCNB redeemed the preferred stock that had been issued under the Capital Purchase Program agreement, but did not redeem the warrant. The Treasury Department sold the warrant to an investor during the fourth quarter 2011.

Critical Accounting Policies

Allowance for Loan Losses. The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that the collectibility of the principal is unlikely. Subsequent recoveries, if any, are credited to the allowance. The allowance is an amount that management believes will be adequate to absorb inherent losses in the loan portfolio, based on evaluations of the collectibility of loans and prior loan loss experience. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, and current economic conditions that may affect the borrowers' ability to pay. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.
The allowance consists of specific and general components. The specific component relates to loans that are classified as doubtful, substandard, or special mention. For such loans an allowance is established when the discounted cash flows or collateral value is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors, which include trends in underperforming loans, trends in the volume and terms of loans, economic trends and conditions, concentrations of credit, trends in the quality of loans, and borrower financial statement exceptions.

Based on its evaluations, management believes that the allowance for loan losses will be adequate to absorb estimated losses inherent in the current loan portfolio.

Acquired Credit Impaired Loans. LCNB accounts for acquisitions using the acquisition method of accounting, which requires that assets acquired and liabilities assumed be measured at their fair values at the acquisition date. Acquired loans are reviewed to determine if there is evidence of deterioration in credit quality since inception and if it is probable that LCNB will be unable to collect all amounts due under the contractual loan agreements. The analysis includes expected prepayments and estimated cash flows including principal and interest payments at the date of acquisition. The amount in excess of the estimated future cash flows is not accreted into earnings. The amount in excess of the estimated future cash flows over the book value of the loan is accreted into interest income over the remaining life of the loan (accretable yield). LCNB records these loans on the acquisition date at their net realizable value. Thus, an allowance for estimated future losses is not established on the acquisition date. Subsequent to the date of acquisition, expected future cash flows on loans acquired are updated and any losses or reductions in estimated cash flows which arise subsequent to the date of acquisition are reflected as a charge through the provision for loan losses. An increase in the expected cash flows adjusts the level of the accretable yield recognized on a prospective basis over the remaining life of the loan. Due to the number, size, and complexity of loans within the acquired loan portfolio, there is always a possibility of inherent undetected losses.

Accounting for Intangibles. LCNB’s intangible assets at December 31, 2015 are composed primarily of goodwill and core deposit intangibles related to the acquisitions of Sycamore during the fourth quarter 2007, First Capital during the first quarter 2013, Eaton National during the first quarter 2014, and BNB during the second quarter 2015. It also includes mortgage servicing rights recorded from sales of fixed-rate mortgage loans. Goodwill is not subject to amortization, but is reviewed annually for impairment. The core deposit intangible for Sycamore was amortized on a straight line basis over six years. The core deposit intangible for First Capital and BNB is being amortized on a straight line basis over nine years. The core deposit intangible for Eaton National is being amortized on a straight line basis over eight years. Mortgage servicing rights are capitalized by allocating the total cost of loans between mortgage servicing rights and the loans based on their estimated fair values. Capitalized mortgage servicing rights are amortized to loan servicing income in proportion to and over the period of estimated servicing income, subject to periodic review for impairment.

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Fair Value Accounting for Investment Securities. Securities classified as available-for-sale are carried at estimated fair value. Unrealized gains and losses, net of taxes, are reported as accumulated other comprehensive income or loss in shareholders' equity. Fair value is estimated using market quotations for U.S. Treasury and equity investments. Fair value for the majority of the remaining available-for-sale securities is estimated using the discounted cash flow method for each security with discount rates based on rates observed in the market.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Market risk for LCNB is primarily interest rate risk. LCNB attempts to mitigate this risk through asset/liability management strategies designed to decrease the vulnerability of its earnings to material and prolonged changes in interest rates. LCNB does not use derivatives such as interest rate swaps, caps or floors to hedge this risk. LCNB has not entered into any market risk instruments for trading purposes.

The Bank's Asset and Liability Management Committee ("ALCO") primarily uses a combination of Interest Rate Sensitivity Analysis (IRSA) and Economic Value of Equity (EVE) analysis for measuring and managing interest rate risk. The IRSA model is used to estimate the effect on net interest income during a one-year period of instantaneous and sustained movements in interest rates, also called interest rate shocks, of 100, 200, and 300 basis points. Management considers the results of any significant downward scenarios to not be meaningful in the current interest rate environment. The base projection uses a current interest rate scenario. As shown below, the December 31, 2015 IRSA indicates that an increase in interest rates at all shock levels will have a positive effect on net interest income. The changes in net interest income for all rate assumptions are within LCNB’s acceptable ranges.

Rate Shock Scenario in Basis Points	Amount (In thousands)	$ Change in Net Interest Income	% Change in Net Interest Income
Up 300	$42,163	3,074	7.86 %
Up 200	41,110	2,021	5.17 %
Up 100	40,089	1,000	2.56 %
Base	39,089	—	— %

IRSA shows the effect on net interest income during a one-year period only. A more long-range model is the EVE analysis, which shows the estimated present value of future cash inflows from interest-earning assets less the present value of future cash outflows for interest-bearing liabilities for the same rate shocks. As shown below, the December 31, 2015 EVE analysis indicates that an increase in interest rates would have a negative effect on the EVE for all shock levels. The changes in the EVE for all rate assumptions are within LCNB’s acceptable ranges.

Rate Shock Scenario in Basis Points	Amount (In thousands)	$ Change in EVE	% Change in EVE
Up 300	$135,725	(3,473)	(2.50)%
Up 200	136,319	(2,879)	(2.07)%
Up 100	137,176	(2,022)	(1.45)%
Base	139,198	—	— %

The IRSA and EVE simulations discussed above are not projections of future income or equity and should not be relied on as being indicative of future operating results. Assumptions used, including the nature and timing of interest rate levels, yield curve shape, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, and reinvestment or replacement of asset and liability cash flows, are inherently uncertain and, as a result, the models cannot precisely measure future net interest income or equity. Furthermore, the models do not reflect actions that borrowers, depositors, and management may take in response to changing economic conditions and interest rate levels.

Item 8. Financial Statements and Supplementary Data

REPORT OF MANAGEMENT'S ASSESSMENT OF INTERNAL CONTROL OVER FINANCIAL REPORTING

LCNB Corp. ("LCNB") is responsible for the preparation, integrity, and fair presentation of the consolidated financial statements included in this annual report. Management of LCNB and its subsidiaries is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15f. LCNB's internal control over financial reporting is a process designed under the supervision of LCNB's Chief Executive Officer and the Chief Financial Officer. The purpose is to provide reasonable assurance to the Board of Directors regarding the reliability of financial reporting and the preparation of LCNB's consolidated financial statements for external purposes in accordance with U.S. generally accepted accounting principles.

Management maintains internal controls over financial reporting. The internal controls contain control processes and actions are taken to correct deficiencies as they are identified. The internal controls are evaluated on an ongoing basis by LCNB's management and Audit Committee. Even effective internal controls, no matter how well designed, have inherent limitations – including the possibility of circumvention or overriding of controls – and therefore can provide only reasonable assurance with respect to financial statement preparation. Also, because of changes in conditions, internal control effectiveness may vary over time.

Management assessed LCNB's internal controls as of December 31, 2015, in relation to criteria for effective internal control over financial reporting described in "Internal Control – Integrated Framework (2013)" issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. Based on this assessment, management believes that, as of December 31, 2015, LCNB's internal control over financial reporting met the criteria.

BKD LLP, an independent registered public accounting firm, has issued an attestation report on the effectiveness of LCNB's internal control over financial reporting as of December 31, 2015.

Submitted by:

LCNB Corp.

/s/ Steve P. Foster	/s/ Robert C. Haines II
Steve P. Foster	Robert C. Haines II
Chief Executive Officer & President	Executive Vice President &
March 9, 2016	Chief Financial Officer
	March 9, 2016

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LCNB CORP. AND SUBSIDIARIES

Report of Independent Registered Public Accounting Firm

Audit Committee, Board of Directors and Shareholders
LCNB Corp.
Lebanon, Ohio

We have audited LCNB Corp. and subsidiaries' (Company) internal control over financial reporting as of December 31, 2015, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the Companying management's assessment of internal control over financial reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because management's assessment and our audit were also conducted to meet the reporting requirements of Section 112 of the Federal Deposit Insurance Corporation Improvement Act (FDICIA), our examination of LCNB Corp.'s internal control over financial reporting included controls over the preparation of financial statements in accordance with accounting principles generally accepted in the United States of America and with the instructions to the Consolidated Financial Statements for Bank Holding Companies (Form FR Y-9C). A Company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, LCNB Corp. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2015, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements of LCNB Corp. and subsidiaries and our report dated March 9, 2016, expressed an unqualified opinion thereon.

/s/ BKD, LLP
BKD, LLP

Cincinnati, Ohio
March 9, 2016

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LCNB CORP. AND SUBSIDIARIES

Report of Independent Registered Public Accounting Firm

Audit Committee, Board of Directors and Shareholders
LCNB Corp.
Lebanon, Ohio

We have audited the accompanying consolidated balance sheets of LCNB Corp. and subsidiaries as of December 31, 2015 and 2014, and the related consolidated statements of income, comprehensive income, shareholders’ equity and cash flows for each of the years in the two-year period ended December 31, 2015. The Company's management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. Our audit included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of LCNB Corp. and subsidiaries as of December 31, 2015 and 2014, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2015, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), LCNB Corp. and subsidiaries' internal control over financial reporting as of December 31, 2015, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 9, 2016, expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ BKD, LLP
BKD, LLP

Cincinnati, Ohio
March 9, 2016

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LCNB CORP. AND SUBSIDIARIES

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
LCNB Corp.
Lebanon, Ohio

We have audited the accompanying consolidated statements of income, comprehensive income, shareholders' equity, and cash flows of LCNB Corp. and Subsidiaries ("LCNB") for the year ended December 31, 2013. LCNB's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated results of operations and cash flows for LCNB for the year ended December 31, 2013, in conformity with U.S. generally accepted accounting principles.

/s/ Clark, Schaefer, Hackett & Co. (successor of J. D. Cloud & Co. L.L.P., through merger)
Clark, Schaefer, Hackett & Co. (successor of J. D. Cloud & Co. L.L.P., through merger)

Cincinnati, Ohio
March 3, 2014

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LCNB CORP. AND SUBSIDIARIES

FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA
LCNB CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
At December 31,
(Dollars in thousands)

	2015	2014
ASSETS:		
Cash and due from banks	$14,155	14,235
Interest-bearing demand deposits	832	1,610
Total cash and cash equivalents	14,987	15,845
Investment securities:		
Available-for-sale, at fair value	377,978	285,365
Held-to-maturity, at cost	22,633	22,725
Federal Reserve Bank stock, at cost	2,732	2,346
Federal Home Loan Bank stock, at cost	3,638	3,638
Loans, net	767,809	695,835
Premises and equipment, net	22,100	20,733
Goodwill	30,183	27,638
Core deposit and other intangibles	5,396	4,780
Bank owned life insurance	22,561	21,936
Other assets	10,514	7,225
TOTAL ASSETS	$1,280,531	1,108,066
LIABILITIES:		
Deposits:		
Noninterest-bearing	$250,306	213,303
Interest-bearing	836,854	732,902
Total deposits	1,087,160	946,205
Short-term borrowings	37,387	16,645
Long-term debt	5,947	11,357
Accrued interest and other liabilities	9,929	8,164
TOTAL LIABILITIES	1,140,423	982,371
COMMITMENTS AND CONTINGENT LIABILITIES		
SHAREHOLDERS' EQUITY:		
Preferred shares - no par value, authorized 1,000,000 shares, none outstanding	—	—
Common shares - no par value, authorized 12,000,000 shares, issued 10,679,174 and 10,064,945 shares at December 31, 2015 and 2014, respectively	76,908	67,181
Retained earnings	74,629	69,394
Treasury shares at cost, 753,627 shares at December 31, 2015 and 2014	(11,665)	(11,665)
Accumulated other comprehensive income (loss), net of taxes	236	785
TOTAL SHAREHOLDERS' EQUITY	140,108	125,695

TOTAL LIABILITES AND SHAREHOLDERS' EQUITY	$1,280,531	1,108,066

The accompanying notes to consolidated financial statements are an integral part of these statements.

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LCNB CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
For the years ended December 31,
(Dollars in thousands, except per share data)

	2015	2014	2013
INTEREST INCOME:			
Interest and fees on loans	$35,285	32,706	27,325
Interest on investment securities:			
Taxable	4,197	3,757	3,369
Non-taxable	2,848	2,713	2,573
Other investments	329	301	230
TOTAL INTEREST INCOME	42,659	39,477	33,497
INTEREST EXPENSE:			
Interest on deposits	3,009	3,161	3,602
Interest on short-term borrowings	24	22	25
Interest on long-term debt	295	407	438
TOTAL INTEREST EXPENSE	3,328	3,590	4,065
NET INTEREST INCOME	39,331	35,887	29,432
PROVISION FOR LOAN LOSSES	1,366	930	588
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	37,965	34,957	28,844
NON-INTEREST INCOME:			
Trust income	3,262	2,903	2,518
Service charges and fees on deposit accounts	4,920	4,838	4,155
Net gain on sales of securities	495	149	1,060
Bank owned life insurance income	625	671	678
Gains from sales of mortgage loans	343	147	339
Other operating income	478	434	340
TOTAL NON-INTEREST INCOME	10,123	9,142	9,090
NON-INTEREST EXPENSE:			
Salaries and employee benefits	17,593	15,762	13,487
Equipment expenses	1,257	1,316	1,232
Occupancy expense, net	2,307	2,232	2,042
State franchise tax	1,001	955	846
Marketing	720	703	561
Amortization of intangibles	700	574	334
FDIC premiums	598	660	499
ATM expense	698	624	534
Computer maintenance and supplies	782	794	616
Telephone expense	707	690	566
Contracted services	842	880	568
Other real estate owned	489	285	(30)
Merger-related expenses	643	1,400	1,433
Other non-interest expense	4,055	3,969	3,524
TOTAL NON-INTEREST EXPENSE	32,392	30,844	26,212

INCOME BEFORE INCOME TAXES	15,696	13,255	11,722
PROVISION FOR INCOME TAXES	4,222	3,386	2,942
NET INCOME	$11,474	9,869	8,780
Earnings per common share:			
Basic	$1.18	1.06	1.12
Diluted	1.17	1.05	1.10
Weighted average shares outstanding:			
Basic	9,704,965	9,297,019	7,852,514
Diluted	9,811,476	9,406,346	7,982,997

The accompanying notes to consolidated financial statements are an integral part of these statements.

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LCNB CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
For the years ended December 31,
(Dollars in thousands)

	2015	2014	2013
Net income	$11,474	9,869	8,780
Other comprehensive income (loss):			
Net unrealized gain (loss) on available-for-sale securities (net of taxes of $169, $1,476, and $2,940 for 2015, 2014, and 2013, respectively)	(329)	2,865	(5,706)
Change in nonqualified pension plan unrecognized net gain (loss) and unrecognized prior service cost (net of taxes of $55, $133, and $38 for 2015, 2014, and 2013, respectively)	107	(260)	73
Reclassification adjustment for:			
Net realized gain on sale of available-for-sale securities included in net income (net of taxes of $168, $51, and $418 for 2015, 2014 and 2013, respectively)	(327)	(98)	(810)
Other comprehensive income (loss)	(549)	2,507	(6,443)
TOTAL COMPREHENSIVE INCOME	$10,925	12,376	2,337
SUPPLEMENTAL INFORMATION: COMPONENTS OF ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX, AS OF YEAR-END:			
Net unrealized gain (loss) on securities available-for-sale	$469	1,125	(1,642)
Net unfunded liability for nonqualified pension plan	(233)	(340)	(80)
Balance at year-end	$236	785	(1,722)

The accompanying notes to consolidated financial statements are an integral part of these statements.

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LCNB CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
For the years ended December 31,
(Dollars in thousands, except share data)

	Common Shares Outstanding	Common Shares	Retained Earnings	Treasury Shares	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance, December 31, 2012	6,731,900	$27,107	61,843	(11,665)	4,721	82,006
Net income			8,780			8,780
Other comprehensive gain (loss), net of taxes					(6,443)	(6,443)
Issuance of common stock	1,642,857	26,909				26,909
Dividend Reinvestment and Stock Purchase Plan	18,348	329				329
Acquisition of First Capital Bancshares, Inc.	888,811	12,321				12,321
Exercise of stock options	5,620	70				70
Excess tax benefit on exercise and forfeiture of stock options		12				12
Compensation expense relating to stock options		37				37
Common stock dividends, $0.64 per share			(5,148)			(5,148)
Balance, December 31, 2013	9,287,536	66,785	65,475	(11,665)	(1,722)	118,873
Net income			9,869			9,869
Other comprehensive gain (loss), net of taxes					2,507	2,507
Dividend Reinvestment and Stock Purchase Plan	23,782	372				372
Compensation expense relating to stock options		24				24
Common stock dividends, $0.64 per share			(5,950)			(5,950)
Balance, December 31, 2014	9,311,318	67,181	69,394	(11,665)	785	125,695
Net income			11,474			11,474
Other comprehensive gain (loss), net of taxes					(549)	(549)
Dividend Reinvestment and Stock Purchase Plan	24,610	390				390
Acquisition of BNB Bancorp, Inc.	560,132	9,063				9,063
Exercise of stock options	13,449	152				152
Excess tax benefit on exercise and forfeiture of stock options		13				13
Compensation expense relating to stock options		19				19
	16,038	90				90

Compensation expense relating to restricted stock						
Common stock dividends, $0.64 per share			(6,239)			(6,239)
Balance, December 31, 2015	9,925,547	$76,908	74,629	(11,665)	236	140,108

The accompanying notes to consolidated financial statements are an integral part of these statements.

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LCNB CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the years ended December 31,
(Dollars in thousands)

	2015	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$11,474	9,869	8,780
Adjustments to reconcile net income to net cash flows from operating activities-			
Depreciation, amortization and accretion	2,997	2,991	2,212
Provision for loan losses	1,366	930	588
Deferred income tax provision (benefit)	(58)	192	192
Increase in cash surrender value of bank owned life insurance	(625)	(671)	(678)
Realized gain on sales of securities available-for-sale	(495)	(149)	(1,060)
Realized loss (gain) on sale of premises and equipment	(1)	(128)	18
Realized loss (gain) from sale and write-downs of other real estate owned and repossessed assets	378	85	(182)
Origination of mortgage loans for sale	(7,725)	(7,480)	(19,267)
Realized gains from sales of loans	(343)	(147)	(339)
Proceeds from sales of loans	7,809	7,552	19,415
Compensation expense related to stock options	19	24	37
Compensation expense related to restricted stock	90	—	—
Increase (decrease) due to changes in assets and liabilities:			
Income receivable	(160)	414	100
Other assets	(3,302)	1,898	370
Other liabilities	1,815	560	248
TOTAL ADJUSTMENTS	1,765	6,071	1,654
NET CASH FLOWS FROM OPERATING ACTIVITIES	13,239	15,940	10,434
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sales of investment securities available-for-sale	97,981	67,296	59,284
Proceeds from maturities and calls of investment securities:			
Available-for-sale	29,700	36,716	26,496
Held-to-maturity	3,515	4,688	9,172
Purchases of investment securities:			
Available-for-sale	(163,859)	(92,180)	(74,083)
Held-to-maturity	(3,413)	(11,090)	(9,687)
Proceeds from redemption of Federal Reserve Bank stock	—	41	—
Purchase of Federal Reserve Bank stock	(256)	(743)	(497)
Proceeds from sale of impaired loans	4,559	—	—
Net (increase) decrease in loans	(42,530)	(10,081)	(21,352)
Proceeds from redemption of bank owned life insurance	—	3,633	—
Proceeds from sales of other real estate owned and repossessed assets	245	750	1,173
Additions to other real estate owned	(20)	(45)	(7)
Purchases of premises and equipment	(504)	(1,052)	(858)
Proceeds from sales of premises and equipment	22	179	1
Net cash acquired from (paid for) acquisition	8,993	(9,114)	9,771

NET CASH FLOWS USED IN INVESTING ACTIVITIES	(65,567)	(11,002)	(587)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net increase (decrease) in deposits	41,822	(4,797)	(22,310)
Net increase (decrease) in short-term borrowings	20,742	7,339	(5,101)
Principal payments on long-term debt	(5,410)	(745)	(3,395)
Proceeds from issuance of common stock	66	58	26,950
Proceeds and excess tax benefit from exercise of stock options	165	—	82
Cash dividends paid on common stock	(5,915)	(5,636)	(4,860)
NET CASH FLOWS PROVIDED BY (USED IN) FINANCING ACTIVITIES	51,470	(3,781)	(8,634)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(858)	1,157	1,213
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	15,845	14,688	13,475
CASH AND CASH EQUIVALENTS AT END OF YEAR	$14,987	15,845	14,688
SUPPLEMENTAL CASH FLOW INFORMATION:			
CASH PAID DURING THE YEAR FOR:			
Interest	$3,396	3,502	4,097
Income taxes	4,820	2,610	3,685
SUPPLEMENTAL DISCLOSURES OF NON-CASH INVESTING ACTIVITY:			
Transfer from loans to other real estate owned and repossessed assets	79	435	131

The accompanying notes to consolidated financial statements are an integral part of these statements.

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LCNB CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

LCNB Corp. (the "Company" or “LCNB”), an Ohio corporation formed in December 1998, is a financial holding company whose principal activity is the ownership of LCNB National Bank (the "Bank"). The Bank was founded in 1877 and provides full banking services, including trust and brokerage services, to customers primarily in Southwestern and South Central Ohio.

BASIS OF PRESENTATION
The consolidated financial statements include the accounts of the Company and its subsidiaries. Significant intercompany accounts and transactions are eliminated in consolidation. The accounting and reporting policies of the Company conform with U.S. generally accepted accounting principles and with general practices in the banking industry.

Certain prior period data presented in the financial statements have been reclassified to conform with the current year presentation. These reclassifications had no effect on net income.

USE OF ESTIMATES
The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

CASH AND CASH EQUIVALENTS
For purposes of reporting cash flows, cash and cash equivalents include cash, balances due from banks, federal funds sold, and interest-bearing demand deposits with original maturities of three months or less. Deposits with other banks routinely have balances greater than FDIC insured limits. Management considers the risk of loss to be very low with respect to such deposits.

INVESTMENT SECURITIES
Certain municipal debt securities that management has the positive intent and ability to hold to maturity are classified as “held-to-maturity” and recorded at amortized cost. Securities not classified as held-to-maturity are classified as “available-for-sale” and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income, a separate component of shareholders’ equity. Amortization of premiums and accretion of discounts are recognized as adjustments to interest income using the level-yield method. Realized gains or losses from the sale of securities are recorded on the trade date and are computed using the specific identification method.

Declines in the fair value of securities below their cost that are deemed to be other-than-temporarily impaired and for which the Company does not intend to sell the securities and it is not more likely than not that the securities will be sold before the anticipated recovery of the impairment are separated into losses related to credit factors and losses related to other factors. The losses related to credit factors are recognized in earnings and losses related to other factors are recognized in other comprehensive income. In estimating other than temporary impairment losses, management considers the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, and the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. The Company's consolidated statements of income as of December 31, 2015, 2014, and 2013, do not reflect any such impairment.

Federal Home Loan Bank ("FHLB") stock is an equity interest in the Federal Home Loan Bank of Cincinnati. It can be sold only at its par value of $100 per share and only to the FHLB or to another member institution. In addition, the equity ownership rights are more limited than would be the case for a public company because of the oversight role exercised by the Federal Housing Finance Agency in the process of budgeting and approving dividends. Federal Reserve Bank stock is similarly restricted in marketability and value. Both investments are carried at cost, which is their par value.

FHLB and Federal Reserve Bank stock are both subject to minimum ownership requirements by member banks. The required investments in common stock are based on predetermined formulas.

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LCNB CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015
(Continued)
NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

LOANS
The Company’s loan portfolio includes most types of commercial and industrial loans, commercial loans secured by real estate, residential real estate loans, consumer loans, agricultural loans and other types of loans. Most of the properties collateralizing the loan portfolio are located within the Company’s market area.

Loans are stated at the principal amount outstanding, net of unearned income, deferred origination fees and costs, and the allowance for loan losses. Interest income is accrued on the unpaid principal balance. The delinquency status of a loan is based on contractual terms and not on how recently payments have been received. Generally, a loan is placed on non-accrual status when it is classified as impaired or there is an indication that the borrower’s cash flow may not be sufficient to make payments as they come due, unless the loan is well secured and in the process of collection. Subsequent cash receipts on non-accrual loans are recorded as a reduction of principal and interest income is recorded once principal recovery is reasonably assured. The current year's accrued interest on loans placed on non-accrual status is charged against earnings. Previous years' accrued interest is charged against the allowance for loan losses. Non-accrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer a reasonable doubt as to the timely collection of interest or principal.

Loan origination fees and certain direct loan origination costs are deferred and the net amount amortized as an adjustment of loan yields. These amounts are being amortized over the lives of the related loans.

In the ordinary course of business, the Company enters into off-balance sheet financial instruments consisting of commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the financial statements when they are funded. The credit risk associated with these commitments is evaluated in a manner similar to the allowance for loan losses.

ALLOWANCE FOR LOAN LOSSES
The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that the collectibility of the principal is unlikely. Consumer loans are charged off when they reach 120 days past due. Subsequent recoveries, if any, are credited to the allowance.

The provision for loan losses is determined by management based upon its evaluation of the amount needed to maintain the allowance for loan losses at a level considered appropriate in relation to the estimated risk of losses inherent in the portfolio. Current methodology used by management to estimate the allowance takes into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, historic categorical trends, current delinquency levels as related to historical levels, portfolio growth rates, changes in composition of the portfolio, the current economic environment, as well as current allowance adequacy in relation to the portfolio. Management is cognizant that reliance on historical information coupled with the cyclical nature of the economy, including credit cycles, affects the allowance. Management considers all of these factors prior to making any adjustments to the allowance due the subjectivity and imprecision involved in allocation methodology. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific and general components. The specific component relates to loans that are specifically reviewed for impairment. For such loans, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers loans not specifically reviewed for impairment and homogeneous loan pools, such as residential real estate and consumer loans. The general component is measured for each loan category separately based on each category's average of historical loss experience over a trailing thirty-six month period, adjusted for qualitative factors. Such qualitative factors may include current economic conditions if different from the three-year historical loss period, trends in underperforming loans, trends in volume and terms of loan categories, concentrations of credit, and trends in loan quality.

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LCNB CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015
(Continued)
NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

A loan is considered impaired when management believes, based on current information and events, it is probable that the Bank will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the loan agreement. An impaired loan is measured by the present value of expected future cash flows using the loan's effective interest rate. An impaired collateral-dependent loan may be measured based on collateral value. Smaller-balance homogeneous loans, including residential mortgage and consumer installment loans, that are not evaluated individually are collectively evaluated for impairment.

Loans acquired from the merger are recorded at fair value with no carryover of the acquired entity's previously established allowance for loan losses. The excess of expected cash flows over the estimated fair value of acquired loans is recognized as interest income over the remaining contractual lives of the loans using the level yield method.

Subsequent decreases in expected cash flows will require additions to the allowance for loan losses. Subsequent improvements in expected cash flows result in the recognition of additional interest income over the then-remaining contractual lives of the loans.

Impaired loans acquired are accounted for under FASB ASC 310-30. Factors considered in evaluating whether an acquired loan was impaired include delinquency status and history, updated borrower credit status, collateral information, and updated loan-to-value information. The difference between contractually required payments at the time of acquisition and the cash flows expected to be collected is referred to as the nonaccretable difference. The interest component of the cash flows expected to be collected is referred to as the accretable yield and is recognized as interest income over the remaining contractual life of the loan using the level yield method. Subsequent decreases in expected cash flows will require additions to the allowance for loan losses. Subsequent improvements in expected cash flows will result in a reclassification from the nonaccretable difference to the accretable yield.

PREMISES AND EQUIPMENT
Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed on both the straight-line and accelerated methods over the estimated useful lives of the assets, generally 15 to 40 years for premises and 3 to 10 years for equipment. Leasehold improvements are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. Costs incurred for maintenance and repairs are expensed as incurred.

OTHER REAL ESTATE OWNED
Other real estate owned includes properties acquired through foreclosure or deed in lieu of foreclosure. Such property is held for sale and is initially recorded at fair value, less costs to sell, establishing a new cost basis. Fair value is primarily based on a property appraisal obtained at the time of transfer and any periodic updates that may be obtained thereafter. The allowance for loan losses is charged for any write down of the loan’s carrying value to fair value at the date of acquisition. Any subsequent reductions in fair value and expenses incurred from holding other real estate owned are charged to other non-interest expense. Costs, excluding interest, relating to the improvement of other real estate owned are capitalized. Gains and losses from the sale of other real estate owned are included in other non-interest expense.

Other real estate owned also includes in-substance foreclosed properties, which are properties that the Company has taken physical control of, regardless of whether formal foreclosure proceedings have occurred.

GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill is the excess of the purchase price over the fair value of the net identifiable assets acquired in a business combination. Goodwill is not amortized, but is instead subject to an annual review for impairment.

Mortgage servicing rights on originated mortgage loans that have been sold are initially recorded at their estimated fair values. Mortgage servicing rights are amortized to loan servicing income in proportion to and over the period of estimated servicing income. Such assets are periodically evaluated as to the recoverability of their carrying value.

The Company's other intangible asset relates to core deposits acquired from business combinations. These intangible assets are amortized on a straight-line basis over their estimated useful lives. Management evaluates whether events or circumstances have occurred that indicate the remaining useful life or carrying value of the amortizing intangible should be revised.

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LCNB CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015
(Continued)
NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

BANK OWNED LIFE INSURANCE
The Company has purchased life insurance policies on certain officers of the Company. The Company is the beneficiary of these policies and has recorded the estimated cash surrender value in other assets in the consolidated balance sheets. Income on the policies, based on the increase in cash surrender value and any incremental death benefits, is included in other non-interest income in the consolidated statements of income.

AFFORDABLE HOUSING TAX CREDIT LIMITED PARTNERSHIP
LCNB has elected to account for its investment in an affordable housing tax credit limited partnership using the proportional amortization method described in FASB ASU 2014-01, "Investments - Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects (A Consensus of the FASB Emerging Issues Task Force)." Under the proportional amortization method, an investor amortizes the initial cost of the investment to income tax expense in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense. The investment in the limited partnership is included in other assets and the unfunded amount is included in accrued interest and other liabilities in LCNB's consolidated balance sheets.

FAIR VALUE MEASUREMENTS
Accounting guidance establishes a fair value hierarchy to prioritize the inputs to valuation techniques used to measure fair value. A financial instrument’s level within the hierarchy is based on the lowest level of input that is significant to the fair value measurement. The three broad input levels are:

- Level 1 – quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the reporting date;
- Level 2 – inputs other than quoted prices included within level 1 that are observable for the asset or liability either directly or indirectly; and
- Level 3 - inputs that are unobservable for the asset or liability.

Accounting guidance permits, but does not require, companies to measure many financial instruments and certain other items at fair value. The decision to elect the fair value option is made individually for each instrument and is irrevocable once made. Changes in fair value for the selected instruments are recorded in earnings. The Company did not select any financial instruments for the fair value election in 2015 or 2014.

ADVERTISING EXPENSE
Advertising costs are expensed as incurred and are recorded as a marketing expense, a component of non-interest expense.

PENSION PLANS
Eligible employees of the Company hired before 2009 participate in a multiple-employer qualified noncontributory defined benefit retirement plan. This plan is accounted for as a multi-employer plan because assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer.

Citizens National had a qualified noncontributory, defined benefit pension plan, which has been assumed by the Company, that covers eligible employees hired before May 1, 2005. This is a single employer plan.

TREASURY STOCK

Common stock shares repurchased are recorded at cost. Cost of shares retired or reissued is determined using the weighted average method.

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LCNB CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015
(Continued)
NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

STOCK OPTIONS AND RESTRICTED STOCK AWARD PLANS
The cost of employee services received in exchange for stock option grants is the grant-date fair value of the award estimated using an option-pricing model. The compensation cost for restricted stock awards is based on the market price of the Company's common stock at the date of grant multiplied by the number of shares granted that are expected to vest. The estimated cost is recognized over the period the employee is required to provide services in exchange for the award, usually the vesting period. The Company uses a Black-Scholes pricing model and related assumptions for estimating the fair value of stock option grants and a five-year vesting period for stock options and restricted stock.

INCOME TAXES
Deferred income taxes are determined using the liability method of accounting. Under this method, the net deferred tax asset or liability is determined based on the tax effects of temporary differences between the book and tax basis of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws.

Management analyzes material tax positions taken in any income tax return for any tax jurisdiction and determines the likelihood of the positions being sustained in a tax examination. 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.

EARNINGS PER SHARE
Basic earnings per share is calculated by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share is adjusted for the dilutive effects of stock options and warrants. The diluted average number of common shares outstanding has been increased for the assumed exercise of stock options and warrants with the proceeds used to purchase treasury shares at the average market price for the period.

RECENT ACCOUNTING PRONOUNCEMENTS
ASU No. 2014-08, "Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity"
ASU No. 2014-08 was issued in April 2014 and changes the criteria for reporting discontinued operations and provides for expanded disclosures in this area. The new guidance provides that only disposals representing a strategic shift in operations should be presented as discontinued operations and that these strategic shifts should have a major effect on an organization's operations and financial results. ASU No. 2014-08 was effective in the first quarter of 2015 for public companies with calendar year-ends.

ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)"
ASU No. 2014-09 was issued in May 2014 and and supersedes most current revenue recognition guidance for contracts to transfer goods or services or other nonfinancial assets. Lease contracts, insurance contracts, and most financial instruments are not included in the scope of this update. ASU No. 2014-09 provides that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance enumerates five steps that entities should follow in achieving this core principle. Additional disclosures providing

information about contracts with customers are required. As extended by ASU No. 2015-14, "Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date," ASU No. 2014-09 is effective for public companies for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Transitional guidance is included in the update. Earlier adoption is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. Since LCNB's products are substantially financial in nature, adoption of ASU No. 2014-09 is not expected to have a material impact on LCNB's results of operations or financial position.

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LCNB CORP. AND SUBSIDIARY
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December 31, 2015
(Continued)
NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

ASU No. 2014-12, "Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period, a consensus of the FASB Emerging Issues Task Force"
ASU No. 2014-12 was issued in June 2014 and requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition and that current guidance for awards with performance conditions be followed. ASU No. 2014-12 is effective for all entities for annual and interim periods beginning after December 15, 2015 and early adoption is permitted. Entities may apply the amendments in the update either prospectively to all awards granted or modified after the effective date or retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. None of LCNB's currently outstanding stock option grants contain the performance targets described in this update and adoption of ASU No. 2014-11 is not expected to have a material impact on its results of operations or financial position.

ASU No. 2014-13, "Consolidation (Topic 810): Measuring the Financial Assets and the Financial Liabilities of a Consolidated Collateralized Financing Entity (a consensus of the FASB Emerging Issues Task Force)"
ASU No. 2014-13 was issued in August 2014 and applies to entities that are required to (1) consolidate a collateralized financing entity ("CFE") under the guidance for Variable Interest Entities, (2) measure all of the financial assets and financial liabilities of the CFE at fair value, and (3) reflect the changes in fair value in earnings. Under ASU 2014-13, entities that meet these criteria can elect to measure both the financial assets and the financial liabilities of the CFE using the more observable of the fair value of the financial assets and the fair value of the financial liabilities, thereby eliminating the difference between the fair value of financial assets and financial liabilities. If that alternative is not elected, then ASU 2014-13 indicates that the fair value of the financial assets and the fair value of the financial liabilities of the consolidated CFE should be measured in accordance with ASC 820, Fair Value Measurement, and differences between the fair value of the financial assets and the financial liabilities of the consolidated CFE should be reflected in earnings and attributed to the reporting entity in the consolidated statement of income or loss. The provisions of ASU 2014-13 are effective for public business entities for annual periods beginning after December 15, 2015 and interim periods within those annual periods. Early adoption is permitted. LCNB currently does not have any CFE investments and adoption of ASU No. 2014-13 is not expected to have a material impact on LCNB's results of operations or financial position.

ASU No. 2014-15, "Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties About an Entity’s Ability to Continue as a Going Concern"
ASU No. 2014-15 was issued in August 2014 and requires management to evaluate for each annual and interim reporting period whether it is probable that the entity will not be able to meet its obligations as they become due within one year after the date that financial statements are issued (or are available to be issued, where applicable). Certain disclosures, as described in the update, are required if management identifies substantial doubt about the entity's ability to continue as a going concern. ASU No. 2014-15 will take effect in the annual periods ending after December 15, 2016, and interim periods within annual periods beginning after December 15, 2016. Early application is permitted. Adoption of ASU No. 2014-15 is not expected to have a material impact on LCNB's results of operations or financial position.

ASU No. 2014-16, "Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity (a consensus of the FASB

Emerging Issues Task Force)"
ASU No. 2014-16 was issued in November 2014 and requires an entity to determine the nature of the host contract by considering all stated and implied substantive terms and features of the hybrid financial instrument, weighing each term and feature on the basis of the relevant facts and circumstances, when evaluating whether the host contract is more akin to a debt or equity instrument. ASU No. 2014-16 is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. The effects of initially adopting ASU No. 2014-16 should be applied on a modified retrospective basis to existing hybrid financial instruments issued in the form of a share as of the beginning of the fiscal year for which the update is effective. Retrospective application to all relevant prior periods is permitted. Early adoption, including adoption in an interim period, is permitted. LCNB currently does not have any outstanding hybrid financial instruments issued as a share and adoption of ASU No. 2014-16 is not expected to have a material impact on LCNB's results of operations or financial position.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

ASU No. 2015-01, "Income Statement - Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items"
ASU No. 2015-01 was issued in January 2015 and eliminates from the income statement the concept of extraordinary items. The amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. Adoption of ASU No. 2015-01 is not expected to have a material impact on LCNB's results of operations.

ASU No. 2015-02, "Consolidation (Topic 810): Amendments to the Consolidation Analysis"
ASU No. 2015-02 was issued in February 2015 and provides additional guidance for consolidation of legal entities. It (1) modifies the evaluation of whether limited partnerships and similar legal entities are variable interest entities or voting interest entities, (2) eliminates the presumption that a general partner should consolidate a limited partnership, (3) affects the consolidation analysis of reporting entities that are involved with variable interest entities, and (4) provides a scope exception from consolidation guidance for reporting entities with interests in legal entities that are required to comply with or operate in accordance with requirements that are similar to those in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. The amendments in this update are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted, including adoption in an interim period. Adoption of ASU No. 2015-02 is not expected to have a material impact on LCNB's results of operations or financial position.

ASU No. 2015-03, "Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs"
ASU No. 2015-03 was issued in April 2015 and requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability. The amendments in this update are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted for financial statements that have not been previously issued. The adoption of ASU No. 2015-03 is to be applied on a retrospective basis, wherein the balance sheet of each individual period presented is adjusted to reflect the period-specific effects of applying the new guidance. Adoption of ASU No. 2015-03 is not expected to have a material impact on LCNB's results of operations or financial position.

ASU No. 2015-05, "Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement"
ASU No. 2015-05 was issued in April 2015 and provides guidance to customers about whether a cloud computing arrangement includes a software license. Examples of cloud computing arrangements include software as a service, platform as a service, infrastructure as a service, and other similar hosting arrangements. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The amendments in this update are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted. Adoption of ASU No. 2015-05 is not expected to have a material impact on LCNB's results of operations or financial position.

ASU No. 2015-07, "Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)"

ASU No. 2015-07 was issued in May 2015 and applies to entities that measure an investment's fair value using the net asset value per share, or an equivalent, as a practical expedient. ASU No. 2015-07 eliminates the requirement to classify such investments within the fair value hierarchy. Formerly, Topic 820 required certain disclosures for all investments eligible to be assessed at fair value with the net asset value per share practical expedient. ASU No. 2015-07 requires these disclosures only for investments that are actually measured using the practical expedient. The amendments in this update are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted. The amendments are to be applied retrospectively to all periods presented. LCNB measures the fair value of a mutual fund investment using the net asset value per share practical expedient and disclosures concerning this investment will be affected by the adoption of ASU No. 2015-07. Adoption will not have an impact on LCNB's results of operations or financial position.

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

ASU No. 2015-15, "Interest - Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements, Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting"
ASU No. 2015-15 was issued in August 2015. Given the absence of authoritative guidance within ASU No. 2015-03 for debt issuance costs related to line-of-credit arrangements, the Securities and Exchange Commission ("SEC") staff announced that they will not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. The amendments in this update are to be applied on a retrospective basis and are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted for financial statements that have not been previously issued. Adoption of ASU No. 2015-15 is not expected to have a material impact on LCNB's results of operations or financial position.

ASU No. 2015-16, "Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments"
ASU No. 2015-16 was issued in September 2015 and applies to all entities that have reported provisional amounts for items in a business combination for which the accounting is incomplete by the end of the reporting period in which the combination occurs and during the measurement period have an adjustment to provisional amounts recognized. ASU No. 2015-16 requires that an acquirer recognize adjustments to provision amounts during the measurement period in the reporting period in which the adjustment amounts are determined. The acquirer is also required to record in the same period's financial statements the effect on earnings of changes in depreciation, amortization, or other income effects, if any, resulting from the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. The update also requires an entity to present separately on the face of the income statement or disclose in the notes the portion of the amount recorded
in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. The amendments in this update are to be applied prospectively and are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Adoption of ASU No. 2015-16 is not expected to have a material impact on LCNB's results of operations or financial position.

ASU No. 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities"
ASU No. 2016-01 was issued in January 2016 and applies to all entities that hold financial assets or owe financial liabilities. It makes targeted changes to generally accepted accounting principles for public companies as follows:
1. Requires most equity investments to be measured at fair value with changes in fair value recognized in net income.
2. Simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. When a qualitative assessment indicates that impairment exists, an entity is required to measure the investment at fair value.
3. Eliminates the requirement to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet.
4. Requires use of the exit price notion when measuring the fair value of financial instruments for disclosure purposes.
5. Requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to

measure the liability at fair value in accordance with the fair value option for financial instruments.

6. Requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements.
7. Clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity’s other deferred tax assets.

For public business entities, the new guidance is effective for annual reporting periods, and interim reporting periods within those annual periods, beginning after December 15, 2017. Adoption of ASU No. 2016-01 is not expected to have a material impact on LCNB's results of operations or financial position.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

ASU No. 2016-02, "Leases (Topic 842)"
ASU No. 2016-02 was issued in February 2016 and requires a lessee to recognize in the statement of financial position a liability to make lease payments ("the lease liability") and a right-of-use asset representing its right to use the underlying asset for the lease term, initially measured at the present value of the lease payments. When measuring assets and liabilities arising from a lease, the lessee should include payments to be made in optional periods only if the lessee is reasonably certain, as defined, to exercise an option to the lease or not to exercise an option to terminate the lease. Optional payments to purchase the underlying asset should be included if the lessee is reasonably certain it will exercise the purchase option. Most variable lease payments should be excluded except for those that depend on an index or a rate or are in substance fixed payments.

A lessee shall classify a lease as a finance lease if it meets any of five listed criteria:
1. The lease transfers ownership of the underlying asset to the lessee by the end of the lease term.
2. The lease grants the lessee an option to purchase the underlying asset that the lessee is reasonably certain to exercise.
3. The lease term is for the major part of the remaining economic life of the underlying asset.
4. The present value of the sum of the lease payments and any residual value guaranteed by the lessee equals or exceeds substantially all of the fair value of the underlying asset.
5. The underlying asset is of such a specialized nature that it is expected to have no alternative use to the lessor at the end of the lease term.

For finance leases, a lessee shall recognize in the statement of comprehensive income interest on the lease liability separately from amortization of the right-of-use asset. Amortization of the right-of-use asset shall be on a straight-line basis, unless another basis is more representative of the pattern in which the lessee expects to consume the right-of-use asset’s future economic benefits. If the lease does not meet any of the five criteria, the lessee shall classify it as an operating lease and shall recognize a single lease cost on a straight-line basis over the lease term. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. If a lessee makes this election, it should recognize lease expense for such leases generally on a straight-line basis over the lease term.

The amendments in this update are to be applied using a modified retrospective approach, as defined, and are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2018. Early application is permitted. LCNB management is currently evaluating the financial statement impact of adopting the new guidance.

NOTE 2 – ACQUISITIONS

On December 29, 2014, LCNB and BNB Bancorp, Inc. (“BNB”) entered into an Agreement and Plan of Merger (“Merger Agreement”) pursuant to which BNB was acquired by LCNB on April 30, 2015. Immediately following the merger of BNB into LCNB, Brookville National Bank ("Brookville National"), a wholly-owned subsidiary of BNB, was merged into LCNB National Bank. Brookville National operated a main office and a branch office, both in Brookville, Ohio. These offices became branches of the Bank after the merger.

Under the terms of the Merger Agreement, the shareholders of BNB common stock received, for each share of BNB common stock, (i) $15.75 in cash and (ii) 2.005 LCNB common shares.

On October 28, 2013, LCNB and Colonial Banc Corp. (“Colonial”) entered into a Stock Purchase Agreement (“Purchase Agreement”) pursuant to which LCNB purchased from Colonial on January 24, 2014 all of the issued and outstanding shares of Eaton National Bank & Trust Co. ("Eaton National"). Immediately following the acquisition, Eaton National was merged into the Bank. Eaton National operated five full–service branches with a main office and another facility in Eaton, Ohio and branch offices in each of West Alexandria, Ohio, New Paris, Ohio, and Lewisburg, Ohio. These offices became branches of the Bank after the merger.

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NOTE 2 – ACQUISITIONS (Continued)

The mergers with BNB and Eaton National were accounted for using the acquisition method of accounting and, accordingly, assets acquired, liabilities assumed, and consideration paid were recorded at their estimated fair values as of the respective merger dates, as summarized in the following table (in thousands):

	BNB	Eaton National
Consideration Paid:		
Common shares issued	$9,063	—
Cash paid to shareholder(s)	4,403	24,750
Total consideration paid	13,466	24,750
Identifiable Assets Acquired:		
Cash and cash equivalents	13,396	15,635
Investment securities	58,239	35,859
Federal Reserve Bank stock	130	41
Federal Home Loan Bank stock	—	784
Loans	34,661	115,944
Premises and equipment	2,311	1,314
Bank owned life insurance	—	3,618
Core deposit intangible	1,418	2,466
Other real estate owned	—	262
Other assets	532	1,624
Total identifiable assets acquired	110,687	177,547
Liabilities Assumed:		
Deposits	99,133	165,335
Short-term borrowings	—	651
Deferred income taxes	576	—
Other liabilities	57	263
Total liabilities assumed	99,766	166,249
Total Identifiable Net Assets Acquired	10,921	11,298
Goodwill resulting from merger	2,545	13,452

The amount of goodwill recorded reflects LCNB's entrance into new markets and related synergies that are expected to result from the acquisitions and represent the excess purchase price over the estimated fair value of the net assets acquired. The goodwill will not be amortizable on LCNB's financial records, but is deductible for tax purposes. The core deposit intangible for BNB and Eaton National is being amortized over nine years and eight years, respectively, using the straight-line method.

Prior to the end of the one-year measurement period for finalizing the purchase allocation for BNB, if information becomes available which would indicate adjustments to the purchase price allocation, such adjustments will be included in the purchase price retrospectively.

Direct costs related to the acquisitions were expensed as incurred and are recorded as a merger-related expense in the consolidated statements of income.

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LCNB CORP. AND SUBSIDIARIES
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(Continued)

NOTE 2 – ACQUISITIONS (Continued)

The results of operations are included in the consolidated statement of income from the dates of the mergers. The estimated amount of BNB's revenue (net interest income plus non-interest income) and net income, excluding merger and data conversion costs, included in LCNB's consolidated statement of income for 2015 were as follows (in thousands):

Total revenue	$1,111
Net income	212

The following table presents unaudited pro forma information as if the merger with BNB had occurred on January 1, 2013 (in thousands). This pro forma information gives effect to certain adjustments, including purchase accounting fair value adjustments, amortization of the core deposit intangible, and related income tax effects. It does not include merger and data conversion costs. The comparable information for 2014 includes adjustments for Eaton National and the comparable information for 2013 includes adjustments for Eaton National and First Capital. The pro forma information does not necessarily reflect the results of operations that would have occurred had the merger with BNB occurred in 2013. In particular, expected operational cost savings are not reflected in the pro forma amounts.

	For Years Ended December 31,		
	2015	2014	2013
Total revenue	$50,213	47,595	50,089
Net income	11,883	10,508	11,505
Basic earnings per common share	1.20	1.07	1.16
Diluted earnings per common share	1.19	1.05	1.14

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(Continued)

NOTE 3 - INVESTMENT SECURITIES

The amortized cost and fair value of available-for-sale investment securities at December 31 are summarized as follows (in thousands):

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
2015				
Investment Securities Available-for-Sale:				
U.S. Treasury notes	$72,672	309	135	72,846
U.S. Agency notes	140,876	164	1,151	139,889
U.S. Agency mortgage-backed securities	29,608	174	404	29,378
Certificates of deposit	248	1	—	249
Municipal securities:				
Non-taxable	103,900	1,713	134	105,479
Taxable	26,738	337	134	26,941
Mutual funds	2,517	—	51	2,466
Trust preferred securities	49	1	—	50
Equity securities	659	40	19	680
	$377,267	2,739	2,028	377,978
Investment Securities Held-to-Maturity:				
Municipal securities:				
Non-taxable	$22,233	95	97	22,231
Taxable	400	—	1	399
	$22,633	95	98	22,630
2014				
Investment Securities Available-for-Sale:				
U.S. Treasury notes	$62,406	290	136	62,560
U.S. Agency notes	84,661	188	1,212	83,637
U.S. Agency mortgage-backed securities	37,838	413	219	38,032
Certificates of deposit	3,076	10	—	3,086
Municipal securities:				
Non-taxable	75,727	1,972	304	77,395
Taxable	16,005	465	75	16,395
Mutual funds	2,483	—	22	2,461
Trust preferred securities	50	—	—	50
Equity securities	1,415	372	38	1,749
	$283,661	3,710	2,006	285,365
Investment Securities Held-to-Maturity:				
Municipal securities:				
Non-taxable	$22,525	108	695	21,938
Taxable	200	—	—	200

	$22,725	108	695	22,138

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LCNB CORP. AND SUBSIDIARIES
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(Continued)

NOTE 3 - INVESTMENT SECURITIES (Continued)

Information concerning securities with gross unrealized losses at December 31, 2015 and 2014, aggregated by length of time that individual securities have been in a continuous loss position, is as follows (in thousands):

	Less Than Twelve Months		Twelve Months or More	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
2015				
Investment Securities Available-for-Sale:				
U.S. Treasury notes	$32,854	75	4,846	60
U.S. Agency notes	104,053	1,000	9,869	151
U.S. Agency mortgage-backed securities	19,190	256	4,068	148
Municipal securities:				
Non-taxable	13,124	74	7,037	60
Taxable	15,601	114	880	20
Mutual funds	1,215	17	268	34
Equity securities	248	12	73	7
	$186,285	1,548	27,041	480
Investment Securities Held-to-Maturity:				
Municipal securities:				
Non-taxable	$832	3	3,426	94
Taxable	399	1	—	—
	$1,231	4	3,426	94
2014				
Investment Securities Available-for-Sale:				
U.S. Treasury notes	$9,141	7	8,774	129
U.S. Agency notes	—	—	65,971	1,212
U.S. Agency mortgage-backed securities	3,795	2	11,456	217
Municipal securities:				
Non-taxable	7,211	58	11,419	246
Taxable	3,117	15	3,668	60
Mutual funds	281	12	1,190	10
Trust preferred securities	50	—	—	—
Equity securities	197	29	123	9
	$23,792	123	102,601	1,883
Investment Securities Held-to-Maturity:				
Municipal securities:				
Non-taxable	$8,152	540	4,200	155
	$8,152	540	4,200	155

Management has determined that the unrealized losses at December 31, 2015 are primarily due to fluctuations in market interest rates and do not reflect credit quality deterioration of the securities. Because the Company does not have the intent to sell the investments and it is more likely than not that the Company will not be required to sell the investments before recovery of their amortized cost, the Company does not consider these investments to be other-than-temporarily impaired.

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LCNB CORP. AND SUBSIDIARIES
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December 31, 2015
(Continued)

NOTE 3 - INVESTMENT SECURITIES (Continued)

Contractual maturities of investment securities at December 31, 2015 were as follows (in thousands). Actual maturities may differ from contractual maturities when issuers have the right to call or prepay obligations.

	Available-for-Sale		Held-to-Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due within one year	$23,011	23,159	3,819	3,831
Due from one to five years	182,774	183,597	3,904	3,882
Due from five to ten years	138,649	138,648	3,168	3,107
Due after ten years	—	—	11,742	11,810
	344,434	345,404	22,633	22,630
U.S. Agency mortgage-backed securities	29,608	29,378	—	—
Mutual funds	2,517	2,466	—	—
Trust preferred securities	49	50	—	—
Equity securities	659	680	—	—
	$377,267	377,978	22,633	22,630

Investment securities with a market value of $215,952,000 and $175,094,000 at December 31, 2015 and 2014, respectively, were pledged to secure public deposits and for other purposes required or permitted by law.

Certain information concerning the sale of investment securities available-for-sale for the years ended December 31 was as follows (in thousands):

	2015	2014	2013
Proceeds from sales	$97,981	67,296	59,284
Gross realized gains	627	252	1,234
Gross realized losses	132	103	174

NOTE 4 - LOANS

Major classifications of loans at December 31 were as follows (in thousands):

	2015	2014
Commercial and industrial	$45,275	35,424
Commercial, secured by real estate	419,633	379,141
Residential real estate	273,139	254,087
Consumer	18,510	18,006
Agricultural	13,479	11,472
Other loans, including deposit overdrafts	665	680
	770,701	698,810
Deferred origination costs (fees), net	237	146
	770,938	698,956
Less allowance for loan losses	3,129	3,121
Loans-net	$767,809	695,835

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LCNB CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015
(Continued)

NOTE 4 - LOANS (Continued)

Loans acquired from the mergers with First Capital, Eaton National, and BNB were recorded at fair value with no carryover of the acquired entity's previously established allowance for loan losses. The excess of expected cash flows over the estimated fair value of acquired loans is recognized as interest income over the remaining contractual lives of the loans using the level yield method. Subsequent decreases in expected cash flows will require additions to the allowance for loan losses. Subsequent improvements in expected cash flows result in the recognition of additional interest income over the then-remaining contractual lives of the loans. Management estimated the cash flows expected to be collected at acquisition using a third-party risk model, which incorporated the estimate of current key assumptions, such as default rates, severity, and prepayment speeds.

Impaired loans acquired are accounted for under FASB ASC 310-30. Factors considered in evaluating whether an acquired loan was impaired include delinquency status and history, updated borrower credit status, collateral information, and updated loan-to-value information. The difference between contractually required payments at the time of acquisition and the cash flows expected to be collected is referred to as the nonaccretable difference. The interest component of the cash flows expected to be collected is referred to as the accretable yield and is recognized as interest income over the remaining contractual life of the loan using the level yield method. Subsequent decreases in expected cash flows will require additions to the allowance for loan losses. Subsequent improvements in expected cash flows will result in a reclassification from the nonaccretable difference to the accretable yield.

The following table provides certain information at the acquisition date on loans acquired from BNB on April 30, 2015 and from Eaton National on January 24, 2014, not including loans considered to be impaired (in thousands):

	BNB	Eaton National
Contractually required principal at acquisition	$32,174	102,483
Less fair value adjustment	199	1,347
Fair value of acquired loans	$31,975	101,136
Contractual cash flows not expected to be collected	$195	1,702

The following table provides details on acquired impaired loans obtained through the mergers with BNB and Eaton National that are accounted for in accordance with FASB ASC 310-30 (in thousands):

	BNB	Eaton National
Contractually required principal at acquisition	$3,511	23,414
Contractual cash flows not expected to be collected (nonaccretable difference)	(404)	(6,088)
Expected cash flows at acquisition	3,107	17,326
Interest component of expected cash flows (accretable discount)	(413)	(2,163)
Fair value of acquired impaired loans	$2,694	15,163

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LCNB CORP. AND SUBSIDIARIES
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(Continued)

NOTE 4 - LOANS (Continued)

Non-accrual, past-due, and accruing restructured loans at December 31 were as follows (in thousands):

	2015		2014	
Non-accrual loans:				
Commercial and industrial	$—		—	
Commercial, secured by real estate	876		4,277	
Agricultural	48		70	
Residential real estate	799		1,252	
Total non-accrual loans	1,723		5,599	
Past-due 90 days or more and still accruing	559		203	
Total non-accrual and past-due 90 days or more and still accruing	2,282		5,802	
Accruing restructured loans	13,723		14,269	
Total	$16,005		20,071	
Percentage of total non-accrual and past-due 90 days or more and still accruing to total loans	0.30	%	0.83	%
Percentage of total non-accrual, past-due 90 days or more and still accruing, and accruing restructured loans to total loans	2.08	%	2.87	%

LCNB sold impaired loans with a carrying value of approximately $4.5 million during the second quarter 2015. The decrease in non-accrual loans at December 31, 2015 as compared to December 31, 2014 is primarily due to this sale.

Interest income that would have been recorded during 2015 and 2014 if loans on non-accrual status at December 31, 2015 and 2014 had been current and in accordance with their original terms was approximately $137,000 and $665,000, respectively.

The Company is not committed to lend additional funds to debtors whose loans have been modified to provide a reduction or deferral of principal or interest because of deterioration in the financial position of the borrower.

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LCNB CORP. AND SUBSIDIARIES
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December 31, 2015
(Continued)

NOTE 4 - LOANS (Continued)

The allowance for loan losses and recorded investment in loans for the years ended December 31 were as follows (in thousands):

	Commercial & Industrial	Commercial, Secured by Real Estate	Residential Real Estate	Consumer	Agricultural	Other	Total
December 31, 2015							
Allowance for loan losses:							
Balance, beginning of year	$ 129	1,990	926	63	11	2	3,121
Provision charged to expenses	208	955	125	(17)	55	40	1,366
Losses charged off	(100)	(1,133)	(304)	(52)	(67)	(74)	(1,730)
Recoveries	7	96	107	60	67	35	372
Balance, end of year	$ 244	1,908	854	54	66	3	3,129
Individually evaluated for impairment	$ 9	306	48	—	—	—	363
Collectively evaluated for impairment	235	1,602	806	54	66	3	2,766
Acquired credit impaired loans	—	—	—	—	—	—	—
Balance, end of year	$ 244	1,908	854	54	66	3	3,129
Loans:							
Individually evaluated for impairment	$ 370	12,351	1,541	56	—	—	14,318
Collectively evaluated for impairment	43,726	399,092	269,001	18,516	13,438	179	743,952
Acquired credit impaired loans	1,191	7,877	3,039	27	48	486	12,668
Balance, end of year	$ 45,287	419,320	273,581	18,599	13,486	665	770,938
December 31, 2014							
Allowance for loan losses:							
Balance, beginning of year	$ 175	2,520	826	66	—	1	3,588
Provision charged to expenses	173	(20)	712	18	11	36	930
Losses charged off	(261)	(573)	(652)	(129)	—	(79)	(1,694)
Recoveries	42	63	40	108	—	44	297
Balance, end of year	$ 129	1,990	926	63	11	2	3,121
Individually evaluated for impairment	$ 10	415	89	—	—	—	514
Collectively evaluated for impairment	119	1,273	836	63	11	2	2,304
Acquired credit impaired loans	—	302	1	—	—	—	303
Balance, end of year	$ 129	1,990	926	63	11	2	3,121

Loans:							
Individually evaluated for impairment	$ 401	13,022	1,701	55	—	—	15,179
Collectively evaluated for impairment	33,941	352,774	249,374	17,954	11,371	167	665,581
Acquired credit impaired loans	1,092	12,984	3,425	81	101	513	18,196
Balance, end of year	$ 35,434	378,780	254,500	18,090	11,472	680	698,956

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NOTE 4 - LOANS (Continued)

	Commercial & Industrial	Commercial, Secured by Real Estate	Residential Real Estate	Consumer	Agricultural	Other	Total
December 31, 2013							
Allowance for loan losses:							
Balance, beginning of year	$ 320	2,296	712	108	—	1	3,437
Provision charged to expenses	(30)	256	327	12	—	23	588
Losses charged off	(119)	(58)	(244)	(181)	—	(67)	(669)
Recoveries	4	26	31	127	—	44	232
Balance, end of year	$ 175	2,520	826	66	—	1	3,588
Individually evaluated for impairment	$ 2	760	270	—	—	—	1,032
Collectively evaluated for impairment	173	1,760	556	66	—	1	2,556
Balance, end of year	$ 175	2,520	826	66	—	1	3,588

The risk characteristics of LCNB's material loan portfolio segments were as follows:

Commercial and Industrial Loans. LCNB's commercial and industrial loan portfolio consists of loans for various purposes, including loans to fund working capital requirements (such as inventory and receivables financing) and purchases of machinery and equipment. LCNB offers a variety of commercial and industrial loan arrangements, including term loans, balloon loans, and lines of credit. Most commercial and industrial loans have a variable rate, with adjustment periods ranging from one month to five years. Adjustments are generally based on a publicly available index rate plus a margin. The margin varies based on the terms and collateral securing the loan. Commercial and industrial loans are offered to businesses and professionals for short and medium terms on both a collateralized and uncollateralized basis. Commercial and industrial loans typically are underwritten on the basis of the borrower's ability to make repayment from the cash flow of the business. Collateral, when obtained, may include liens on furniture, fixtures, equipment, inventory, receivables, or other assets. As a result, such loans involve complexities, variables, and risks that require thorough underwriting and more robust servicing than other types of loans.

Commercial, Secured by Real Estate Loans. Commercial real estate loans include loans secured by a variety of commercial, retail, and office buildings, religious facilities, multifamily (more than two-family) residential properties, construction and land development loans, and other land loans. Commercial real estate loan products generally amortize over five to twenty-five years and are payable in monthly principal and interest installments. Some have balloon payments due within one to ten years after the origination date. Many have adjustable interest rates with adjustment periods ranging from one to ten years, some of which are subject to established "floor" interest rates.

Commercial real estate loans are underwritten based on the ability of the property, in the case of income producing property, or the borrower's business to generate sufficient cash flow to amortize the debt. Secondary emphasis is placed upon global debt service, collateral value, financial strength of any guarantors, and other factors. Commercial real estate loans are generally originated with a 75% maximum loan to appraised value ratio.

Residential Real Estate Loans. Residential real estate loans include loans secured by first or second mortgage liens on one to two-family residential property. Home equity lines of credit and mortgage loans secured by owner-occupied agricultural property are included in this category. First and second mortgage loans are generally amortized over five to thirty years with monthly principal and interest payments. Home equity lines of credit generally have a five year draw period with interest only payments followed by a repayment period with monthly payments based on the amount outstanding. LCNB offers both fixed and adjustable rate mortgage loans. Adjustable rate loans are available with adjustment periods ranging between one to ten years and adjust according to an established index plus a margin, subject to certain floor and ceiling rates. Home equity lines of credit have a variable rate based on the Wall Street Journal prime rate plus a margin.

LCNB does not originate reverse mortgage loans or residential real estate loans generally considered to be “subprime.”

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NOTE 4 - LOANS (Continued)

Residential real estate loans are underwritten primarily based on the borrower's ability to repay, prior credit history, and the value of the collateral. LCNB requires private mortgage insurance for first mortgage loans that have a loan to appraised value ratio of greater than 80%.
Consumer Loans. LCNB's portfolio of consumer loans generally includes secured and unsecured loans to individuals for household, family and other personal expenditures. Secured loans include loans to fund the purchase of automobiles, recreational vehicles, boats, and similar acquisitions. Consumer loans made by LCNB generally have fixed rates and terms ranging up to 72 months, depending upon the nature of the collateral, size of the loan, and other relevant factors.

Consumer loans generally have higher interest rates, but pose additional risks of collectibility and loss when compared to certain other types of loans. Collateral, if present, is generally subject to damage, wear, and depreciation. The borrower's ability to repay is of primary importance in the underwriting of consumer loans.

Agricultural Loans. LCNB's portfolio of agricultural loans includes loans for financing agricultural production or for financing the purchase of equipment used in the production of agricultural products. LCNB's agricultural loans are generally secured by farm machinery, livestock, crops, vehicles, or other agri-related collateral.

The Company uses a risk-rating system to quantify loan quality. A loan is assigned to a risk category based on relevant information about the ability of the borrower to service the debt including, but not limited to, current financial information, historical payment experience, credit documentation, public information, and current economic trends. The categories used are:

- Pass – loans categorized in this category are higher quality loans that do not fit any of the other categories described below.
- Other Assets Especially Mentioned (OAEM) - loans in this category are currently protected but are potentially weak. These loans constitute a risk but not to the point of justifying a classification of substandard. The credit risk may be relatively minor yet constitute an undue risk in light of the circumstances surrounding a specific asset.
- Substandard – loans in this category are inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the possibility that the Company will sustain some loss if the deficiencies are not corrected.
- Doubtful – loans classified in this category have all the weaknesses inherent in loans classified 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.

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NOTE 4 - LOANS (Continued)

An analysis of the Company's loan portfolio by credit quality indicators at December 31 is as follows (in thousands):

	Pass	OAEM	Substandard	Doubtful	Total
December 31, 2015					
Commercial & industrial	$44,596	—	691	—	45,287
Commercial, secured by real estate	397,938	9,316	12,066	—	419,320
Residential real estate	267,567	1,935	4,079	—	273,581
Consumer	18,528	—	71	—	18,599
Agricultural	12,246	850	390	—	13,486
Other	665	—	—	—	665
Total	$741,540	12,101	17,297	—	770,938
December 31, 2014					
Commercial & industrial	$34,322	—	1,112	—	35,434
Commercial, secured by real estate	353,957	6,421	18,402	—	378,780
Residential real estate	246,335	920	7,245	—	254,500
Consumer	17,979	—	111	—	18,090
Agricultural	11,273	—	199	—	11,472
Other	680	—	—	—	680
Total	$664,546	7,341	27,069	—	698,956

The Company evaluates the loan risk grading system definitions and allowance for loan loss methodology on an ongoing basis. No significant changes were made to either during the past year.

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NOTE 4 - LOANS (Continued)

A loan portfolio aging analysis at December 31 is as follows (in thousands):

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans Receivable	Total Loans Greater Than 90 Days and Accruing
December 31, 2015							
Commercial & industrial	$—	—	—	—	45,287	45,287	—
Commercial, secured by real estate	73	81	876	1,030	418,290	419,320	—
Residential real estate	777	198	1,124	2,099	271,482	273,581	516
Consumer	62	7	43	112	18,487	18,599	43
Agricultural	—	—	—	—	13,486	13,486	—
Other	109	—	—	109	556	665	—
Total	$1,021	286	2,043	3,350	767,588	770,938	559
December 31, 2014							
Commercial & industrial	$4	—	—	4	35,430	35,434	—
Commercial, secured by real estate	1,000	83	3,179	4,262	374,518	378,780	9
Residential real estate	648	297	1,289	2,234	252,266	254,500	177
Consumer	59	28	17	104	17,986	18,090	17
Agricultural	73	70	—	143	11,329	11,472	—
Other	106	—	—	106	574	680	—
Total	$1,890	478	4,485	6,853	692,103	698,956	203

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NOTE 4 - LOANS (Continued)

Impaired loans for the years ended December 31 were as follows (in thousands):

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2015					
With no related allowance recorded:					
Commercial & industrial	$1,205	1,500	—	1,467	206
Commercial, secured by real estate	16,345	18,335	—	18,575	2,229
Residential real estate	3,734	5,055	—	4,092	453
Consumer	81	109	—	106	25
Agricultural	48	151	—	81	487
Other	486	701	—	510	82
Total	$21,899	25,851	—	24,831	3,482
With an allowance recorded:					
Commercial & industrial	$356	356	9	370	21
Commercial, secured by real estate	3,883	4,014	306	4,007	114
Residential real estate	846	958	48	864	37
Consumer	2	1	—	—	—
Agricultural	—	—	—	—	—
Other	—	—	—	—	—
Total	$5,087	5,329	363	5,241	172
Total:					
Commercial & industrial	$1,561	1,856	9	1,837	227
Commercial, secured by real estate	20,228	22,349	306	22,582	2,343
Residential real estate	4,580	6,013	48	4,956	490
Consumer	83	110	—	106	25
Agricultural	48	151	—	81	487
Other	486	701	—	510	82
Total	$26,986	31,180	363	30,072	3,654

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(Continued)

NOTE 4 - LOANS (Continued)

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2014					
With no related allowance recorded:					
Commercial & industrial	$1,092	2,077	—	1,823	161
Commercial, secured by real estate	21,822	26,715	—	23,360	1,373
Residential real estate	4,057	5,549	—	4,645	379
Consumer	117	178	—	179	14
Agricultural	101	619	—	121	20
Other	513	744	—	550	43
Total	$27,702	35,882	—	30,678	1,990
With an allowance recorded:					
Commercial & industrial	$401	406	10	319	19
Commercial, secured by real estate	4,184	4,538	717	4,108	117
Residential real estate	1,069	1,265	90	1,026	44
Consumer	19	20	—	18	2
Agricultural	—	—	—	—	—
Other	—	—	—	—	—
Total	$5,673	6,229	817	5,471	182
Total:					
Commercial & industrial	$1,493	2,483	10	2,142	180
Commercial, secured by real estate	26,006	31,253	717	27,468	1,490
Residential real estate	5,126	6,814	90	5,671	423
Consumer	136	198	—	197	16
Agricultural	101	619	—	121	20
Other	513	744	—	550	43
Total	$33,375	42,111	817	36,149	2,172

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(Continued)

NOTE 4 - LOANS (Continued)

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2013					
With no related allowance recorded:					
Commercial & industrial	$332	531	—	700	35
Commercial, secured by real estate	10,883	12,317	—	11,612	748
Residential real estate	2,096	2,967	—	2,345	182
Consumer	—	—	—	7	—
Agricultural	—	—	—	13	6
Total	$13,311	15,815	—	14,677	971
With an allowance recorded:					
Commercial & industrial	$165	270	2	186	2
Commercial, secured by real estate	7,725	7,725	760	7,368	252
Residential real estate	1,645	1,663	270	1,123	44
Consumer	27	27	—	17	2
Agricultural	—	—	—	—	—
Total	$9,562	9,685	1,032	8,694	300
Total:					
Commercial & industrial	$497	801	2	886	37
Commercial, secured by real estate	18,608	20,042	760	18,980	1,000
Residential real estate	3,741	4,630	270	3,468	226
Consumer	27	27	—	24	2
Agricultural	—	—	—	13	6
Total	$22,873	25,500	1,032	23,371	1,271

Of the interest income recognized on impaired loans during 2015, 2014, and 2013, approximately $96,000, $8,000, and $0, respectively, were recognized on a cash basis. The Company continued to accrue interest on certain loans classified as impaired during 2015, 2014, and 2013 because they were restructured or considered well secured and in the process of collection.

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NOTE 4 - LOANS (Continued)

Loan modifications that were classified as troubled debt restructurings during the years ended December 31 were as follows (dollars in thousands):

	2015			2014			2013		
	Number of Loans	Pre-Modification Recorded Balance	Post-Modification Recorded Balance	Number of Loans	Pre-Modification Recorded Balance	Post-Modification Recorded Balance	Number of Loans	Pre-Modification Recorded Balance	Post-Modification Recorded Balance
Commercial and industrial	—	$ —	$ —	8	$ 658	$ 340	1	$ 22	$ 22
Commercial, secured by real estate	1	75	74	2	896	1,214	3	1,594	1,594
Residential real estate	7	217	221	2	82	82	6	508	508
Consumer	2	9	9	3	40	40	2	27	27
	10	$ 301	$ 304	15	$ 1,676	$ 1,676	12	$ 2,151	$ 2,151

The pre-modification and post-modification recorded balances for the commercial and industrial and commercial, secured by real estate categories in 2014 changed because a borrower had multiple loans classified as commercial and industrial and a loan classified as commercial, secured by real estate, which were all modified into a loan classified as commercial, secured by real estate.

Each restructured loan is separately negotiated with the borrower and includes terms and conditions that reflect the borrower’s ability to pay the debt as modified. Modifications may include interest only payments for a period of time, temporary or permanent reduction of the loan’s interest rate, capitalization of delinquent interest, or extensions of the maturity date.

LCNB is not committed to lend additional funds to borrowers whose loan terms were modified in a troubled debt restructuring.

There were no troubled debt restructurings that subsequently defaulted within twelve months of the restructuring date for the years ended December 31, 2015 and 2014. A restructured automobile loan with a balance of $13,000 was charged off during the first quarter 2013, which was within twelve months of the loan's modification date.

All troubled debt restructurings are considered impaired loans. The allowance for loan loss on such restructured loans is based on the present value of future expected cash flows.

Approximately $147,000 of impaired loans without a valuation allowance and $125,000 of impaired loans with a valuation allowance at December 31, 2015 consisted of loans that were modified during 2015 and were determined to be troubled debt restructurings. Approximately $1,329,000 of impaired loans without a valuation allowance and $299,000 of impaired loans with a valuation allowance at December 31, 2014 consisted of loans that were modified during 2014 and were determined to be troubled debt restructurings.

Mortgage loans sold to and serviced for the Federal Home Loan Mortgage Corporation and other investors are not included in the accompanying consolidated balance sheets. The unpaid principal balances of those loans at December 31, 2015, 2014 and 2013 were approximately $111,837,000, $120,433,000, and $90,343,000 respectively.

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NOTE 4 - LOANS (Continued)

Mortgage servicing right assets are included in core deposit and other intangibles in the consolidated balance sheets. Amortization of mortgage servicing rights is an adjustment to loan servicing income, which is included with other operating income in the consolidated statements of income. Activity in the mortgage servicing rights portfolio during the years ended December 31 was as follows (in thousands):

	2015	2014	2013
Balance, beginning of year	$591	498	475
Amount capitalized to mortgage servicing rights	78	292	191
Amortization of mortgage servicing rights	(181)	(199)	(168)
Balance, end of year	$488	591	498

NOTE 5 - ACQUIRED CREDIT IMPAIRED LOANS

The following table provides, as of December 31, the major classifications of loans acquired that are accounted for in accordance with FASB ASC 310-30 (in thousands):

	2015	2014
Commercial & industrial	$1,191	1,092
Commercial, secured by real estate	7,877	12,984
Residential real estate	3,039	3,425
Consumer	27	81
Agricultural	48	101
Other loans, including deposit overdrafts	486	513
	12,668	18,196
Less allowance for loan losses	—	303
Loans, net	$12,668	17,893

The following table provides the outstanding balance and related carrying amount for acquired impaired loans at December 31 (in thousands):

	2015	2014
Outstanding balance	$16,507	26,697
Carrying amount	12,668	18,196

Activity during 2015 and 2014 for the accretable discount related to acquired impaired loans is as follows (in thousands):

	2015	2014
Accretable discount, beginning of year	$2,674	1,107
Accretable discount acquired during period	413	2,163
Reclass from nonaccretable discount to accretable discount	983	177
Less disposals	(850)	(249)
Less accretion	(1,717)	(524)
Accretable discount, end of year	$1,503	$2,674

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NOTE 6 – OTHER REAL ESTATE OWNED

Other real estate owned includes property acquired through foreclosure or deed-in-lieu of foreclosure and also includes property deemed to be in-substance foreclosed and are included in other assets in the consolidated balance sheets. Changes in other real estate owned were as follows (in thousands):

	2015	2014
Balance, beginning of year	$1,370	1,463
Additions	99	480
Additions due to merger	—	262
Reductions due to sales	(205)	(735)
Reductions due to valuation write downs	(418)	(100)
Balance, end of year	$846	1,370

Other real estate owned at December 31 consisted of (in thousands):

	2015	2014
Commercial real estate	$846	1,265
Residential real estate	—	105
	$846	1,370

The total recorded investment in residential consumer mortgage loans secured by residential real estate that was in the process of foreclosure at December 31, 2015 was $260,000.

NOTE 7 - PREMISES AND EQUIPMENT

Premises and equipment at December 31 are summarized as follows (in thousands):

	2015	2014
Land	$6,660	6,045
Buildings	21,463	19,728
Equipment	13,005	12,627
Construction in progress	9	49
Total	41,137	38,449
Less accumulated depreciation	19,037	17,716
Premises and equipment, net	$22,100	20,733

Depreciation charged to expense was, $1,427,000 in 2015, and $1,479,000 in 2014, and $1,456,000 in 2013.

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NOTE 8 - LEASES

Some of the Bank's branches, telephone equipment, and other equipment are leased under agreements expiring at various dates through 2050. These leases are accounted for as operating leases. The leases generally provide for renewal options and most require periodic changes in rental amounts based on various indices. Minimum annual rentals for each of the years 2016 through 2020 and thereafter for non-cancelable leases having terms in excess of one year were as follows (in thousands):

2016	$479
2017	370
2018	264
2019	221
2020	38
Thereafter	3,834
Total	$5,206

Rental expense for all leased branches and equipment was approximately $542,000 in 2015, $537,000 in 2014, and $484,000 in 2013.

NOTE 9 - GOODWILL AND OTHER INTANGIBLE ASSETS

Changes in goodwill during 2015 and 2014 were as follows (in thousands):

	2015	2014
Balance, beginning of year	$27,638	14,186
Additions from acquisitions	2,545	13,452
Balance, end of year	$30,183	27,638

Other intangible assets in the consolidated balance sheets at December 31, 2015 and 2014 were as follows (in thousands):

	2015			2014		
	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
Core deposit intangibles	$6,458	1,550	4,908	5,040	851	4,189
Mortgage servicing rights	1,496	1,008	488	1,418	827	591
Total	$7,954	2,558	5,396	6,458	1,678	4,780

The estimated aggregate future amortization expense for each of the next five years for intangible assets remaining as of December 31, 2015 is as follows (in thousands):

2016	$884
2017	857
2018	837
2019	821
2020	804

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NOTE 10 - AFFORDABLE HOUSING TAX CREDIT LIMITED PARTNERSHIP

LCNB is a limited partner in a limited partnership that sponsors affordable housing projects utilizing the Low Income Housing Tax Credit (LIHTC) pursuant to Section 42 of the Internal Revenue Code. The purpose of this investment is to achieve a satisfactory return on capital, to facilitate the sale of additional affordable housing product offerings, and to assist in achieving goals associated with the Community Reinvestment Act. The primary activities of the limited partnership include the identification, development, and operation of multi-family housing that is leased to qualifying residential tenants.

The following table presents the balances of LCNB's affordable housing tax credit investment and related unfunded commitment at December 31 (in thousands):

	2015	2014
Affordable housing tax credit investment	$1,000	—
Less amortization	12	—
Net affordable housing tax credit investment	$988	—
Unfunded commitment	$907	—

LCNB expects to fund the unfunded commitment over ten years.

The following table presents other information relating to LCNB's affordable housing tax credit investment for the years indicated (in thousands):

	Year ended December 31,		
	2015	2014	2013
Tax credits and other tax benefits recognized	$14	—	—
Tax credit amortization expense included in provision for income taxes	12	—	—

NOTE 11 - CERTIFICATES OF DEPOSIT

Contractual maturities of time deposits at December 31, 2015 were as follows (in thousands):

2016	$85,904
2017	31,822
2018	25,670
2019	21,575
2020	48,742
Thereafter	4,242
	$217,955

The aggregate amount of time deposits in denominations of $250,000 or more at December 31, 2015 and 2014 was $20,987,000 and $24,374,000, respectively.

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NOTE 12 - BORROWINGS

Funds borrowed from the FHLB at December 31 by year of maturity were as follows (dollars in thousands):

	Outstanding Balance	Average Rate	
December 31, 2015			
2016	$349	2.82	%
2017	5,295	5.11	%
2018	248	2.82	%
2019	55	2.82	%
2020	—	—	%
Thereafter	—	—	%
Total	$5,947	4.86	%
December 31, 2014			
2015	$5,410	2.06	%
2016	349	2.82	%
2017	5,295	5.11	%
2018	248	2.82	%
2019	55	2.82	%
Thereafter	—	—	%
Total	$11,357	3.53	%

All advances from the FHLB are secured by a blanket pledge of the Company's 1-4 family first lien mortgage loans in the amount of approximately $231 million and $212 million at December 31, 2015 and 2014, respectively. Additionally, the Company was required to hold minimum levels of FHLB stock, based on the outstanding borrowings. Total remaining borrowing capacity, including short-term borrowing arrangements, at December 31, 2015 was approximately $99.6 million. One of the factors limiting remaining borrowing capacity is ownership of FHLB stock. The Company could increase its remaining borrowing capacity by purchasing additional FHLB stock.

Short-term borrowings at December 31 were as follows (dollars in thousands):

	2015			2014		
	Amount	Rate		Amount	Rate	
Line of credit	$13,187	1.00	%	$5,021	0.75	%
FHLB short-term advance	10,000	0.35	%	—	—	%
Repurchase agreements	14,200	0.10	%	11,624	0.10	%
	$37,387	0.48	%	$16,645	0.30	%

At December 31, 2015, the Company had short-term borrowing arrangements with three financial institutions and the Federal Home Loan Bank of Cincinnati. The first arrangement provides that the Company can borrow up to $7 million in federal funds at the interest rate in effect at the time of the borrowing. The second arrangement provides that the Company can borrow up to $10 million in federal funds at the interest rate in effect at the time of the borrowing. The third arrangement is a short-term line of credit for a maximum amount of $20 million at an interest rate equal to the lending institution's federal funds rate plus a spread of 50 basis points.

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NOTE 12 - BORROWINGS (continued)

Under the terms of the Cash Management Advance program with the Federal Home Loan Bank of Cincinnati, the Company can borrow up to $55.3 million in short-term advances, subject to total remaining borrowing capacity limitations. The Company has the option of selecting a variable rate of interest for up to 90 days or a fixed rate of interest for up to 30 days. The interest rate on the Cash Management Advance program is the published rate in effect at the time of the advance. This agreement expires on August 26, 2016.

Repurchase agreements are an option customers may use in managing their cash positions. The repurchase agreements mature the next business day after issuance. They are secured by U.S. Agency notes and such collateral securities are held by the Federal Reserve Bank. The maximum amount of outstanding agreements at any month-end during 2015 and 2014 totaled $16,250,000 and $12,927,000, respectively. The average balance during 2015 and 2014 was $12,699,000 and $11,367,000, respectively.

As of December 31, 2015 and 2014, approximately $1.6 million and $1.2 million, respectively, of the repurchase agreements outstanding were held by a company owned by a member of the Company’s Board of Directors.

NOTE 13 - INCOME TAXES

The provision for federal income taxes consists of (in thousands):

	2015	2014	2013
Income taxes currently payable	$4,280	3,194	2,750
Deferred income tax provision (benefit)	(58)	192	192
Provision for income taxes	$4,222	3,386	2,942

A reconciliation between the statutory income tax and the Company's effective tax rate follows:

	2015	2014	2013
Statutory tax rate	34.0 %	34.0 %	34.0 %
Increase (decrease) resulting from -			
Tax exempt interest	(6.0)%	(6.8)%	(7.2)%
Tax exempt income on bank owned life insurance	(1.4)%	(1.7)%	(2.0)%
Other – net	0.3 %	— %	0.3 %
Effective tax rate	26.9 %	25.5 %	25.1 %

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NOTE 13 - INCOME TAXES (continued)

Deferred tax assets and liabilities at December 31 consist of the following (in thousands):

	2015	2014
Deferred tax assets:		
Allowance for loan losses	$1,064	1,061
Net unrealized losses on investment securities available-for-sale	246	470
Fair value adjustment on loans acquired from merger with First Capital	847	1,184
Write-down of other real estate owned	338	196
Pension and deferred compensation	971	849
Other	440	274
	3,906	4,034
Deferred tax liabilities:		
Depreciation of premises and equipment	(1,332)	(1,280)
Amortization of intangibles	(840)	(950)
Deferred loan fees	(2)	(3)
FHLB stock dividends	(349)	(349)
Fair value adjustment on securities acquired from merger with First Capital	(70)	(143)
	(2,593)	(2,725)
Net deferred tax assets (liabilities)	$1,313	1,309

As of December 31, 2015 and 2014 there were no unrecognized tax benefits and the Company does not anticipate the total amount of unrecognized tax benefits will significantly change within the next twelve months. There were no amounts recognized for interest and penalties in the consolidated statements of income for the three-year period ended December 31, 2015.

The Company is no longer subject to examination by federal tax authorities for years before 2012.

NOTE 14 - COMMITMENTS AND CONTINGENT LIABILITIES

LCNB is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. They involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheets. The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contract amount of those instruments.

The Bounce Protection product, a customer deposit overdraft program, is offered as a service and does not constitute a contract between the customer and LCNB.

LCNB uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

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NOTE 14 - COMMITMENTS AND CONTINGENT LIABILITIES (continued)

Financial instruments whose contract amounts represent off-balance-sheet credit risk at December 31 were as follows (in thousands):

	2015	2014
Commitments to extend credit:		
Commercial loans	$8,160	5,152
Other loans:		
Fixed rate	2,293	877
Adjustable rate	1,362	2,011
Unused lines of credit:		
Fixed rate	6,378	6,496
Adjustable rate	90,153	67,981
Unused overdraft protection amounts on demand and NOW accounts	10,057	10,206
Standby letters of credit	457	563
	$118,860	93,286

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract or agreement. Unused lines of credit include amounts not drawn on line of credit loans. Commitments to extend credit and unused lines of credit generally have fixed expiration dates or other termination clauses.

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. These guarantees generally are fully secured and have varying maturities.

The Company evaluates each customer’s credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company, is based on management’s credit evaluation of the borrower. Collateral held varies, but may include accounts receivable; inventory; property, plant and equipment; residential realty; and income-producing commercial properties.

Capital expenditures include the construction or acquisition of new office buildings, improvements to LCNB's offices, purchases of furniture and equipment, and additions or improvements to LCNB's information technology system. Commitments outstanding for capital expenditures as of December 31, 2015 totaled approximately $11,026,000, which includes estimated costs for a new operations center to be built in Lebanon, Ohio.

The Company and its subsidiaries are parties to various claims and proceedings arising in the normal course of business. Management, after consultation with legal counsel, believes that the liabilities, if any, arising from such proceedings and claims will not be material to the consolidated financial position or results of operations.

NOTE 15 - REGULATORY MATTERS

The Federal Reserve Act requires depository institutions to maintain cash reserves with the Federal Reserve Bank. In 2015 and 2014, the Bank maintained average reserve balances of $11,329,000 and $11,766,000, respectively. The reserve balances at December 31, 2015 and 2014 were $633,000 and $18,638,000, respectively.

The principal source of income and funds for LCNB Corp. is dividends paid by the Bank. The payment of dividends is subject to restriction by regulatory authorities. For 2015, the restrictions generally limit dividends to the aggregate of net income for the year 2015 plus the net earnings retained for 2014 and 2013. In addition, dividend payments may not reduce capital levels below minimum regulatory guidelines. At December 31, 2015, approximately $8,333,000 of the Bank's earnings retained was available for dividends in 2016 under this guideline. Dividends in excess of these limitations would require the prior approval of the Comptroller of the Currency.

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NOTE 15 - REGULATORY MATTERS (continued)

The Company (consolidated) and the Bank must meet certain minimum capital requirements set by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a material effect on the Company's and Bank's financial statements. The Company’s and Bank’s capital amounts and classification are also subject to qualitative judgments by regulators about components, risk weightings, and other factors.

For various regulatory purposes, financial institutions are classified into categories based upon capital adequacy:

	Minimum Requirement		To Be Considered Well-Capitalized	
Ratio of Common Equity Tier 1 Capital to risk-weighted assets	4.5	%	6.5	%
Ratio of tier 1 capital to risk-weighted assets	6.0	%	8.0	%
Ratio of total capital (tier 1 capital plus tier 2 capital) to risk-weighted assets	8.0	%	10.0	%
Leverage ratio (tier 1 capital to adjusted quarterly average total assets)	4.0	%	5.0	%

A new rule requiring a Capital Conservation Buffer will begin phase-in on January 1, 2016. Under the fully-implemented rule, a financial institution will need to maintain a Capital Conservation Buffer composed of Common Equity Tier 1 Capital of at least 2.5% above its minimum risk-weighted capital requirements to avoid limitations on its ability to make capital distributions, including dividend payments to shareholders and certain discretionary bonus payments to executive officers. A financial institution with a buffer below 2.5% will be subject to increasingly stringent limitations on capital distributions as the buffer approaches zero.

As of the most recent notification from their regulators, the Company and Bank were categorized as "well-capitalized" under the regulatory framework for prompt corrective action. Management believes that no conditions or events have occurred since the last notification that would change the Bank's category.

A summary of the regulatory capital of the Consolidated Company and Bank at December 31 follows (dollars in thousands):

	2015 Consolidated Company		Bank		2014 Consolidated Company		Bank	
Regulatory Capital:								
Shareholders' equity	$140,108		138,396		125,695		119,350	
Goodwill and other intangible assets	(32,146	)	(32,146	)	(31,886	)	(31,886	)
Accumulated other comprehensive (income) loss	(256	)	(261	)	(785	)	(583	)
Tier 1 risk-based capital	107,706		105,989		93,024		86,881	
Eligible allowance for loan losses	3,129		3,129		3,121		3,121	
Total risk-based capital	$110,835		109,118		96,145		90,002	
Capital Ratios:								
Common Equity Tier 1 Capital to risk-weighted assets	13.46	%	13.26	%	N/A		N/A	
Tier 1 capital to risk-weighted assets	13.46	%	13.26	%	13.92	%	13.03	%

Total capital (tier 1 capital plus tier 2 capital) to risk-weighted assets	13.85 %	13.65 %	14.38 %	13.50 %
Leverage ratio (tier 1 capital to adjusted quarterly average total assets)	8.62 %	8.49 %	8.53 %	7.98 %

NOTE 15 - REGULATORY MATTERS (continued)

LCNB Corp. filed a Registration Statement on Form S-3 with the SEC on July 27, 2011 to register 400,000 shares for use in its Amended and Restated Dividend Reinvestment and Stock Purchase Plan (the "Amended Plan"). Formerly LCNB purchased the shares needed for its Dividend and Stock Purchase Plan in the secondary market. Under the Amended Plan, LCNB has the option of purchasing shares in the secondary market, using treasury shares, or issuing new shares.

Two warrants for the purchase of an aggregate total of 217,063 common shares of LCNB stock at an exercise price of $9.26 per share were outstanding at December 31, 2015. The warrants carry a ten year term and were 100% vested at the date of grant, which was January 9, 2009. During February 2016, LCNB agreed to repurchase both warrants for $1,545,000, which will be accounted for as a reduction to common shares in the shareholders' equity section of the consolidated balance sheets.

NOTE 16 - ACCUMULATED OTHER COMPREHENSIVE INCOME

Changes in accumulated other comprehensive income (loss) for 2015 and 2014 were as follows (in thousands):

	2015			2014		
	Unrealized Gains and Losses on Available-for-Sale Securities	Changes in Pension Plan Assets and Benefit Obligations	Total	Unrealized Gains and Losses on Available-for-Sale Securities	Changes in Pension Plan Assets and Benefit Obligations	Total
Balance at beginning of year	$1,126	(341)	785	(1,641)	(81)	(1,722)
Before reclassifications	(330)	108	(222)	2,865	(260)	2,605
Reclassifications	(327)	—	(327)	(98)	—	(98)
Balance at end of year	$469	(233)	236	1,126	(341)	785

Reclassifications out of accumulated other comprehensive income (loss) during 2015 and 2014 and the affected line items in the consolidated statements of income were as follows (in thousands):

	2015	2014	Affected Line Item in the Consolidated Statements of Income
Realized gain on sales of securities	$495	149	Net gain on sale of securities
Less provision for income taxes	168	51	Provision for income taxes
Reclassification adjustment, net of taxes	$327	98	

NOTE 17 - RETIREMENT PLANS

Prior to January 1, 2009, the Company had a single-employer qualified noncontributory defined benefit retirement plan that covered substantially all regular full-time employees. Effective January 1, 2009, the Company redesigned the plan and merged it into a multiple-employer plan, which is accounted for as a multi-employer plan because assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer. Employees hired on or after January 1, 2009 are not eligible to participate in this plan.

Effective February 1, 2009, the Company amended the plan to reduce benefits for those whose age plus vesting service equaled less than 65 at that date. Also effective February 1, 2009, an enhanced 401(k) plan was made available to those hired on or after January 1, 2009 and to those who received benefit reductions from the amendments to the noncontributory defined benefit retirement plan. Employees hired on or after January 1, 2009 receive a 50% employer match on their contributions into the 401(k) plan, up to a maximum company contribution of 3% of each individual employee’s annual compensation. Employees who received a benefit reduction under the retirement plan amendments receive an automatic contribution of 5% or 7% of annual compensation, depending on the sum of an employee’s age and vesting service, into the 401(k) plan, regardless of the

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NOTE 17 - RETIREMENT PLANS (continued)

contributions made by the employees. This contribution is made annually and these employees will not receive any employer matches to their 401(k) contributions.

Certain information pertaining to the qualified noncontributory defined benefit retirement plan is as follows:

Legal name	Pentegra Defined Benefit Plan for Financial Institutions
Plan's employer identification number	13-5645888
Plan number	333

The plan is at least 80% funded as of July 1, 2015 and 2014. A funding improvement or rehabilitation plan has not been implemented, nor has a surcharge been paid to the plan.

Funding and administrative costs of the qualified noncontributory defined benefit retirement plan and 401(k) plan charged to salaries and employee benefits in the consolidated statements of income for the years ended December 31 were as follows (in thousands):

	2015	2014	2013
Qualified noncontributory defined benefit retirement plan	$984	967	486
401(k) plan	346	326	294

The Company expects a minimum contribution of $200,000 to the qualified noncontributory defined benefit retirement plan in 2016. The Company expects to contribute $250,000 to the 401(k) plan in 2016. The Company's contributions to the qualified noncontributory defined benefit retirement plan do not represent more than 5% of total contributions to the plan.

Citizens National had a qualified noncontributory defined benefit pension plan which covered employees hired before May 1, 2005. The Company assumed this plan at the time of the merger. At December 31, 2015, the amount of the asset for this plan was $40,000, representing the funded status of the plan.

The Bank has a benefit plan which permits eligible officers to defer a portion of their compensation. The deferred compensation balance, which accrues interest at 8% annually, is distributable in cash after retirement or termination of employment. The amount of such deferred compensation liability at December 31, 2015 and 2014 was $3,199,000 and $3,012,000, respectively.

The Bank also has supplemental income plans which provide certain employees an amount based on a percentage of average compensation, payable in accordance with individually defined schedules upon retirement. The projected benefit obligation included in other liabilities for the supplemental income plans at December 31, 2015 and 2014 is $1,295,000 and $1,106,000, respectively. The average discount rate used to determine the present value of the obligations was approximately 5.0% in 2015 and 5.3% in 2014. The service cost associated with the plans was $183,000 for 2015, $43,000 for 2014, and $111,000 for 2013. Interest costs were $56,000, $56,000, and $47,000 for 2015, 2014, and 2013, respectively.

The deferred compensation plan and supplemental income plans are nonqualified and unfunded. Participation in each plan is limited to a select group of management.

Effective February 1, 2009, the Company established a nonqualified defined benefit retirement plan, which is also unfunded, for certain highly compensated employees. The nonqualified plan ensures that participants receive the full amount of benefits to which they would have been entitled under the noncontributory defined benefit retirement plan in the absence of limits on benefit levels imposed by certain sections of the Internal Revenue Code.

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NOTE 17 - RETIREMENT PLANS (continued)

The components of net periodic pension cost of the nonqualified defined benefit retirement plan for the years ended December 31 are summarized as follows (in thousands):

	2015	2014	2013
Service cost	$38	68	71
Interest cost	68	60	46
Amortization of unrecognized (gain) loss	171	—	25
Amortization of unrecognized prior service cost	—	15	29
Net periodic pension cost	$277	143	171

A reconciliation of changes in the projected benefit obligation of the nonqualified defined benefit retirement plan at December 31 follows (in thousands):

	2015	2014	2013
Projected benefit obligation at beginning of year	$1,741	1,213	1,153
Service cost	38	68	71
Interest cost	68	60	46
Actuarial (gain) or loss	10	407	(57)
Benefits paid	(14)	(7)	—
Settlements	—	—	—
Curtailment	—	—	—
Projected benefit obligation at end of year	$1,843	1,741	1,213

Amounts recognized in other liabilities in the consolidated balance sheets for the nonqualified defined benefit retirement plan at December 31, 2015 and 2014 were $1,843,000 and $1,741,000, respectively.

The accumulated benefit obligation for the nonqualified defined benefit retirement plan at December 31, 2015 and 2014 was $1,752,000 and $1,633,000, respectively.

Amounts recognized in accumulated other comprehensive income, net of tax, at December 31 for the nonqualified defined benefit retirement plan consists of (in thousands):

	2015	2014	2013
Net actuarial (gain)/loss	$233	339	70
Past service cost	—	—	10
	$233	339	80

The estimated unrecognized net actuarial loss that will be amortized from accumulated other comprehensive income into net periodic benefit cost during 2016 for the nonqualified defined benefit retirement plan is $168,000.

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NOTE 17 - RETIREMENT PLANS (continued)

Key weighted-average assumptions used to determine the benefit obligation and net periodic pension costs for the nonqualified defined benefit retirement plan for the years ended December 31 were as follows:

	2015		2014		2013	
Benefit obligation:						
Discount rate	4.34	%	3.95	%	4.95	%
Salary increase rate	2.00	%	2.00	%	3.00	%
Net periodic pension cost:						
Discount rate	3.95	%	4.95	%	4.05	%
Salary increase rate	2.00	%	3.00	%	3.00	%
Amortization period in years	1.98		3.95		2.99	

The nonqualified defined benefit retirement plan is not funded. Therefore no contributions will be made in 2016. Estimated future benefit payments reflecting expected future service for the years ended after December 31, 2015 are (in thousands):

2016	$75
2017	138
2018	138
2019	137
2020	137
2021-2025	678

NOTE 18 - STOCK BASED COMPENSATION

LCNB established an Ownership Incentive Plan (the "2002 Plan") during 2002 that allowed for stock-based awards to eligible employees, as determined by the Board of Directors. The awards were in the form of stock options, share awards, and/or appreciation rights. The 2002 Plan provided for the issuance of up to 200,000 shares. The 2002 Plan expired on April 16, 2012. Any outstanding unexercized options, however, continue to be exercisable in accordance with their terms.

The 2015 Ownership Incentive Plan (the "2015 Plan") was ratified by LCNB's shareholders at the annual meeting on April 28, 2015 and allows for stock-based awards to eligible employees, as determined by the Compensation Committee of the Board of Directors. Awards may be made in the form of stock options, appreciation rights, restricted shares, and/or restricted share units. The 2015 Plan provides for the issuance of up to 450,000 shares. The 2015 Plan will terminate on April 28, 2025 and is subject to earlier termination by the Compensation Committee.

Stock-based awards may be in the form of treasury shares or new shares.

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NOTE 18 - STOCK BASED COMPENSATION (continued)

LCNB has not granted stock options since 2012. Option awards granted to date under the 2002 Plan vest ratably over a five year period and expire ten years after the date of grant. Stock options outstanding at December 31, 2015 were as follows:

	Outstanding Stock Options			Exercisable Stock Options		
Exercise Price Range	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)
$9.00 - 10.99	17,633	$9.00	3.1	17,633	$9.00	3.1
$11.00 - 12.99	53,266	12.04	4.6	44,477	12.00	4.4
$17.00 - 18.99	12,962	18.41	0.6	12,962	18.41	0.6
	83,861	12.39	3.7	75,072	12.40	3.4

The following table summarizes stock option activity for the years indicated:

	2015		2014		2013	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding at January 1,	99,810	12.16	104,966	$12.43	110,586	$12.42
Granted	—	—	—	—	—	—
Exercised	(13,449)	11.31	—	—	(5,620)	12.32
Expired	(2,500)	9.00	(5,156)	17.66	—	—
Outstanding at December 31,	83,861	12.39	99,810	12.16	104,966	12.43
Exercisable at December 31,	75,072	12.40	79,909	12.18	67,899	12.86

The following table provides information related to stock options exercised during the years indicated (in thousands):

	2015	2014	2013
Intrinsic value of options exercised	$67	—	41
Cash received from options exercised	152	—	70
Tax benefit realized from options exercised	13	—	12

The aggregate intrinsic value (the amount by which the current market value of the underlying stock exceeds the exercise price of the option) for options outstanding at December 31, 2015 that were “in the money” (market price greater than exercise price) was $360,000. The aggregate intrinsic value at that date for only the options that were exercisable was $324,000. The aggregate intrinsic value for options outstanding at December 31, 2014 that were in the money was $334,000 and the aggregate intrinsic value at that date for only the options that were exercisable was $274,000.The intrinsic value changes based on changes in the market value of the Company’s stock.

Total expense related to options included in salaries and wages in the consolidated statements of income for the years ended December 31, 2015, 2014, and 2013 was $19,000, $24,000, and $37,000, respectively. The related tax benefit for 2015, 2014, and 2013 was $6,000, $8,000, and $13,000, respectively. Total compensation cost related to option awards to be recognized through the first quarter of 2017 is approximately $6,000.

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NOTE 18 - STOCK BASED COMPENSATION (continued)

Restricted stock awards granted under the 2015 Plan were as follows:

	2015	
	Shares	Weighted Average Grant Date Fair Value
Outstanding at January 1,	—	$—
Granted	16,038	15.47
Vested	—	—
Forfeited	—	—
Outstanding at December 31,	16,038	$15.47

Total expense related to restricted stock awards included in salaries and wages in the consolidated statements of income for the year ended December 31, 2015 was $90,000 and the related tax benefit was $31,000. Unrecognized compensation expense for restricted stock awards was $158,000 at December 31, 2015 and is expected to be recognized over a period of five years.

NOTE 19 - EARNINGS PER SHARE

Basic earnings per common share is calculated by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per common share is adjusted for the dilutive effects of stock options, warrants, and restricted stock. The diluted average number of common shares outstanding has been increased for the assumed exercise of stock options and warrants with proceeds used to purchase treasury shares at the average market price for the period. Earnings per share for the years ended December 31 were calculated as follows (in thousands, except share and per share data):

	2015	2014	2013
Net income	$11,474	9,869	8,780
Weighted average number of shares outstanding used in the calculation of basic earnings per common share	9,704,965	9,297,019	7,852,514
Add dilutive effect of:			
Stock options	17,174	18,545	23,456
Stock warrants	89,328	90,782	107,027
Restricted shares	9	—	—
Adjusted weighted average number of shares outstanding used in the calculation of diluted earnings per common share	9,811,476	9,406,346	7,982,997
Earnings per common share:			
Basic	$1.18	1.06	1.12
Diluted	1.17	1.05	1.10

Options to purchase 12,962, 12,962, and 6,400 shares of common stock at weighted average prices of $18.41, $18.41, and $18.95 per share were outstanding at December 31, 2015, 2014, and 2013, respectively, and were not included in the computation of diluted earnings per common share because the exercise prices of the options were greater than the average market prices of the common shares.

NOTE 20 - RELATED PARTY TRANSACTIONS

The Company has entered into related party transactions with various directors and executive officers. Management believes these transactions do not involve more than a normal risk of collectibility or present other unfavorable features. The following table provides a summary of the loan activity for these officers and directors for the years ended December 31 (in thousands):

	2015	2014
Beginning balance	$1,192	1,001
Additions	106	594
Reductions	(207)	(403)
Ending Balance	$1,091	1,192

Deposits from executive officers, directors and related interests of such persons held by the Company at December 31, 2015 and 2014 amounted to $3,577,000 and $3,507,000, respectively.

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NOTE 21 - FAIR VALUE OF FINANCIAL INSTRUMENTS

The majority of LCNB's financial debt securities are classified as available-for-sale. The securities are reported at fair value with unrealized holding gains and losses reported net of income taxes in accumulated other comprehensive income.

LCNB utilizes a pricing service for determining the fair values of most of its investment securities. Fair value for U.S. Treasury notes are determined based on market quotations (level 1). Fair value for most of the other investment securities is calculated using the discounted cash flow method for each security. The discount rates for these cash flows are estimated by the pricing service using rates observed in the market (level 2). Cash flow streams are dependent on estimated prepayment speeds and the overall structure of the securities given existing market conditions. In addition, LCNB has invested in trust preferred securities, equity securities, and four mutual funds that are not priced by the pricing service. Market quotations (level 1) are used to determine fair values for the trust preferred securities and equity securities. Investments in mutual funds that are publicly traded in active markets and that publish daily net asset values are considered to have level 1 inputs. An investment in a mutual fund that is not traded in an active market is considered to have level 2 inputs because an investor can have its interest in the fund redeemed for the balance of its capital account at any quarter-end assuming the fund is given a 60 day notice. The investment in this fund is carried at fair value, which approximates cost.

Assets that may be recorded at fair value on a nonrecurring basis include impaired loans, other real estate owned, and other repossessed assets. A loan is considered impaired when management believes it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement. Impaired loans are carried at the present value of estimated future cash flows using the loan's existing rate or the fair value of collateral if the loan is collateral dependent, if this value is less than the loan balance. The inputs are considered to be level 3.

Other real estate owned is adjusted to fair value upon transfer of the loan to foreclosed assets, usually based on an appraisal of the property. Subsequently, foreclosed assets are carried at the lower of carrying value or fair value. These inputs are also considered to be level 3

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NOTE 21 - FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

The following table summarizes the valuation of LCNB's assets recorded at fair value by input levels as of December 31 (in thousands):

		Fair Value Measurements at the End of the Reporting Period Using		
	Fair Value Measurements	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2015				
Recurring fair value measurements:				
Investment securities available-for-sale:				
U.S. Treasury notes	$ 72,846	72,846	—	—
U.S. Agency notes	139,889	—	139,889	—
U.S. Agency mortgage-backed securities	29,378	—	29,378	—
Certificates of deposit	249	—	249	—
Municipal securities:				
Non-taxable	105,479	—	105,479	—
Taxable	26,941	—	26,941	—
Mutual funds	2,466	1,466	1,000	—
Trust preferred securities	50	50	—	—
Equity securities	680	680	—	—
Total recurring fair value measurements	$ 377,978	75,042	302,936	—
Nonrecurring fair value measurements:				
Impaired loans	$ 4,722	—	—	4,722
Other real estate owned and repossessed assets	846	—	—	846
Total nonrecurring fair value measurements	$ 5,568	—	—	5,568
December 31, 2014				
Recurring fair value measurement:				
Investment securities available-for-sale:				
U.S. Treasury notes	$ 62,560	62,560	—	—
U.S. Agency notes	83,637	—	83,637	—
U.S. Agency mortgage-backed securities	38,032	—	38,032	—
Certificates of deposit with other banks	3,086	—	3,086	—
Municipal securities:				
Non-taxable	77,395	—	77,395	—
Taxable	16,395	—	16,395	—
Mutual funds	2,461	1,461	1,000	—
Trust preferred securities	50	50	—	—

Equity securities	1,749	1,749	—	—
Total recurring fair value measurements	$ 285,365	65,820	219,545	—
Nonrecurring fair value measurements:				
Impaired loans	$ 4,872	—	—	4,872
Other real estate owned and repossessed assets	1,370	—	—	1,370
Total nonrecurring fair value measurements	$ 6,242	—	—	6,242

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LCNB CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015
(Continued)
NOTE 21 - FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

The following table presents quantitative information about unobservable inputs used in nonrecurring Level 3 fair value measurements at December 31, 2015 and 2014 (dollars in thousands):

	Fair Value	Valuation Technique	Unobservable Inputs	Range High	Range Low	Weighted Average
2015						
Impaired loans	$4,722	Estimated sales price	Adjustments for comparable properties, discounts to reflect current market conditions	Not applicable		
		Discounted cash flows	Discount rate	11.00 %	4.00 %	5.27 %
Other real estate owned	846	Estimated sales price	Adjustments for comparable properties, discounts to reflect current market conditions	Not applicable		
2014						
Impaired loans	$4,872	Estimated sales price	Adjustments for comparable properties, discounts to reflect current market conditions	Not applicable		
		Discounted cash flows	Discount rate	10.50%	4.00%	5.36%
Other real estate owned	1,370	Estimated sales price	Adjustments for comparable properties, discounts to reflect current market conditions			

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LCNB CORP. AND SUBSIDIARIES
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December 31, 2015
(Continued)
NOTE 21 - FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

Carrying amounts and estimated fair values of financial instruments as of December 31 were as follows (in thousands):

			Fair Value Measurements at the End of the Reporting Period Using		
	Carrying Amount	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
2015					
FINANCIAL ASSETS:					
Cash and cash equivalents	$14,987	14,987	14,987	—	—
Investment securities, held-to-maturity	22,633	22,630	—	—	22,630
Federal Reserve Bank stock	2,732	2,732	2,732	—	—
Federal Home Loan Bank stock	3,638	3,638	3,638	—	—
Loans, net	767,809	761,388	—	—	761,388
Accrued interest receivable	3,380	3,380	208	1,280	1,892
FINANCIAL LIABILITIES:					
Deposits	1,087,160	1,087,914	869,940	217,974	—
Short-term borrowings	37,387	37,387	37,387	—	—
Long-term debt	5,947	6,290	—	6,290	—
Accrued interest payable	345	345	16	329	—
2014					
FINANCIAL ASSETS:					
Cash and cash equivalents	$15,845	15,845	15,845	—	—
Investment securities, held-to-maturity	22,725	22,138	—	—	22,138
Federal Reserve Bank stock	2,346	2,346	2,346	—	—
Federal Home Loan Bank stock	3,638	3,638	3,638	—	—
Loans, net	695,835	699,715	—	—	699,715
Accrued interest receivable	2,849	2,849	178	885	1,786
FINANCIAL LIABILITIES:					
Deposits	946,205	947,541	731,766	215,775	—
Short-term borrowings	16,645	16,645	16,645	—	—
Long-term debt	11,357	11,944	—	11,944	—
Accrued interest payable	413	413	13	400	—

The fair value of off-balance-sheet financial instruments at December 31, 2015 and 2014 was not material.

Fair values of financial instruments are based on various assumptions, including the discount rate and estimates of future cash flows. Therefore, the fair values presented may not represent amounts that could be realized in actual transactions. In addition, because the required disclosures exclude certain financial instruments and all nonfinancial instruments, any aggregation of the fair value amounts presented would not represent the underlying value of the Company. The following methods and assumptions were used to estimate the fair value of certain financial instruments:

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NOTE 21 - FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

Cash and cash equivalents
The carrying amounts presented are deemed to approximate fair value.

Investment securities, held-to-maturity
Fair values for securities, held-to-maturity is estimated using discounted cash flow analysis, using interest rates offered on investments with similar maturities and investment quality.

Federal Home Loan Bank and Federal Reserve Bank stock
The carrying value of Federal Home Loan Bank and Federal Reserve Bank stock approximates fair value based on the respective redemptive provisions.

Loans
Fair value is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities, incorporating assumptions of current and projected prepayment speeds. These current rates approximate market rates.

Deposits
The fair value of demand deposits, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities, which approximates market rates.

Borrowings
The carrying amounts of federal funds purchased, repurchase agreements, and U.S. Treasury demand note borrowings are deemed to approximate fair value of short-term borrowings. For long-term debt, fair values are estimated based on the discounted value of expected net cash flows using current interest rates.

Accrued interest receivable and Accrued interest payable
Carrying amount approximates fair value and is aligned with the underlying assets or liabilities.

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LCNB CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015
(Continued)

NOTE 22 – QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

The following table sets forth certain quarterly results for the years ended December 31, 2015 and 2014 (dollars in thousands, except per share data):

	Three Months Ended			
	March 31	June 30	Sep. 30	Dec. 31
2015				
Interest income	$10,090	11,348	10,409	10,812
Interest expense	762	748	912	906
Net interest income	9,328	10,600	9,497	9,906
Provision for loan losses	69	677	240	380
Net interest income after provision	9,259	9,923	9,257	9,526
Total non-interest income	2,306	2,831	2,386	2,600
Total non-interest expenses	7,649	8,426	8,088	8,229
Income before income taxes	3,916	4,328	3,555	3,897
Provision for income taxes	1,082	1,205	922	1,013
Net income	$2,834	3,123	2,633	2,884
Earnings per common share:				
Basic	$0.30	0.33	0.26	0.29
Diluted	0.30	0.32	0.26	0.29
2014				
Interest income	$9,278	9,926	9,906	10,367
Interest expense	915	920	911	844
Net interest income	8,363	9,006	8,995	9,523
Provision for loan losses	81	255	401	193
Net interest income after provision	8,282	8,751	8,594	9,330
Total non-interest income	2,077	2,301	2,315	2,449
Total non-interest expenses	8,672	7,600	7,238	7,334
Income before income taxes	1,687	3,452	3,671	4,445
Provision for income taxes	364	841	953	1,228
Net income	$1,323	2,611	2,718	3,217
Earnings per common share:				
Basic	$0.14	0.28	0.30	0.34
Diluted	0.14	0.28	0.29	0.34

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LCNB CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015
(Continued)

NOTE 23 - PARENT COMPANY FINANCIAL INFORMATION

Condensed financial information for LCNB Corp., parent company only, follows (in thousands):
Condensed Balance Sheets:

December 31,	2015	2014
Assets:		
Cash on deposit with subsidiary	$534	3,985
Investment securities available-for-sale, at fair value	888	1,970
Investment in subsidiary	138,396	119,350
Other assets	290	419
Total assets	$140,108	125,724
Liabilities	$—	29
Shareholders' equity	140,108	125,695
Total liabilities and shareholders' equity	$140,108	125,724

Condensed Statements of Income

Year ended December 31,	2015	2014	2013
Income:			
Dividends from subsidiaries	$5,400	8,800	10,525
Interest and dividends	58	91	89
Net gain on sales of securities	254	10	124
Total income	5,712	8,901	10,738
Total expenses	1,016	1,077	127
Income before income tax expense/benefit and equity in undistributed income of subsidiaries	4,696	7,824	10,611
Income tax (expense) benefit	250	350	(12)
Equity in undistributed income (loss) of subsidiaries	6,528	1,695	(1,819)
Net income	$11,474	9,869	8,780

LCNB CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015
(Continued)
NOTE 23 - PARENT COMPANY FINANCIAL INFORMATION (continued)

Condensed Statements of Cash Flows

Year ended December 31,	2015	2014	2013
Cash flows from operating activities:			
Net income	$11,474	9,869	8,780
Adjustments for non-cash items -			
(Increase) decrease in undistributed income of subsidiaries	(6,528)	(1,695)	1,819
Other, net	42	(474)	7
Net cash flows from operating activities	4,988	7,700	10,606
Cash flows from investing activities:			
Purchases of securities available-for-sale	(215)	(107)	(563)
Proceeds from sales of available-for-sale securities	1,217	227	569
Cash paid for business acquisition	(3,757)	(24,750)	(7,815)
Net cash flows from (used in) investing activities	(2,755)	(24,630)	(7,809)
Cash flows from financing activities:			
Principal payments on long-term debt	—	—	(1,792)
Proceeds from issuance of common stock	390	372	27,238
Cash dividends paid on common stock	(6,239)	(5,950)	(5,148)
Other	165	—	70
Net cash flows from (used in) financing activities	(5,684)	(5,578)	20,368
Net change in cash	(3,451)	(22,508)	23,165
Cash at beginning of year	3,985	26,493	3,328
Cash at end of year	$534	3,985	26,493

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LCNB CORP. AND SUBSIDIARIES

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosures

None

Item 9A. Controls and Procedures

Disclosure Controls and Procedures

An evaluation of the effectiveness of LCNB's internal controls over financial reporting was carried out under the supervision and with the participation of LCNB's management, including the Chief Executive Officer and Chief Financial Officer. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that LCNB's disclosure controls and procedures were effective as of the end of the period covered by this annual report.

Internal Control Over Financial Reporting

Information required by this item is set forth in the "Report of Management's Assessment of Internal Control over Financial Reporting" and the "Report of Independent Registered Public Accounting Firm" included in Item 8 of this 2015 Annual Report on Form 10-K.

Changes in Internal Control over Financial Reporting

During the fourth quarter 2015, there were no changes in LCNB's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, LCNB's internal control over financial reporting.

Item 9B. Other Information

None

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LCNB CORP. AND SUBSIDIARIES

PART III

Portions of the Company's Definitive Proxy Statement included in the Notice of Annual Meeting of Shareholders to be held April 26, 2016, which proxy statement will be mailed to shareholders within 120 days from the end of the fiscal year ended December 31, 2015, (the "Proxy Statement") are incorporated by reference into Part III.

Item 10. Directors, Executive Officers and Corporate Governance

The information required by this item concerning the Executive Officers and Directors of the Registrant is incorporated herein by reference under the caption "Directors and Executive Officers" of the Proxy Statement.

The information required by this item concerning the Audit Committee and Code of Business Conduct and Ethics is incorporated herein by reference under the captions "Board of Directors Meetings and Committees," "Audit Committee Report," and "Code of Ethics" of the Proxy Statement.

The information required by this item concerning Section 16(a) Beneficial Ownership Reporting Compliance is incorporated herein by reference under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" of the proxy Statement.

Item 11. Executive Compensation

The information contained in the Proxy Statement under the captions "Board of Directors Meetings and Committees" "Compensation Committee Interlocks and Insider Participation" "Equity Compensation Plan Information," "Compensation of Executive Officers," and "Compensation Committee Report on Executive Compensation" is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information contained in the Proxy Statement under the captions "Market Price of Stock and Dividend Data" and "Voting Securities and Principal Holders" is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information contained in the Proxy Statement under the captions "Election of Directors," "Directors and Executive Officers," "Board of Directors Meetings and Committees," and "Certain Relationships and Related Transactions" is incorporated herein by reference.

Item 14. Principal Accounting Fees and Services

The information contained in the Proxy Statement under the captions "Independent Registered Accounting Firm" and "Board of Directors Meetings and Committees" is incorporated herein by reference.

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LCNB CORP. AND SUBSIDIARIES

PART IV
Item 15. Exhibits, Financial Statement Schedules

(a)1. Financial Statements

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM
FINANCIAL STATEMENTS
Consolidated Balance Sheets as of December 31, 2015 and 2014.
Consolidated Statements of Income for the Years Ended December 31, 2015, 2014, and 2013.
Consolidated Statements of Comprehensive Income for the Years Ended December 31, 2015, 2014, and 2013.
Consolidated Statements of Shareholders' Equity for the Years Ended December 31, 2015, 2014, and 2013.
Consolidated Statements of Cash Flows for the Years Ended December 31, 2015, 2014, and 2013.
Notes to Consolidated Financial Statements

2. Financial Statement Schedules – None

3. Exhibits required by Item 601 Regulation S-K.

(a) Exhibit No.	Exhibit Description
2.1	Agreement and Plan of Merger dated as of October 9, 2012 by and between LCNB Corp. and First Capital Bancshares, Inc. – incorporated by reference to the Registrant's Form S-4 filed on October 29, 2012, Part I, Annex A.
2.2	Stock Purchase Agreement between LCNB Corp. and Colonial Banc Corp. dated as of October 28, 2013 - incorporated by reference to the Registrant's Current Report on Form 8-K filed on October 28, 2013, Exhibit 2.1.
2.3	Agreement and Plan of Merger dated as of December 29, 2014 by and between LCNB Corp. and BNB Bancorp, Inc., - incorporated by reference to the Registrant's Current Report on Form 8-K filed on January 2, 2015, Exhibit 2.1.
3.1	Amended and Restated Articles of Incorporation of LCNB Corp., as amended – incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2010, Exhibit 3.1.
3.2	Code of Regulations of LCNB Corp. - Incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2005, Exhibit 3(ii).
4.1	Warrant to Purchase Shares of Common Stock of the Registrant, dated January 9, 2009 - incorporated by reference to the Registrant's Current Report on Form 8-K filed on January 9, 2009, Exhibit 4.1.
4.2	Letter Agreement, dated as of January 9, 2009 between the Registrant and the U.S. Department of the Treasury, which includes the Securities Purchase Agreement – Standard Terms – incorporated by reference to the Registrant's Current Report on Form 8-K filed on January 9, 2009, Exhibit 10.1.
4.3	Substitute Warrant to Purchase Shares of Common Stock of the Registrant, dated January 9, 2009 – incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2009, Exhibit 4.3.
4.4	

	Repurchase Letter Agreement, dated as of October 21, 2009 between the Registrant and the U.S. Department of the Treasury – incorporated by reference to the Registrant's Current Report on Form 8-K filed on October 21, 2009, Exhibit 10.1.
10.1	LCNB Corp. Ownership Incentive Plan - incorporated by reference to Registrant's Form DEF 14A Proxy Statement pursuant to Section 14(a), dated March 15, 2002, Exhibit A (000-26121).

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LCNB CORP. AND SUBSIDIARIES

(a) Exhibit No.	Exhibit Description
10.2	LCNB Corp. 2015 Ownership Incentive Plan - incorporated by reference to Registrant's Form DEF 14A Proxy Statement pursuant to Section 14(a), dated March 13, 2015, Exhibit A (001-35292)
10.3	Form of Option Grant Agreement under the LCNB Corp. Ownership Incentive Plan - incorporated by reference to the Registrant's Form 10-K for the fiscal year ended December 31, 2005, Exhibit 10.2.
10.4	Letter Agreement, dated as of January 9, 2009 between the Registrant and the U.S. Department of the Treasury, which includes the Securities Purchase Agreement – Standard Terms - incorporated by reference to the Registrant's Current Report on Form 8-K filed on January 9, 2009, Exhibit 10.1.
10.5	Nonqualified Executive Retirement Plan – incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the period ended June 30, 2009, Exhibit 10.4.
10.6	Repurchase Letter Agreement, dated as of October 21, 2009 between the Registrant and the U.S. Department of the Treasury – incorporated by reference to the Registrant's Current Report on Form 8-K filed on October 21, 2009, Exhibit 10.1.
10.7	Form of Restricted Share Grant Agreement under the LCNB Corp. 2015 Ownership Incentive Plan.
14.1	LCNB Corp. Code of Business Conduct and Ethics - incorporated by reference to Registrant's 2003 Form 10-K, Exhibit 14.1.
14.2	LCNB Corp. Code of Ethics for Senior Financial Officers - Incorporated by reference to Registrant's 2003 Form 10-K, Exhibit 14.2.
21	LCNB Corp. Subsidiaries.
23.1	Consent of Independent Registered Public Accounting Firm.
23.2	Consent of Independent Registered Public Accounting Firm.
31.1	Certification of Chief Executive Officer under Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer under Section 302 of the Sarbanes-Oxley Act of 2002.
32	Certification of Chief Executive Officer and Chief Financial Officer under Section 906 of the Sarbanes-Oxley Act of 2002.
99.1	Certification of Chief Executive Officer Pursuant to Section 111(b)(4) of the Emergency Stabilization Act of 2008 - incorporated by reference to Registrant's 2009 Form 10-K, Exhibit 99.1.
99.2	Certification of Chief Financial Officer Pursuant to Section 111(b)(4) of the Emergency Stabilization Act of 2008 - incorporated by reference to Registrant's 2009 Form 10-K, Exhibit 99.2.
101	The following financial information from LCNB Corp.’s Annual Report on Form 10-K for the year ended December 31, 2015 is formatted in Extensible Business Reporting Language: (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Shareholders’ Equity, (v) the Consolidated Statements of Cash Flows, and (vi) the Notes to Consolidated Financial Statements, tagged as blocks of text.

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LCNB CORP. AND SUBSIDIARIES

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

LCNB Corp.
(Registrant)

/s/ Steve P. Foster
Steve P. Foster
Chief Executive Officer & President
March 9, 2016

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated:

/s/ Steve P. Foster Steve P. Foster Chief Executive Officer, President, & Director (Principal Executive Officer) March 9, 2016	/s/ William H. Kaufman William H. Kaufman Director March 9, 2016
/s/ Robert C. Haines II Robert C. Haines II Executive Vice President & Chief Financial Officer (Principal Financial and Accounting Officer) March 9, 2016	/s/ Anne E. Krehbiel Anne E. Krehbiel Director March 9, 2016
/s/ Stephen P. Wilson Stephen P. Wilson Chairman of the Board of Directors March 9, 2016	John H. Kochensparger III Director March 9, 2016
/s/ Spencer S. Cropper Spencer S. Cropper Director March 9, 2016	/s/ George L. Leasure George L. Leasure Director March 9, 2016