CITIZENS & NORTHERN CORP
Form 10-Q
May 11, 2009

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2009

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: 000-16084

CITIZENS & NORTHERN CORPORATION

(Exact name of Registrant as specified in its charter)

PENNSYLVANIA	23-2451943
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

90-92 MAIN STREET, WELLSBORO, PA 16901
(Address of principal executive offices) (Zip code)

570-724-3411
(Registrant s telephone number including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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). Yes o No **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. (Check one):

Large accelerated filer o	Accelerated filer þ	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller Reporting Company o

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

Indicate the number of shares outstanding of each of the registrant s classes of common stock, as of the latest practicable date.

Common Stock ($1.00 par value)	8,976,899 Shares Outstanding on May 1, 2009

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PART 1 FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
Consolidated Balance Sheet

(In Thousands Except Share Data)	**March 31, 2009 (Unaudited)**	**December 31, 2008 (Note)**
ASSETS		
Cash and due from banks:		
Noninterest-bearing	$ 15,775	$ 18,105
Interest-bearing	38,475	5,923
Total cash and cash equivalents	54,250	24,028
Trading securities	2,685	2,306
Available-for-sale securities	418,428	419,688
Held-to-maturity securities	405	406
Loans, net	723,388	735,687
Bank-owned life insurance	22,448	22,297
Accrued interest receivable	5,755	5,846
Bank premises and equipment, net	25,554	25,909
Foreclosed assets held for sale	1,057	298
Intangible asset Core deposit intangibles	746	826
Intangible asset Goodwill	11,942	12,014
Other assets	38,266	32,332
TOTAL ASSETS	$1,304,924	$1,281,637
LIABILITIES		
Deposits:		
Noninterest-bearing	$ 127,898	$ 124,922
Interest-bearing	746,108	739,135
Total deposits	874,006	864,057
Dividends payable	2,320	2,147
Short-term borrowings	41,769	48,547
Long-term borrowings	236,453	236,926
Accrued interest and other liabilities	9,230	7,934
TOTAL LIABILITIES	1,163,778	1,159,611
STOCKHOLDERS EQUITY		
Preferred stock, $1,000 par value; authorized 30,000 shares; $1,000 liquidation preference per share; 26,440 shares issued at March 31, 2009 and no shares issued at December 31, 2008	25,622	0
Common stock, par value $1.00 per share; authorized 20,000,000 shares in 2009 and 2008; issued 9,284,148 in 2009 and 2008	9,284	9,284
Paid-in capital	45,294	44,308

Retained earnings	90,745	97,757
Unamortized stock compensation	(104)	(48)
Treasury stock, at cost; 323,152 shares at March 31, 2009 and 348,041 shares at December 31, 2008	(5,626)	(6,061)
Sub-total	165,215	145,240
Accumulated other comprehensive loss:		
Unrealized losses on available-for-sale securities (including $7,856 at March 31, 2009 for which a portion of an other-than-temporary impairment loss has been recognized in earnings)	(23,816)	(23,120)
Defined benefit plans	(253)	(94)
Total accumulated other comprehensive loss	(24,069)	(23,214)
TOTAL STOCKHOLDERS EQUITY	141,146	122,026
TOTAL LIABILITIES & STOCKHOLDERS EQUITY	$1,304,924	$1,281,637

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

Note: The balance sheet at December 31, 2008 has been derived from the audited financial statements at that date but does not include all the information and notes required by U.S. generally accepted accounting principles for complete financial statements.

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CITIZENS & NORTHERN CORPORATION FORM 10-Q
CITIZENS & NORTHERN CORPORATION
CONSOLIDATED STATEMENT OF INCOME

	3 Months Ended	
(In Thousands, Except Per Share Data) (Unaudited)	**March 31, 2009**	**March 31, 2008**
INTEREST INCOME		
Interest and fees on loans	$ 11,357	$12,312
Interest on balances with depository institutions	1	13
Interest on loans to political subdivisions	393	365
Interest on federal funds sold	8	50
Interest on trading securities	23	33
Income from available-for-sale and held-to-maturity securities:		
Taxable	4,654	4,991
Tax-exempt	936	703
Dividends	199	233
Total interest and dividend income	17,571	18,700
INTEREST EXPENSE		
Interest on deposits	3,981	5,627
Interest on short-term borrowings	170	306
Interest on long-term borrowings	2,455	2,723
Total interest expense	6,606	8,656
Interest margin	10,965	10,044
(Credit) provision for loan losses	(173)	904
Interest margin after provision for loan losses	11,138	9,140
OTHER INCOME		
Service charges on deposit accounts	1,047	946
Service charges and fees	190	174
Trust and financial management revenue	769	877
Insurance commissions, fees and premiums	81	72
Increase in cash surrender value of life insurance	151	198
Other operating income	528	1,220
Sub-total	2,766	3,487
Total other-than-temporary impairment losses on available- for-sale securities	(24,981)	(249)
Portion of loss recognized in other comprehensive loss (before taxes)	8,301	0
Net impairment losses recognized in earnings	(16,680)	(249)
Realized gains on available-for-sale securities, net	1	139
	(16,679)	(110)

Net impairment losses recognized in earnings and realized gains on available-for-sale securities		
Total other (loss) income	(13,913)	3,377
OTHER EXPENSES		
Salaries and wages	3,341	3,691
Pensions and other employee benefits	1,244	1,151
Occupancy expense, net	742	754
Furniture and equipment expense	674	648
Pennsylvania shares tax	318	292
Other operating expense	2,319	1,928
Total other expenses	8,638	8,464
(Loss) income before income tax (credit) provision	(11,413)	4,053
Income tax (credit) provision	(4,388)	937
Net (loss) income	(7,025)	3,116
U.S. Treasury preferred dividends	309	0
NET (LOSS) INCOME AVAILABLE TO COMMON SHAREHOLDERS	$ (7,334)	$ 3,116
PER SHARE DATA:		
Net (loss) income per average common share basic	$ (0.82)	$ 0.35
Net (loss) income per average common share diluted	$ (0.82)	$ 0.35

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

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CITIZENS & NORTHERN CORPORATION FORM 10-Q
Consolidated Statements of Cash Flows

	3 Months Ended	
(In Thousands)	March 31, 2009	March 31, 2008
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net (loss) income	$ (7,025)	$ 3,116
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
(Credit) provision for loan losses	(173)	904
Net impairment losses realized in earnings and gains on available-for-sale securities	16,679	110
Gain on sale of foreclosed assets, net	(1)	(34)
Depreciation expense	713	719
Loss on disposition of premises and equipment	10	0
Accretion and amortization on securities, net	(50)	119
Accretion and amortization on loans, deposits and borrowings, net	(81)	(104)
Increase in cash surrender value of life insurance	(151)	(198)
Stock-based compensation	190	142
Amortization of core deposit intangibles	80	138
Deferred income taxes	(5,615)	(77)
Net increase in trading securities	(379)	(2,370)
Increase in accrued interest receivable and other assets	(1,050)	(2,046)
(Decrease) increase in accrued interest payable and other liabilities	(950)	1,055
Net Cash Provided by Operating Activities	2,197	1,474
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from maturity of held-to-maturity securities	1	1
Proceeds from sales of available-for-sale securities	6,430	6,692
Proceeds from calls and maturities of available-for-sale securities	14,224	18,431
Purchase of available-for-sale securities	(31,369)	(25,463)
Purchase of Federal Home Loan Bank of Pittsburgh stock	(4)	(283)
Redemption of Federal Home Loan Bank of Pittsburgh stock	0	1,164
Net decrease in loans	11,586	5,144
Purchase of premises and equipment	(368)	(283)
Return of principal on limited partnership investment	13	9
Proceeds from sale of foreclosed assets	187	259
Net Cash Provided by Investing Activities	700	5,671
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in deposits	9,913	4,372
Net (decrease) increase in short-term borrowings	(6,778)	1,217
Proceeds from long-term borrowings	0	10,000
Repayments of long-term borrowings	(415)	(14,325)
Purchase of treasury stock	0	(440)
Issuance of US Treasury preferred stock and warrant	26,409	0

Sale of treasury stock	13	0
Tax benefit from compensation plans	92	0
US Treasury preferred dividends paid	(106)	0
Common dividends paid	(1,803)	(2,151)
Net Cash Provided by (Used in) Financing Activities	27,325	(1,327)
INCREASE IN CASH AND CASH EQUIVALENTS	30,222	5,818
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	24,028	31,661
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 54,250	$ 37,479
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Assets acquired through foreclosure of real estate loans	$ 945	$ 163
Interest paid	$ 6,503	$ 8,731
Income taxes paid	$ 0	$ 362

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

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CITIZENS & NORTHERN CORPORATION FORM 10-Q
Consolidated Statement of Changes in Stockholders Equity

(In Thousands Except Per Share Data)	Preferred Stock	Common Stock	Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Unamortized Stock Compensation	Treasury Stock	Total
Balance, December 31, 2008	**$ 0**	**$9,284**	**$44,308**	**$97,757**	**$(23,214)**	**$ (48)**	**$(6,061)**	**$122,026**
Comprehensive (loss) income:								
Net loss				(7,025)				(7,025)
Unrealized gain on securities, net of reclassification and tax (including unrealized loss, net of tax, of $5,479 on securities for which an other-than-temporary impairment loss has been recognized)					1,682			1,682
Change in value of FASB 158 adjustment to equity					(159)			(159)
Total comprehensive loss								(5,502)
Reclassify non-credit portion of other-than-temporary impairment losses recognized in prior period				2,378	(2,378)			0
Issuance of U.S. Treasury preferred stock	25,588		821					26,409
Accretion of discount associated with U.S. Treasury preferred stock	34			(34)				0
Cash dividends on U.S. Treasury preferred stock				(275)				(275)
Cash dividends declared on common stock, $.24 per share				(2,148)				(2,148)
Shares issued for dividend reinvestment plan			(11)				352	341
Shares issued from treasury related to exercise of stock options			(3)				16	13
Restricted stock granted			10			(79)	69	0
Forfeiture of restricted stock			(1)			3	(2)	0
Stock-based compensation expense			170			20		190
Tax benefit from employee benefit plan				92				92
Balance, March 31, 2009	**$25,622**	**$9,284**	**$45,294**	**$90,745**	**$(24,069)**	**$(104)**	**$(5,626)**	**$141,146**

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

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Notes to Consolidated Financial Statements

1. BASIS OF INTERIM PRESENTATION

The financial information included herein, with the exception of the consolidated balance sheet dated December 31, 2008, is unaudited; however, such information reflects all adjustments (consisting solely of normal recurring adjustments) that are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations, cash flows and changes in stockholders equity for the interim periods. Certain 2008 information has been reclassified for consistency with the 2009 presentation.

Results reported for the three months ended March 31, 2009 might not be indicative of the results for the year ending December 31, 2009.

This document has not been reviewed or confirmed for accuracy or relevance by the Federal Deposit Insurance Corporation or any other regulatory agency.

2. CHANGES IN ACCOUNTING PRINCIPLES

As of January 1, 2009, the Corporation adopted the following new accounting pronouncements:

FASB Staff Position (FSP) FAS 115-2 and FAS 124-2, Recognition and Presentation of Other-Than-Temporary Impairments amends other-than-temporary impairment (OTTI) accounting guidance for debt securities, requires new disclosures and changes the presentation and amount of OTTI recognized in the income statement. The FSP requires impairment of debt securities be separated into (a) the amount of the total impairment related to credit loss, which is recognized in the income statement, and (b) the amount of the total impairment related to all other factors, which is recognized in other comprehensive income. The total OTTI is presented in the income statement with an offset for the amount of total OTTI recognized in other comprehensive income. As required, the Corporation recognized the cumulative effect of adopting this FSP as an increase in retained earnings of $2,378,000, and a decrease in accumulated other comprehensive loss of the same amount, as of January 1, 2009. For the three-month period ended March 31, 2009, the effect of adopting this FSP was to reduce impairment losses recognized in earnings by $8,301,000, and reduce the income tax provision by $2,822,000, resulting in an increase in net income of $5,479,000, or $0.61 per average common share. Disclosures required by this FSP are provided in Note 6 to the Consolidated Financial Statements.

FSP FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly provides additional guidance for estimating fair value in accordance with FASB Statement No. 157, Fair Value Measurements, when the volume and level of activity for the asset or liability have significantly decreased. This FSP also includes guidance on identifying circumstances that indicate a transaction is not orderly. There were no changes in the Corporation s valuation techniques or their application that resulted from adoption of this FSP. The FSP amends the disclosure requirements of FASB Statement No. 157 to require the Corporation to disclose in interim and annual periods the inputs and valuation techniques used to measure fair value and to discuss changes in valuation techniques and related inputs during the period. Further, the FSP requires presentation of information concerning securities in more detailed major security types than had been required in the past. Disclosures required by this FSP are provided in Note 5 to the Consolidated Financial Statements.

FSP FAS 107-1 and APB 28-1, Interim Disclosures about Fair Values of Financial Instruments requires the Corporation to provide disclosures each quarter that had previously been required only on an annual basis, about the fair value of financial instruments. The required disclosures are provided in Note 7 to the Consolidated Financial Statements.

3. PER COMMON SHARE DATA

Basic net (loss) income per average common share represents income available to common shareholders divided by the weighted-average number of shares of common stock outstanding. As shown in the table that follows, diluted net income per common share for the three months ended March 31, 2008 was computed using weighted average common shares outstanding, plus weighted-average common shares available from the exercise of all dilutive stock options, less the number of common shares that could be repurchased with the proceeds of stock option exercises based on the average share price of the Corporation s common stock during the period. For the three months ended March 31, 2009,

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outstanding stock options and the warrant (issued in January 2009) are anti-dilutive, and are therefore excluded in determining diluted loss per common share.

Quarter Ended March 31, 2009	Net Income	Weighted-Average Common Shares	Earnings Per Share
Earnings per common share basic and diluted	$(7,334,000)	8,956,076	$(0.82)
Quarter Ended March 31, 2008			
Earnings per common share basic	$ 3,116,000	8,974,407	$ 0.35
Dilutive effect of potential common stock arising from stock options:			
Exercise of outstanding stock options		148,788	
Hypothetical share repurchase at $19.31		(131,868)	
Earnings per common share diluted	$ 3,116,000	8,991,327	$ 0.35

4. COMPREHENSIVE (LOSS) INCOME

Comprehensive (loss) income is the total of (1) net (loss) income, and (2) all other changes in equity from non-stockholder sources, which are referred to as other comprehensive income. The components of comprehensive (loss) income, and the related tax effects, are as follows:

	3 Months Ended March 31,	
(In Thousands)	**2009**	**2008**
Net (loss) income	$ (7,025)	$ 3,116
Unrealized losses on available-for-sale securities:		
Unrealized holding losses on available-for-sale securities	(14,130)	(9,743)
Reclassification adjustment for losses realized in income	16,679	110
Other comprehensive gain (loss) before income tax	2,549	(9,633)
Income tax related to other comprehensive gain (loss)	867	(3,275)
Other comprehensive gain (loss) on available-for-sale securities	1,682	(6,358)
Unfunded pension and postretirement obligations:		
Change in items from defined benefit plans included in accumulated other comprehensive loss	(253)	0
Amortization of net transition obligation, prior service cost and net actuarial loss included in net periodic benefit cost	12	5
Other comprehensive (loss) gain before income tax	(241)	5
Income tax related to other comprehensive (loss) gain	(82)	1
Other comprehensive (loss) gain on unfunded retirement obligations	(159)	4

Net other comprehensive gain (loss)	1,523	(6,354)
Total comprehensive loss	$ (5,502)	$(3,238)

In the three-month period ended March 31, 2009, the Corporation recognized other comprehensive loss of $8,301,000 before income tax, or $5,479,000 after income tax, related to available-for-sale debt securities for which a portion of an OTTI loss has been recognized in earnings.

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5. ASSETS MEASURED AT FAIR VALUE ON A RECURRING BASIS

The Corporation measures certain assets at fair value on a recurring basis. Fair value is defined as the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. Statement of Financial Accounting Standards No. 157 establishes a framework for measuring fair value that includes a hierarchy used to classify the inputs used in measuring fair value. The hierarchy prioritizes the inputs used in determining valuations into three levels. The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement. The levels of the fair value hierarchy are as follows:

Level 1 Fair value is based on unadjusted quoted prices in active markets that are accessible to the Corporation for identical assets. These generally provide the most reliable evidence and are used to measure fair value whenever available.

Level 2 Fair value is based on significant inputs, other than Level 1 inputs, that are observable either directly or indirectly for substantially the full term of the asset through corroboration with observable market data. Level 2 inputs include quoted market prices in active markets for similar assets, quoted market prices in markets that are not active for identical or similar assets and other observable inputs.

Level 3 Fair value is based on significant unobservable inputs. Examples of valuation methodologies that would result in Level 3 classification include option pricing models, discounted cash flows and other similar techniques.

At March 31, 2009, assets measured at fair value on a recurring basis and the valuation methods used are as follows:

	March 31, 2009 Market Values Based on:			
(In Thousands)	**Quoted Prices in Active Markets (Level 1)**	**Other Observable Inputs (Level 2)**	**Unobservable Inputs (Level 3)**	**Total Fair Value**
AVAILABLE-FOR-SALE SECURITIES:				
Obligations of other U.S. Government agencies	$ 0	$ 16,048	$ 0	$ 16,048
Obligations of states and political subdivisions	14,882	71,976	0	86,858
Mortgage-backed securities	0	178,423	0	178,423
Collateralized mortgage obligations	0	64,012	0	64,012
Corporate bonds	0	1,069	0	1,069
Trust preferred securities issued by individual institutions	0	6,793	0	6,793
Collateralized debt obligations:				
Pooled trust preferred securities senior tranches	0	0	8,347	8,347
Pooled trust preferred securities mezzanine tranches	0	0	41,486	41,486
Other collateralized debt obligations	0	692	0	692
Total debt securities	14,882	339,013	49,833	403,728
Marketable equity securities	14,700	0	0	14,700
Total available-for-sale securities	29,582	339,013	49,833	418,428

TRADING SECURITIES,				
Obligations of states and political subdivisions	1,000	1,685	0	2,685
Total	$ 30,582	$340,698	$ 49,833	$421,113

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Management determined there were virtually no trades of pooled trust-preferred securities in the second half of 2008 or the first quarter of 2009, except for a limited number of transactions that took place as a result of bankruptcies, forced liquidations or similar circumstances. Also, in management s judgment, there were no available quoted market prices in active markets for assets sufficiently similar to the Corporation s pooled trust-preferred securities to be reliable as observable inputs. Accordingly, in the third quarter of 2008, the Corporation changed its method of valuing pooled trust-preferred securities from a Level 2 methodology that had been used in prior periods, based on price quotes received from pricing services, to a Level 3 methodology, using discounted cash flows.

At March 31, 2009, management calculated the fair values of pooled trust-preferred securities by applying discount rates to estimated cash flows for each security. Management used the cash flow estimates for each security determined using the process described in Note 6. Management used discount rates considered reflective of a market participant s expectations regarding the extent of credit and liquidity risk inherent in the securities. In establishing the discount rates, management considered: (1) the implied discount rates as of the end of 2007, prior to the market for trust-preferred securities becoming inactive; (2) adjustment to the year-end 2007 discount rates for the change in the spread between indicative market rates (3-month LIBOR, for most of the Corporation s securities) over corresponding risk-free rates (3-month U.S. Treasury Bill, for most of the Corporation s securities) in 2009; and (3) an additional adjustment an increase of 2% in the discount rate for liquidity risk. Management considered the additional 2% increase in the discount rate necessary in order to give some consideration to price estimates based on trades made under distressed conditions, as reported by brokers and pricing services. Management s estimates of cash flows and discount rates used to calculate fair values of pooled trust-preferred securities were based on sensitive assumptions, and market participants might use substantially different assumptions, which could result in calculations of fair values that would be substantially different than the amounts calculated by management.

Following is a reconciliation of activity for assets (pooled trust-preferred securities) measured at fair value based on significant unobservable information:

	3 Months Ended	
	Mar. 31, 2009 (Current)	Mar. 31, 2008 (Prior Year)
Balance, beginning of period	$ 58,914	$ 0
Transfers	0	0
Purchases, issuances and settlements	113	0
Realized (loss) on security deemed worthless	(335)	0
Unrealized (losses) included in earnings	(11,105)	0
Unrealized gains included in other comprehensive income	2,246	0
Balance, end of period	$ 49,833	$ 0

Unrealized losses included in earnings are from the Corporation s other-than-temporary impairment analysis of securities, as described in Note 6, and are included in net impairment losses recognized in earnings in the consolidated statement of income.

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6. SECURITIES

The Corporation s trading assets at March 31, 2009 and December 31, 2008 were composed exclusively of municipal bonds. Gains and losses from trading activities are included in other operating income in the consolidated statement of income as follows (in thousands):

	3 Months Ended	
	Mar. 31, 2009 (Current)	Mar. 31, 2008 (Prior Year)
Gross realized gains	$ 40	$ 35
Gross realized losses	0	0
Net change in unrealized gains/losses	(57)	(16)
Net (losses) gains	$(17)	$ 19
Income tax (credit) provision related to net losses	$ (6)	$ 6

Amortized cost and fair value of available-for-sale and held-to-maturity securities at March 31, 2009 and December 31, 2008 are summarized as follows:

	March 31, 2009			
(In Thousands)	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
AVAILABLE-FOR-SALE SECURITIES:				
Obligations of other U.S. Government agencies	$ 15,500	$ 548	$ 0	$ 16,048
Obligations of states and political subdivisions	95,303	181	(8,626)	86,858
Mortgage-backed securities	174,032	4,407	(16)	178,423
Collateralized mortgage obligations	67,584	339	(3,911)	64,012
Corporate bonds	1,000	69	0	1,069
Trust preferred securities issued by individual institutions	10,383	0	(3,590)	6,793
Collateralized debt obligations:				
Pooled trust preferred securities senior tranches	11,926	0	(3,579)	8,347
Pooled trust preferred securities mezzanine tranches	63,113	0	(21,627)	41,486
Other collateralized debt obligations	692	0	0	692
Total debt securities	439,533	5,544	(41,349)	403,728
Marketable equity securities	14,973	807	(1,080)	14,700
Total	$454,506	$6,351	$(42,429)	$418,428
HELD-TO-MATURITY SECURITIES:				
Obligations of the U.S. Treasury	$ 303	$ 12	$ 0	$ 315

Obligations of other U.S. Government agencies	100	3	0	103
Mortgage-backed securities	2	0	0	2
Total	$ 405	$ 15	$ 0	$ 420

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(In Thousands)	Amortized Cost	December 31, 2008 Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
AVAILABLE-FOR-SALE SECURITIES:				
Obligations of other U.S. Government agencies	$ 15,500	$ 701	$ 0	$ 16,201
Obligations of states and political subdivisions	80,838	197	(6,812)	74,223
Mortgage-backed securities	171,453	2,632	(229)	173,856
Collateralized mortgage obligations	70,619	187	(2,572)	68,234
Corporate bonds	1,000	117	0	1,117
Trust preferred securities issued by individual institutions	10,436	0	(2,835)	7,601
Collateralized debt obligations:				
Pooled trust preferred securities senior tranches	11,938	0	(3,296)	8,642
Pooled trust preferred securities mezzanine tranches	70,826	0	(20,554)	50,272
Other collateralized debt obligations	692	0	0	692
Total debt securities	433,302	3,834	(36,298)	400,838
Marketable equity securities	21,405	1,918	(4,473)	18,850
Total	$454,707	$5,752	$(40,771)	$419,688
HELD-TO-MATURITY SECURITIES:				
Obligations of the U.S. Treasury	$ 304	$ 16	$ 0	$ 320
Obligations of other U.S. Government agencies	100	4	0	104
Mortgage-backed securities	2	0	0	2
Total	$ 406	$ 20	$ 0	$ 426

The following table presents gross unrealized losses and fair value of available-for-sale investments aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at March 31, 2009 and December 31, 2008.

March 31, 2009

(In Thousands)	Less Than 12 Months Fair Value	Unrealized Losses	12 Months or More Fair Value	Unrealized Losses	Total Fair Value	Unrealized Losses
AVAILABLE-FOR-SALE SECURITIES:						
Obligations of other U.S. Government agencies	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Obligations of states and political subdivisions	31,847	(2,837)	30,270	(5,789)	62,117	(8,626)
Mortgage-backed securities	1,434	(3)	3,439	(13)	4,873	(16)

Collateralized mortgage obligations	6,812	(1,299)	32,893	(2,612)	39,705	(3,911)
Corporate bonds	0	0	0	0	0	0
Trust preferred securities issued by individual institutions	3,240	(1,770)	3,553	(1,820)	6,793	(3,590)
Collateralized debt obligations:						
Pooled trust preferred securities senior tranches	8,347	(3,579)	0	0	8,347	(3,579)
Pooled trust preferred securities mezzanine tranches	0	0	41,486	(21,627)	41,486	(21,627)
Other collateralized debt obligations	0	0	0	0	0	0
Total debt securities	51,680	(9,488)	111,641	(31,861)	163,321	(41,349)
Marketable equity securities	1,001	(422)	869	(658)	1,870	(1,080)
Total temporarily impaired available-for-sale securities	$52,681	$(9,910)	$112,510	$(32,519)	$165,191	$(42,429)

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December 31, 2008

(In Thousands)	Less Than 12 Months Fair Value	Less Than 12 Months Unrealized Losses	12 Months or More Fair Value	12 Months or More Unrealized Losses	Total Fair Value	Total Unrealized Losses
AVAILABLE-FOR-SALE SECURITIES:						
Obligations of other U.S. Government agencies	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Obligations of states and political subdivisions	29,867	(3,202)	26,679	(3,610)	56,546	(6,812)
Mortgage-backed securities	21,746	(137)	6,713	(92)	28,459	(229)
Collateralized mortgage obligations	26,117	(1,054)	17,644	(1,518)	43,761	(2,572)
Corporate bonds	0	0	0	0	0	0
Trust preferred securities issued by individual institutions	3,810	(1,201)	3,791	(1,634)	7,601	(2,835)
Collateralized debt obligations:						
Pooled trust preferred securities senior tranches	8,642	(3,296)	0	0	8,642	(3,296)
Pooled trust preferred securities mezzanine tranches	0	0	41,911	(20,554)	41,911	(20,554)
Other collateralized debt obligations	0	0	0	0	0	0
Total debt securities	90,182	(8,890)	96,738	(27,408)	186,920	(36,298)
Marketable equity securities	4,062	(1,080)	6,407	(3,393)	10,469	(4,473)
Total temporarily impaired available-for-sale securities	$94,244	$(9,970)	$103,145	$(30,801)	$197,389	$(40,771)

Management evaluates securities for OTTI at least on a quarterly basis, and more frequently when economic or market conditions warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) whether the Corporation intends to sell the security or more likely than not will be required to sell the security before its anticipated recovery. The Corporation recognized net impairment losses in earnings, as follows:

(In Thousands)	3 Months Ended March 31, 2009	3 Months Ended March 31, 2008
Pooled trust preferred securities mezzanine tranches	$(11,105)	$ 0
Marketable equity securities (bank stocks)	(5,575)	(249)
Net impairment losses recognized in earnings	$(16,680)	$(249)

A summary of information management considered in evaluating debt and equity securities for OTTI at March 31, 2009 is provided below.

Debt Securities

In addition to the effects of volatility in interest rates on individual debt securities, management believes valuations of debt securities at March 31, 2009 have been negatively impacted by events affecting the overall credit markets during the last quarter of 2007, all of 2008 and the first quarter of 2009. There have been widespread disruptions to the normal operation of bond markets. Particularly with regard to pooled trust-preferred securities, trading volume has been limited and consisted almost entirely of sales by distressed sellers.

At March 31, 2009, management performed an assessment for possible OTTI of the Corporation s investments in state and political subdivisions, collateralized mortgage obligations and trust preferred securities issued by individual issuers (banking companies) on an issue-by-issue basis, relying on information obtained from various sources, including publicly available financial data, ratings by external agencies, brokers and other sources. The extent of individual analysis applied to each security depended on the size of the Corporation s investment, as well as management s perception of the credit risk associated with each security. Based on the results of the assessment, management believes impairment of these debt securities at March 31, 2009 to be temporary.

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Trust-preferred securities are very long-term (usually 30-year maturity) instruments with characteristics of both debt and equity, mainly issued by banks. The Corporation s investments in pooled trust-preferred securities are each made up of 30 or more companies with geographic and size diversification. Almost all of the Corporation s pooled trust-preferred securities are composed of debt issued by banking companies, with lesser amounts issued by insurance companies and real estate investment trusts.

All of the Corporation s pooled trust-preferred securities were deemed investment grade by Moody s and/or Fitch when they were purchased; however, all of the rated securities have been downgraded by Moody s and by Fitch. As of March 31, 2009, the Corporation s investment in a senior tranche security has an investment grade rating; however, all the mezzanine tranche securities have ratings several levels below investment grade or are not rated. In 2008 and the first quarter 2009, some of the issuers of trust-preferred securities that are included in the Corporation s pooled investments have elected to defer payment of interest on these obligations (trust-preferred securities typically permit deferral of quarterly interest payments for up to five years), and some issuers have defaulted. Trust-preferred securities are structured so that the issuers pay more interest into the trusts than would be required for pass through to the investors in the rated notes (such as the Corporation), with the excess used to cover administrative and other expenses, and to provide a cushion for some protection against the risk of loss for investors in the rated notes.

As of March 31, 2009, management evaluated the pooled trust-preferred securities for OTTI by estimating the cash flows expected to be received from each security, taking into account estimated levels of deferrals and defaults by the underlying issuers. In determining cash flows, management assumed all issuers currently deferring or in default would make no future payments, and assigned estimated future default levels for the remaining issuers in each security based on financial strength ratings assigned by a national ratings service. Management calculated the present value of each security based on the current book yield, adjusted for future changes in 3-month LIBOR (which is the index rate on the Corporation s adjustable rate pooled trust-preferred securities) based on the applicable forward curve. Management s estimates of cash flows used to evaluate other-than-temporary impairment of pooled trust-preferred securities were based on sensitive assumptions regarding the timing and amounts of defaults that may occur, and changes in those assumptions could produce different conclusions for each security.

For the senior tranche security with an amortized cost of $11,926,000, and for seven of the mezzanine tranche securities with an aggregate amortized cost of $27,375,000, the present value at March 31, 2009 determined based on estimated cash flows had not declined from management s previous assumptions used to determine book value, and accordingly, impairment was deemed temporary. However, for thirteen of the securities, the present values declined, including one security which was deemed worthless and written off in the amount of $335,000. For the remaining twelve securities, the Corporation wrote the amortized cost basis down to present value, resulting in net OTTI charges to earnings totaling $11,105,000 (pretax).

As described in Note 2, the Corporation adopted FSP FAS 115-2 and FAS 124-2, Recognition and Presentation of Other-Than-Temporary Impairments, effective January 1, 2009. As a result of implementing the FSP, the Corporation separated OTTI related to the trust-preferred securities into (a) the amount of the total impairment related to credit loss, which is recognized in the income statement, and (b) the amount of the total impairment related to all other factors, which is recognized in other comprehensive income. The Corporation measured the credit loss component of OTTI based on the difference between: (1) the present value of estimated cash flows, at the book yield in effect prior to recognition of any OTTI, as of March 31, 2009, and (2) the present value of estimated cash flows as of December 31, 2008 using book yield and management s cash flow assumptions at that time. For the three-month period ended March 31, 2009, the effect of adopting this FSP was to reduce pre-tax impairment losses recognized in earnings by $8,301,000.

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A roll-forward of the OTTI amount related to credit losses for the three months ended March 31, 2009 is as follows:

(In Thousands)	
Balance of credit losses on debt securities for which a portion of OTTI was recognized in other comprehensive income, beginning of period (as measured effective January 1, 2009 upon adoption of FSP FAS 115-2 and FAS 124-2)	$ (2,362)
Additional credit loss for which an OTTI was not previously recognized	(7,497)
Additional credit loss for which an OTTI was previously recognized when the Corporation does not intend to sell the security and it is not more likely than not the Corporation will be required to sell the security before recovery of its amortized cost basis	(3,608)
Balance of credit losses on debt securities for which a portion of OTTI was recognized in other comprehensive income, end of period	$(13,467)

Equity Securities

The Corporation s marketable equity securities include stocks of banking companies, and to a lesser extent, a mix of non-financial equities which include large cap domestic and foreign companies, as well as equity-based mutual funds and similar instruments. At March 31, 2009, the fair value of bank equities was $12,800,000, and the fair value of non-bank equities was $1,900,000. Management evaluates the financial condition, earnings, dividend payment prospects and other relevant factors related to each issuer for which the stock is in an unrealized loss position, to determine whether the Corporation can realistically expect to recover its cost basis without realizing a loss. Management s decision to record OTTI losses on bank stocks in the three months ended March 31, 2009 was based on a combination of: (1) significant market depreciation, including an average reduction in market prices of 15% in the first quarter 2009, and (2) the possibility the Corporation may sell some of the stocks in 2009 to generate capital losses, which could be carried back and offset against capital gains generated in 2006 and 2007 to realize tax refunds. After the impact of the impairment charges, the Corporation held 3 bank stocks in an unrealized loss position at March 31, 2009, with an aggregate cost basis of $301,000, fair value of $265,000 and an unrealized loss of $36,000. Consistent with declines in U.S. and worldwide equity markets, the values of the non-financial equities fell in the last half of 2008 and first quarter 2009. At March 31, 2009, the total amortized cost basis of investments in non-bank equities in an unrealized loss position was $2,649,000, with an aggregate fair value of $1,605,000 and an unrealized loss of $1,044,000, or 39% of cost. There were 47 non-bank equities in an unrealized loss position at March 31, 2009. The largest unrealized loss amounts were from: (1) Federated Index Trust Mid-Cap Fund, which is indexed to the S&P 400 Mid-Cap Index, with an unrealized loss of $272,000 or 47% of cost, and (2) iShares MCSI EAFE Index Funds, an exchange traded fund indexed to international stocks, with an unrealized loss of $191,000, or 54% of cost. In the case of these two securities, as well as the rest of the non-bank equities, management believes the impairment to be a product of the current, cyclical downturn in equity markets, and management expects the Corporation to hold the securities until its cost basis can be recovered.

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7. FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. When possible, fair value is determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Corporation s financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument. SFAS No. 107 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Therefore, the aggregate fair value amounts presented may not represent the underlying fair value of the Corporation.

The Corporation used the following methods and assumptions in estimating fair value disclosures for financial instruments:

CASH AND CASH EQUIVALENTS The carrying amounts of cash and short-term instruments approximate fair values.

SECURITIES Fair values for securities, excluding restricted equity securities, are based on quoted market prices or other methods as described in Note 5. The carrying value of restricted equity securities approximates fair value based on applicable redemption provisions.

LOANS Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as commercial, commercial real estate, residential mortgage and other consumer. Each loan category is further segmented into fixed and adjustable rate interest terms and by performing and nonperforming categories. The fair value of performing loans is calculated by discounting contractual cash flows, adjusted for estimated prepayments based on historical experience, using estimated market discount rates that reflect the credit and interest rate risk inherent in the loans. Fair value of nonperforming loans is based on recent appraisals or estimates prepared by the Corporation s lending officers.

DEPOSITS The fair value of deposits with no stated maturity, such as noninterest-bearing demand deposits, savings, money market and interest checking accounts, is (by definition) equal to the amount payable on demand at March 31, 2009 and December 31, 2008. The fair value of all other deposit categories is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits of similar remaining maturities. The fair value estimates of deposits do not include the benefit that results from the low-cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market, commonly referred to as the core deposit intangible.

BORROWED FUNDS The fair value of borrowings is estimated using discounted cash flow analyses based on rates currently available to the Corporation for similar types of borrowing arrangements.

ACCRUED INTEREST The carrying amounts of accrued interest receivable and payable approximate fair values.

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The estimated fair values, and related carrying amounts, of the Corporation s financial instruments are as follows:

	March 31, 2009		December 31, 2008	
(In Thousands)	**Carrying Amount**	**Fair Value**	**Carrying Amount**	**Fair Value**
Financial assets:				
Cash and cash equivalents	$ 54,250	$ 54,250	$ 24,028	$ 24,028
Trading securities	2,685	2,685	2,306	2,306
Available-for-sale securities	418,428	418,428	419,688	419,688
Held-to-maturity securities	405	420	406	426
Restricted equity securities	8,958	8,958	8,954	8,954
Loans, net	723,388	721,503	735,687	725,586
Accrued interest receivable	5,755	5,755	5,846	5,846
Financial liabilities:				
Deposits	874,006	883,989	864,057	870,767
Short-term borrowings	41,769	41,330	48,547	47,653
Long-term borrowings	236,453	243,470	236,926	240,521
Accrued interest payable	960	960	956	956

8. DEFINED BENEFIT PLANS

The Corporation sponsors a defined benefit health care plan that provides postretirement medical benefits and life insurance to employees who meet certain age and length of service requirements. This plan contains a cost-sharing feature, which causes participants to pay for all future increases in costs related to benefit coverage. Accordingly, actuarial assumptions related to health care cost trend rates do not affect the liability balance at March 31, 2009 and December 31, 2008, and will not affect the Corporation s future expenses. The Corporation uses a December 31 measurement date for the postretirement plan.

The Corporation s defined benefit pension plan was frozen and terminated, effective December 31, 2007. In September 2008, the Corporation funded and settled substantially all of its obligations under the Plan.

In 2007, the Corporation assumed the Citizens Trust Company Retirement Plan, a defined benefit pension plan for which benefit accruals and participation were frozen in 2002. The Citizens Trust Company Retirement Plan is not significant in comparison to the other defined benefit plans, and information related to that plan is not included in the table that follows.

The components of net periodic benefit costs from these defined benefit plans are as follows:

Defined Benefit Plans

	Pension Three Months Ended March 31,		Postretirement Three Months Ended March 31,	
(In Thousands)	**2009**	**2008**	**2009**	**2008**
Service cost	$0	$ 10	$19	$17
Interest cost	0	149	23	20
Expected return on plan assets	0	(77)	0	0
Amortization of transition (asset) obligation	0	(6)	9	9
Amortization of prior service cost	0	0	3	2
Recognized net actuarial loss	0	0	0	0
Net periodic benefit cost	$0	$ 76	$54	$48

In the first quarter 2009, the Corporation funded postretirement contributions totaling $15,000, with estimated annual postretirement contributions of $75,000 expected in 2009 for the full year.

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9. STOCK-BASED COMPENSATION PLANS

In January 2009, the Corporation granted options to purchase a total of 79,162 shares of common stock through its Stock Incentive and Independent Directors Stock Incentive Plans. In January 2008, the Corporation granted options to purchase a total of 83,257 shares of common stock. The exercise price for the 2009 awards is $19.88 per share, and the exercise price for the 2008 awards is $17.50 per share, based on the market price as of the date of each grant. The Corporation records stock option expense based on estimated fair value calculated using an option valuation model. The Corporation recorded total stock option expense of $170,000 in the first quarter 2009 and $118,000 in the first quarter 2008. The Corporation expects total stock option expense for the year ending December 31, 2009 to be approximately $334,000, and total stock option expense for the year ended December 31, 2008 was $209,000.

In calculating the fair value, the Corporation utilized the Black-Scholes option-pricing model. The calculated fair value of each option granted, and significant assumptions used in the calculations, are as follows:

	2009	**2008**
Fair value of each option granted	$4.21	$3.15
Volatility	28%	23%
Expected option lives	9 Years	9 Years
Risk-free interest rate	3.15%	4.05%
Dividend yield	3.94%	3.74%

In calculating the estimated fair value of stock option awards, management based its estimates of volatility and dividend yield on the Corporation s experience over the immediately prior period of time consistent with the estimated lives of the options. The risk-free interest rate was based on the published yield of zero-coupon U.S. Treasury strips with an applicable maturity as of the grant dates. The 9-year expected option life used for both 2009 and 2008 awards was based on management s estimates of the average term for all options issued under both plans. For the 2009 and 2008 awards, management assumed a 23% forfeiture rate for options granted under the Stock Incentive Plan, and a 0% forfeiture rate for the Directors Stock Incentive Plan. These estimated forfeiture rates were determined based on the Corporation s historical experience.

Also, the Corporation awarded a total of 3,890 shares in January 2009 and 5,062 shares in January 2008 of restricted stock under the Stock Incentive and Independent Directors Stock Incentive Plans. Compensation cost related to restricted stock is recognized based on the market price of the stock at the grant date over the vesting period. Total restricted stock expense amounted to $20,000 in the first quarter of 2009, and $24,000 in the first quarter of 2008.

10. ISSUANCE OF PREFERRED STOCK AND WARRANT UNDER THE TARP CAPITAL PURCHASE PROGRAM

On January 16, 2009, the Corporation issued 26,440 shares of Series A Preferred Stock (Preferred Stock) and a Warrant to purchase up to 194,794 shares of common stock at an exercise price of $20.36 per share. The Corporation sold the Preferred Stock and Warrant to the United States Department of the Treasury (Treasury) under the TARP Capital Purchase Program (the Program) for an aggregate price of $26,440,000.

The Preferred Stock has no maturity date. The Preferred Stock has a par value of $1,000 per share and a liquidation preference amount of $1,000 per share. The Preferred Stock pays a cumulative dividend rate of 5% per annum for the first five years and will reset to a rate of 9% per annum after year five. The dividend is payable quarterly in arrears. The Treasury may transfer the Preferred Stock to a third party at any time. The American Recovery and Reinvestment Act of 2009, which became effective in February 2009, included a change to the Program that permits the Corporation to redeem the Preferred Stock at any time, subject to approval of banking regulators, for a price equal to the original issue price plus any accrued but unpaid dividends. If the Corporation were to redeem all the outstanding shares of Preferred Stock by December 31, 2009, 50% of the common shares issuable pursuant to the Warrant would be cancelled.

The shares of Preferred Stock are non-voting, other than class voting rights on (i) any authorization or issuance of shares ranking senior to the Preferred Stock, (ii) any amendment to the rights of the shares of Preferred Stock, or (iii) any merger, exchange or similar transaction which would adversely affect the rights of the Preferred Stock. If dividends on the Preferred Stock are not paid in full for six dividend periods, whether or not consecutive, the holders of the Preferred Stock will have the right to elect 2 directors. The right to elect directors will end when full dividends have been paid for four consecutive dividend periods. As of March 31, 2009, no dividends on the preferred stock were in arrears.

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Pursuant to participation in the Program, the Corporation may continue to pay dividends on its common stock, subject to the following requirements and limitations: (1) all accrued and unpaid dividends for all past dividend periods on the Preferred Stock must be fully paid; and (2) consent of the Treasury is required for any increase in the per share dividends on common shares until January 16, 2012, unless prior to that date, the Corporation has redeemed the Preferred Stock in whole or the Treasury has transferred all of the Preferred Stock to third parties. Also, until January 16, 2012 (unless prior to that date, the Corporation has redeemed the Preferred Stock in whole or the Treasury has transferred all of the Preferred Stock to third parties) the Treasury s consent is required for any repurchases of common stock, except for repurchases of shares in connection with employee benefit plans in the ordinary course of business consistent with past practice.

The Warrant is exercisable and has a term of 10 years. The number of common shares that could be acquired upon exercise was based on 15% of the total proceeds, with the exercise price determined using the average market price of the Corporation s common stock for the 20 trading days immediately prior to issuance. The Warrant is not subject to restrictions on transfer, except that Treasury may only transfer or exercise the Warrant with respect to one-half of the shares underlying the Warrant prior to the earlier of (i) the date on which the Corporation has received proceeds of at least $26,440,000 from a qualifying equity offering of Tier 1 perpetual preferred stock or common stock and (ii) December 31, 2009. Treasury has agreed that it will not vote any of the shares of common stock that it acquires upon exercise of the Warrant. This does not apply to any other person who acquires from Treasury any portion of the Warrant, or the shares of common stock underlying the Warrant.

In 2009, the Corporation recorded issuance of the Preferred Stock and Warrant as increases in stockholders equity. Proceeds from the transaction, net of direct issuance costs of $31,000, have been allocated between Preferred Stock and the Warrant based on their respective fair values at the date of issuance. The fair value of the Preferred Stock was estimated based on dividend rates on recent preferred stock and other capital issuances by banking companies, and the fair value of the Warrant was estimated using the Black-Scholes option model. The amount allocated to the Warrant (recorded as an increase in Paid in Capital) was $821,000, and the amount initially allocated to Preferred Stock was $25,588,000. As a result, the Preferred Stock s initial carrying value was at a discount to the liquidation value or stated value of $26,440,000. In accordance with the SEC s Staff Accounting Bulletin No. 68, Increasing Rate Preferred Stock, the discount is considered an unstated dividend cost that shall be accreted over the period preceding commencement of the perpetual dividend using the effective interest method, by charging the imputed dividend cost against retained earnings and increasing the carrying amount of the Preferred Stock by a corresponding amount. The discount is therefore being accreted over five years, resulting in an effective dividend rate (including stated dividends and the accretion of the discount on Preferred Stock) of 5.80%. In the first quarter 2009, total dividends on Preferred Stock of $309,000, which has been deducted from net income to arrive at net income available to common shareholders in the Consolidated Statements of Income, included a quarterly dividend paid in February 2009 of $106,000, dividends accrued based on the stated value of $169,000 and accretion of the discount on Preferred Stock of $34,000.

11. CONTINGENCIES

In the normal course of business, the Corporation may be subject to pending and threatened lawsuits in which claims for monetary damages could be asserted. In management s opinion, the Corporation s financial position and results of operations would not be materially affected by the outcome of such pending legal proceedings.

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

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Certain statements in this section and elsewhere in this quarterly report on Form 10-Q are forward-looking statements. Citizens & Northern Corporation and its wholly-owned subsidiaries (collectively, the Corporation) intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Reform Act of 1995. Forward-looking statements, which are not historical facts, are based on certain assumptions and describe future plans, business objectives and expectations, and are generally identifiable by the use of words such as, should , likely , expect , plan , anticipate , target , forecast , and goal . These forwa statements are subject to risks and uncertainties that are difficult to predict, may be beyond management s control and could cause results to differ materially from those expressed or implied by such forward-looking statements. Factors which could have a material, adverse impact on the operations and future prospects of the Corporation include, but are not limited to, the following:

- changes in monetary and fiscal policies of the Federal Reserve Board and the U. S. Government, particularly related to changes in interest rates
- changes in general economic conditions
- legislative or regulatory changes
- downturn in demand for loan, deposit and other financial services in the Corporation s market area
- increased competition from other banks and non-bank providers of financial services
- technological changes and increased technology-related costs
- changes in accounting principles, or the application of generally accepted accounting principles.

These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements.

REFERENCES TO 2009 AND 2008

Unless otherwise noted, all references to 2009 in the following discussion of operating results are in