FARMERS CAPITAL BANK CORP
Form 10-K
March 12, 2015
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the Fiscal Year Ended December 31, 2014

or

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

Commission File Number 000-14412

Farmers Capital Bank Corporation
(Exact name of registrant as specified in its charter)

Kentucky	61-1017851
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

P.O. Box 309

202 West Main St.	
Frankfort, Kentucky	40601
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (502) 227-1668

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

Common Stock - $.125 per share Par Value	The NASDAQ Global Select Market
(Title of each class)	(Name of each exchange on which registered)

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

None
(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.

Yes 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.

Yes 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.

Yes No

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 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 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.

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.

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes No

The aggregate market value of the registrant's outstanding voting stock held by non-affiliates on June 30, 2014 (the last business day of the registrant's most recently completed second fiscal quarter) was $160 million based on the closing price per share of the registrant's common stock reported on the NASDAQ.

As of March 1, 2015, there were 7,490,158 shares of common stock outstanding.

Documents incorporated by reference:

Portions of the Registrant’s Proxy Statement relating to the Registrant’s 2015 Annual Meeting of Shareholders are incorporated by reference into Part III.

An index of exhibits filed with this Form 10-K can be found on page 134.

FARMERS CAPITAL BANK CORPORATION

FORM 10-K

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PART I

Item 1. Business

The disclosures set forth in this item are qualified by Item 1A ("*Risk Factors*") beginning on page 23 and the section captioned *"Forward-Looking Statements"* in Item 7 ("*Management's Discussion and Analysis of Financial Condition and Results of Operations"*) beginning on page 39 of this report and other cautionary statements contained elsewhere in this report.

Organization

Farmers Capital Bank Corporation (the "Registrant," "Company," "we," "us," or "Parent Company") is a bank holding company with four wholly-owned bank subsidiaries. The Registrant was originally formed as a bank holding company under the Bank Holding Company Act of 1956, as amended, on October 28, 1982 under the laws of the Commonwealth of Kentucky ("Commonwealth"). The Company provides a wide range of banking and bank-related services to customers throughout Central and Northern Kentucky. The Company's four bank subsidiaries include Farmers Bank & Capital Trust Company ("Farmers Bank"), Frankfort, Kentucky; United Bank & Trust Company ("United Bank"), Versailles, Kentucky; First Citizens Bank ("First Citizens"), Elizabethtown, Kentucky; and Citizens Bank of Northern Kentucky, Inc. ("Citizens Northern"), Newport, Kentucky.

The Company also owns FCB Services, Inc., ("FCB Services"), a data processing subsidiary located in Frankfort, Kentucky; FFKT Insurance Services, Inc., ("FFKT Insurance"), a captive property and casualty insurance company in Frankfort, Kentucky; and Farmers Capital Bank Trust I ("Trust I"), Farmers Capital Bank Trust II ("Trust II"), and Farmers Capital Bank Trust III ("Trust III"), which are unconsolidated trusts established to complete the private offering of trust preferred securities. In the case of Trust I and Trust II, the proceeds of the offerings were used to finance the cash portion of the acquisition in 2005 of Citizens Bancorp Inc. ("Citizens Bancorp"), the former parent company of Citizens Northern. For Trust III, the proceeds of the offering were used to finance the cost of acquiring Company shares under a share repurchase program during 2007. EKT Properties, Inc. ("EKT"), established during 2008 to manage and liquidate certain real estate properties repossessed by the Company, was dissolved effective at year end 2014.

The Company provides a broad range of financial services at its 36 locations in 23 communities throughout Central and Northern Kentucky to individual, business, agriculture, government, and educational customers. Its primary deposit products are checking, savings, and term certificate accounts. Its primary lending products are residential mortgage, commercial lending, and consumer installment loans. Substantially all loans and leases are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Commercial loans and leases are expected to be repaid from cash flow from operations of businesses. Other services provided by the Company include, but are not limited to, cash management services, issuing letters of credit, safe deposit box rental, and providing funds transfer services. The Company has minor amounts of other financial instruments, including deposit accounts in other financial institutions and federal funds sold, neither of which represent a potential concentration of credit risk.

While the chief decision-makers monitor the revenue streams of the various products and services, operations are managed and financial performance is evaluated on a Company-wide basis. Operating segments are aggregated into one as operating results for all segments are similar. Accordingly, all of the financial service operations are considered by management to be aggregated in one reportable segment. As of December 31, 2014, the Company had $1.8 billion in consolidated total assets.

Organization Chart

Subsidiaries of Farmers Capital Bank Corporation at December 31, 2014 are indicated in the table that follows. Percentages reflect the ownership interest held by the parent company of each of the subsidiaries. Tier 2 subsidiaries are direct subsidiaries of Farmers Capital Bank Corporation. Tier 3 subsidiaries are direct subsidiaries of the Tier 2 subsidiary listed immediately above them. Tier 4 subsidiaries are direct subsidiaries of the Tier 3 subsidiary listed immediately above them. Tier 5 subsidiaries are direct subsidiaries of the Tier 4 subsidiary listed immediately above them.

Tier	Entity
1	Farmers Capital Bank Corporation, Frankfort, KY (Parent Company)
2	United Bank & Trust Company, Versailles, KY 100%
3	EGT Properties, Inc., Georgetown, KY 100%
4	WCO, LLC, Versailles, KY 6.6%
4	NUBT Properties, LLC, Georgetown, KY 83%
5	Flowing Creek Realty, LLC, Bloomfield, IN 67%
2	Farmers Bank & Capital Trust Company, Frankfort, KY 100%
3	Farmers Bank Realty Co., Frankfort, KY 100%
3	Leasing One Corporation, Frankfort, KY 100%
3	EG Properties, Inc., Frankfort, KY 100%
4	WCO, LLC, Versailles, KY 93.4%
3	Austin Park Apartments, LTD, Frankfort, KY 99%
3	Frankfort Apartments II, LTD, Frankfort, KY 99.9%
3	Farmers Capital Insurance Corporation, Frankfort, KY 100%
2	First Citizens Bank, Elizabethtown, KY 100%
3	HBJ Properties, LLC, Elizabethtown, KY 100%
2	Citizens Bank of Northern Kentucky, Inc., Newport, KY 100%
3	ENKY Properties, Inc., Newport, KY 100%
4	NUBT Properties, LLC, Georgetown, KY 17%
5	Flowing Creek Realty, LLC, Bloomfield, IN 67%
2	FCB Services, Inc., Frankfort, KY 100%
2	FFKT Insurance Services, Inc., Frankfort, KY 100%
2	Farmers Capital Bank Trust I, Frankfort, KY 100%
2	Farmers Capital Bank Trust II, Frankfort, KY 100%
2	Farmers Capital Bank Trust III, Frankfort, KY 100%

Farmers Bank

Farmers Bank, originally organized in 1850, is a state chartered bank engaged in a wide range of commercial and personal banking activities, which include accepting savings, time and demand deposits; making secured and unsecured loans to corporations, individuals and others; providing cash management services to corporate and individual customers; issuing letters of credit; renting safe deposit boxes; and providing funds transfer services. The bank's lending activities include making commercial, construction, mortgage, and personal loans and lines of credit. The bank serves as an agent in providing credit card loans. It acts as trustee of personal trusts, as executor of estates, as trustee for employee benefit trusts and as registrar, transfer agent and paying agent for bond issues.

Farmers Bank conducts business at its principal office and four branches in Frankfort, the capital of Kentucky, as well as two branches in Anderson County, and one branch each in Mercer and Boyle Counties. It is the largest bank operating in both Franklin and Anderson Counties based on total bank deposits. The market served by Farmers Bank is diverse, and includes government, commerce, finance, industry, medicine, education, and agriculture. The bank serves many individuals and corporations throughout Central Kentucky. On December 31, 2014, it had total consolidated assets of $687 million, including loans net of unearned income of $313 million. On the same date, total deposits were $555 million and shareholders' equity totaled $68.7 million.

Farmers Bank had six active direct subsidiaries at year-end 2014: Farmers Bank Realty Co. ("Farmers Realty"), Leasing One Corporation ("Leasing One"), Farmers Capital Insurance Corporation (“Farmers Insurance”), EG Properties, Inc. (“EG Properties”), Austin Park Apartments, LTD (“Austin Park”), and Frankfort Apartments II, LTD (“Frankfort Apartments”).

Farmers Realty was incorporated in 1978 for the purpose of owning certain real estate used by the Company and Farmers Bank in the ordinary course of business. Farmers Realty had total assets of $3.5 million on December 31, 2014.

Leasing One was incorporated in August 1993 to operate as a commercial equipment leasing company. At year-end 2014, it had total assets of $6.5 million, including leases net of unearned income of $145 thousand. During 2010, the board of directors of Leasing One reduced the staff and curtailed new lending. Servicing existing leases and terming out residuals are the extent of its ongoing activity at the present time.

Farmers Insurance was organized in 1988 to engage in insurance activities permitted to the Company under federal and state law. Farmers Bank capitalized this corporation in December 1998. Farmers Insurance acts as an agent for an otherwise unrelated title insurance company and offers title insurance coverage on property financed by the Company. At year-end 2014, it had total assets of $514 thousand. During 2014, Farmers Insurance liquidated its previously held 50% interest in Farmers Fidelity Insurance Agency, LLP (“Farmers Fidelity”). The Creech & Stafford Insurance Agency, Inc., an otherwise unrelated party to the Company, held the other 50% interest in Farmers Fidelity. Farmers

Fidelity was a direct writer of property and casualty coverage, both individual and commercial.

In November 2002, Farmers Bank incorporated EG Properties. EG Properties is involved in real estate management and liquidation for certain properties repossessed by Farmers Bank. EG Properties holds a 93.4% interest in WCO, LLC (“WCO”), which was formed during 2012 to hold certain real estate repossessed by Farmers Bank and United Bank. EG Properties had total assets of $17.5 million at year-end 2014.

FORE Realty, LLC was organized in December 2009 for the purpose of managing and liquidating certain properties repossessed by Farmers Bank. This entity was dissolved effective December 31, 2014.

Farmers Bank is a limited partner in Austin Park and Frankfort Apartments, two low income housing tax credit partnerships located in Frankfort, Kentucky. These investments provided federal income tax credits to the Company over a 10 year period and have been fully exhausted; however, the Company maintained its investment in these partnerships over a 15 year compliance period in order to avoid possible recapture of the tax credits. The compliance period has since ended and Farmers Bank is in the process of liquidating its investments in these partnerships. In December 2009, Farmers Bank became a limited partner in St. Clair Properties, LLC (“St. Clair Properties”). The objective of St. Clair Properties is to restore and preserve certain qualifying historic structures in Frankfort for which the Company received federal and state tax credits. Farmers Bank liquidated its interest in St. Clair Properties during December 2014. Farmers Bank’s cumulative share of losses from Austin Park and Frankfort Apartments at year-end 2014 exceeded the amount invested, reducing its carrying value of the partnerships to zero.

United Bank

On February 15, 1985, the Company acquired United Bank, a state chartered bank originally organized in 1880. It is engaged in a general banking business providing full service banking to individuals, businesses and governmental customers. United Bank conducts business in its principal office and two branches in Woodford County, Kentucky, four branches in Scott County, two branches in Fayette County, and four branches in Jessamine County. Based on total bank deposits, United Bank is the largest bank operating in both Woodford and Scott Counties, and ranks as the second largest bank in Jessamine County. On December 31, 2014, United Bank had total consolidated assets of $524 million, including loans net of unearned income of $277 million. On the same date, total deposits were $390 million and shareholders' equity was $63.5 million.

United Bank has one direct subsidiary, EGT Properties, Inc. ("EGT Properties"). EGT Properties was created in March 2008 and is involved in real estate management and liquidation for certain repossessed properties of United Bank. EGT Properties holds a 6.6% interest in WCO and an 83% interest in NUBT Properties, LLC ("NUBT"), the parent company of Flowing Creek Realty, LLC ("Flowing Creek"). Flowing Creek holds certain real estate repossessed by United Bank and Citizens Northern along with parties unrelated to the Company. NUBT holds a 67% interest in Flowing Creek and unrelated financial institutions hold the remaining 33% interest. EGT Properties had total assets of $22.4 million at year-end 2014.

First Citizens

On March 31, 1986, the Company acquired First Citizens, a state chartered bank originally organized in 1964. It is engaged in a general banking business providing full service banking to individuals, businesses and governmental customers. It conducts business at its main office and three branches in Hardin County, Kentucky along with two branch offices in Bullitt County. First Citizens incorporated HBJ Properties, LLC ("HBJ Properties") during 2012 to hold, manage, and liquidate certain properties repossessed by First Citizens. HBJ Properties had total assets of $4.5 million at year-end 2014.

First Citizens also provides bill payment services under the name of FirstNet. This service specializes in the processing of federal benefit and military allotment processing. First Citizens provides payment services to companies which provide products and services to both military individuals and beneficiaries of Federal benefits.

Based on total bank deposits in Hardin County, First Citizens is the third largest bank operating in Hardin County. On December 31, 2014, First Citizens had total consolidated assets of $312 million, including loans net of unearned income of $192 million. On the same date, total deposits were $269 million and shareholders' equity was $29.8 million.

Citizens Northern

On December 6, 2005, the Company acquired Citizens Bancorp in Newport, Kentucky. Citizens Bancorp was subsequently merged into Citizens Acquisition, a former bank holding company subsidiary of the Company. During January 2007, Citizens Acquisition was merged into the Company, leaving Citizens Northern as a direct subsidiary of the Parent Company. Citizens Northern is a state chartered bank organized in 1993 and is engaged in a general banking business providing full service banking to individuals, businesses, and governmental customers. It conducts business in its principal office in Newport and four branches in Campbell County, Kentucky, one branch in Boone County and two branches in Kenton County. Based on total bank deposits, Citizens Northern ranks as the second largest bank operating in Campbell County. At year-end 2014, Citizens Northern had total consolidated assets of $255 million, including loans net of unearned income of $149 million. On the same date, total deposits were $209 million and shareholders' equity was $25.2 million.

In March 2008, Citizens Northern incorporated ENKY Properties, Inc. ("ENKY"). ENKY was established to manage and liquidate certain real estate properties repossessed by Citizens Northern. ENKY also holds a 17% interest in NUBT, the parent company of Flowing Creek. Flowing Creek holds real estate repossessed by Citizens Northern and United Bank along with parties unrelated to the Company. NUBT holds a 67% interest in Flowing Creek and unrelated financial institutions hold the remaining 33% interest. ENKY had total assets of $5.1 million at year-end 2014.

Nonbank Subsidiaries

FCB Services was organized in 1992 and provides data processing services and support for the Company and its subsidiaries. It is located in Frankfort, Kentucky. It also provides data processing services for nonaffiliated entities. FCB Services had total assets of $3.8 million at December 31, 2014.

FFKT Insurance was incorporated during 2005. It is a captive property and casualty insurance company insuring primarily deductible exposures and uncovered liability related to properties of the Company. FFKT Insurance had total assets of $2.9 million at December 31, 2014.

Trust I, Trust II, and Trust III are each separate Delaware statutory business trusts sponsored by the Company. The Company completed two private offerings of trust preferred securities during 2005 through Trust I and Trust II totaling $25.0 million. During 2007, the Company completed a private offering of trust preferred securities through Trust III totaling $22.5 million. The Company owns all of the common securities of each of the Trusts. The Company does not consolidate the Trusts into its financial statements consistent with applicable accounting standards.

EKT was created in September 2008 to manage and liquidate certain real estate properties repossessed by the Company's subsidiary banks. EKT was dissolved effective December 31, 2014.

Lending Summary

A significant part of the Company's operating activities include originating loans, approximately 89% of which are secured by real estate at December 31, 2014. Real estate lending primarily includes loans secured by owner and non-owner occupied one-to-four family residential properties as well as commercial real estate mortgage loans to developers and owners of other commercial real estate. Real estate lending primarily includes both variable and adjustable rate products. Loan rates on variable rate loans generally adjust upward or downward immediately based on changes in the loan's index, normally prime rate as published by the Wall Street Journal. Rates on adjustable rate loans move upward or downward after an initial fixed term of normally one, three, or five years. Rate adjustments on adjustable rate loans are made annually after the initial fixed term expires and are indexed mainly to shorter-term Treasury indexes. Generally, variable and adjustable rate loans contain provisions that cap the amount of interest rate increases of up to 600 basis points and rate decreases of up to 100 basis points over the life of the loan. In recent years, it has been increasingly common for the Company to set a floor equal to the initial rate without further downward adjustments. In addition to the lifetime caps and floors on rate adjustments, loans secured by residential real estate typically contain provisions that limit annual increases at a maximum of 100 basis points. There is typically no annual limit applied to loans secured by commercial real estate.

The Company also makes fixed rate commercial real estate loans to a lesser extent with repayment periods generally ranging from three to five years. The Company's subsidiary banks make first and second residential mortgage loans secured by real estate not to exceed 90% loan to value without seeking third party guarantees. Commercial real estate loans are made primarily to small and mid-sized businesses, secured by real estate not exceeding 80% loan to value. Other commercial loans are asset based loans secured by equipment and lines of credit secured by receivables and include lending across a diverse range of business types.

Commercial lending and real estate construction lending, including commercial leasing, generally includes a higher degree of credit risk than other loans, such as residential mortgage loans. Commercial loans, like other loans, are evaluated at the time of approval to determine the adequacy of repayment sources and collateral requirements. Collateral requirements vary to some degree among borrowers and depend on the borrower's financial strength, the terms and amount of the loan, and collateral available to secure the loan. Credit risk results from the decreased ability or willingness to pay by a borrower. Credit risk also results when a liquidation of collateral occurs and there is a shortfall in collateral value as compared to a loan's outstanding balance. For construction loans, inaccurate initial estimates of a project's costs or the property's completed value could weaken the Company's position and lead to the property having a value that is insufficient to satisfy full payment of the amount of funds advanced for the property. Secured and unsecured direct consumer lending generally is made for automobiles, boats, and other motor vehicles. The Company does not presently engage in indirect consumer lending. Credit card lending is limited to one bank subsidiary and is considered nominal risk exposure due to extremely low volume. In most cases loans are restricted to the subsidiaries' general market area.

Loan Policy

The Company has a company-wide lending policy in place that is amended and approved from time to time as needed to reflect current economic conditions, law and regulatory changes, and product offerings in its markets. The policy has established minimum standards that each of its bank subsidiaries must adopt. Additionally, the policy is subject to amendment based on positive and negative trends observed within the lending portfolio as a whole. For example, the loan to value limits and amortization terms contained within the policy were reduced during 2009 due to the declining economy and related real estate market decline. While new appraisals now reflect that decline, appraisal reviews and downward adjustments are a continuing area of focus to reduce credit risk. The lending policy is evaluated for underwriting criteria by the Company's internal audit department in its loan review capacity as well as by the Company's Chief Credit Officer and its regulatory authorities. Suggested revisions from these groups are taken into account, analyzed, and implemented by management where improvements are warranted.

The Company's subsidiary banks may amend their lending policy so long as the amendment is no less stringent than the company-wide lending policy. These amendments are done within the control structure and oversight of the parent company. The Company's control structure includes a Chief Credit Officer. This position oversees all lending at affiliate institutions where the size and risk of individual credits are deemed significant to the Company. The Chief Credit Officer also monitors trends in asset quality, portfolio composition, concentrations of credit, reports of examinations, internal audit reports, work-out strategies for large credits, and other responsibilities as matters evolve.

The Company's Chief Credit Officer analyzes all loans in excess of $2.5 million prior to it being presented to the board of directors of the originating affiliate bank. All new loans, regardless of the amount, to an existing credit relationship in excess of $2.5 million are also analyzed by the Chief Credit Officer prior to being presented to the board of directors of the affiliate for consideration. The Chief Credit Officer reviews all loans to insiders for adherence to underwriting standards and regulatory compliance as well as credits identified as substandard.

Procedures

The lending policy lists the products and credit services offered by each of the Company's subsidiary banks. Each product and service has an established written procedure to adhere to when transacting business with a customer. The lending policy also establishes pre-determined lending authorities for loan officers commensurate with their abilities and experience. Further, the policy establishes committees to review and approve or deny credit requests at various lending amounts. This includes subcommittees of the bank boards of directors and, at certain lending levels, the entire bank board.

Generally, for loans in excess of $2.5 million, the subsidiaries bank's full board of directors will be presented with the loan request. This only occurs when the potential credit has first been recommended by the loan officer and chief credit officer of the subsidiary bank, and then by the directors' loan committee and the Chief Credit Officer. When loan requests are within policy guidelines and the amount requested is within their lending authority, lenders are permitted to approve and close the transaction. A review of the loan file and documentation takes place within 30 days to ensure policy and procedures are being followed. Approval authorities are under regular review for adjustment by affiliate management and the Parent Company. Loan requests outside of standard policy may be made on a case by case basis when justified, documented, and approved by either the board of directors of the subsidiary bank, committee, or other authorized person as determined by the size of the transaction. Procedures are in place which require ongoing monitoring subsequent to loan approval. For example, updated financial statements are required periodically for certain types of credits and risk ratings are re-evaluated at least annually for credit relationships in excess of $500 thousand, which includes analyzing updated cash flows and loan to value ratios. Annual site visits are made for credit relationships of $1.0 million or above.

Underwriting

Underwriting criteria for all types of loans are prescribed within the lending policy.

Residential Real Estate

Residential real estate mortgage lending made up 39% of the loan portfolio at year-end 2014. Underwriting criteria and procedures for residential real estate mortgage loans include:

- Monthly debt payments of the borrower to gross monthly income should not exceed 45% with stable employment;
- Interest rate shocks are applied for variable rate loans to determine repayment capabilities at elevated rates;
- Loan to value limits of up to 90%. Loan to value ratios exceeding 90% require additional third party guarantees;
- A thorough credit investigation using the three nationally available credit repositories;
- Incomes and employment is verified;
- Insurance is required in an amount to fully replace the improvements with the lending bank named as loss payee/mortgagee;
- Flood certifications are procured to ensure the improvements are not in a flood plain or are insured if they are within the flood plain boundaries;
- Collateral is investigated using current appraisals and is supplemented by the loan officer's knowledge of the locale and salient factors of the local market. Only appraisers which are state certified or licensed and on the banks' approved list are utilized to perform this service;
- Title attorneys and closing agents are required to maintain malpractice liability insurance and be on the banks approved list;
- Secondary market mortgages must meet the underwriting criteria of the purchasers, which is generally the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation;
- Adjustable rate owner occupied home loans are tied to market based rates such as are published by the Federal Reserve Board ("Federal Reserve" or "FRB"), commonly the one year constant maturity Treasury bill is used; and
- Residential real estate mortgage loans are made for terms not to exceed 30 years.

The Company strives to offer qualified mortgages as defined by the Consumer Financial Protection Bureau. However, the Company will also allow non-qualified mortgages with the review and approval of the Company's Chief Credit Officer or Chief Executive Officer of the affiliate bank. The qualified mortgage rule applies to home loans and is designed to ensure that borrowers can afford to repay loans by prohibiting or limiting certain high risk products and features such as charging excessive upfront points and fees, prohibiting interest-only loans, negative amortizing loans, loans exceeding repayment terms of 30 years, and, in most cases, balloon loans. Qualified mortgages also limit the borrower's debt to income ratio to 43%.

Commercial Real Estate

Commercial real estate lending made up 40% of the loan portfolio at year-end 2014. Commercial real estate lending underwriting criteria is documented in the lending policy and includes loans secured by office buildings, retail stores, warehouses, hotels, and other commercial properties. Underwriting criteria and procedures for commercial real estate loans include:

Procurement of Federal income tax returns and financial statements for the past three years and related supplemental information deemed relevant;
Detailed financial and credit analysis is performed and presented to various committees;
Cash investment from the applicant in an amount equal to 20% of cost (loan to value ratio not to exceed 80%). Additional collateral may be taken in lieu of a full 20% investment in limited circumstances;
Cash flows from the project financed and global cash flow of the principals and their entities must produce a minimum debt coverage ratio of 1.25:1;
For non-profits, including churches, a 1.0:1 debt coverage minimum ratio;
Past experience of the customer with the bank;
Experience of the investor in commercial real estate;
Tangible net worth analysis;
Interest rate shocks for variable rate loans;
General and local commercial real estate conditions;
Alternative uses of the security in the event of a default;
Thorough analysis of appraisals;
References and resumes are procured for background knowledge of the principals/guarantors;
Credit enhancements are utilized when necessary and/or desirable such as assignments of life insurance and the use of guarantors and firm take-out commitments;
Frequent financial reporting is required for income generating real estate such as: rent rolls, tenant listings, average daily rates and occupancy rates for hotels;
Commercial real estate loans are made with amortization terms not to exceed 20 years; and
For lending arrangements determined to be more complex, loan agreements with financial and collateral representations and warranties are employed to ensure the ongoing viability of the borrower.

Real Estate Construction

The Company's real estate construction lending has declined over the last several years due to related economic conditions. Where the Company's markets continue to demonstrate demand, construction lending continues with close monitoring of the borrower and the local economy. At year-end 2014, real estate construction lending comprised approximately 10% of the total loan portfolio.

Real estate construction lending underwriting criteria is documented in the lending policy and includes loans to individuals for home construction, loans to businesses primarily for the construction of owner-occupied commercial real estate, and for land development activities. Underwriting criteria and procedures for such lending include:

- 20% capital injection from the applicant (loan to value ratio not to exceed 80%);
- 25% capital injection for land acquisition for development (loan to value ratio not to exceed 75%);
- Pre-sell, pre-lease, and take-out commitments are procured and evaluated/verified;
- Draw requests require documentation of expenses;
- On site progress inspections are completed to protect the lending bank affiliate;
- Control procedures are in place to minimize risk on construction projects such as conducting lien searches and requiring affidavits;
- Lender on site visits and periodic financial discussions with owners/operators; and
- Real estate construction loans are made for terms not to exceed 12 months and 18 months for residential and commercial purposes, respectively.

Commercial, Financial, and Agriculture

Commercial, financial, and agriculture lending underwriting criteria is documented in the lending policy and includes loans to small and medium sized businesses secured by business assets, loans to financial institutions, and loans to farmers and for the production of agriculture. At year-end 2014, these loans made up approximately 9% of the total loan portfolio. Underwriting criteria and procedures for such loans are detailed below.

For commercial loans secured by business assets, the following loan to value ratios and debt coverage are required by policy:

- Inventory 50%;
- Accounts receivable less than 90 days past due 75%;
- Furniture, fixtures, and equipment 60%;
- Borrowing-base certificates are required for monitoring asset based loans;
- Stocks, bonds, and mutual funds are often pledged by business owners. Marketability and volatility is taken into account when valuing these types of collateral and lending is generally limited to 60% of their value;

Debt coverage ratios from cash flows must meet the policy minimum of 1.25:1. This coverage applies to global cash flow and guarantors, if any; and

Commercial loans secured by business assets are made for terms to match the economic useful lives of the asset securing the loan. Loans secured by furniture, fixtures, and equipment are made for terms not to exceed seven years. Lien searches are performed to ensure lien priority for credits exceeding certain thresholds.

Loans to financial institutions are generally secured by the capital stock of the financial institution with a loan to value ratio not to exceed 60% and repayment terms not exceeding 10 years. Capital stock values of non-public companies are determined by common metrics such as a multiple of tangible book value or by obtaining third party estimates. Financial covenants are also obtained that require the borrower to maintain certain levels of asset quality, capital adequacy, liquidity, profitability, and regulatory compliance. At year-end 2014, loans to financial institutions were zero.

Agricultural lending, such as for tobacco or corn, is limited to 75% of expected sales proceeds while lending for cattle and farm equipment is capped at 80% loan to value.

Interest Only Loans

Interest only loans are limited to construction lending and properties recently completed and undergoing an occupancy stabilization period. These loans are short-term in nature, usually with maturities of less than one year.

Installment Loans

Installment lending is a small component of the Company's portfolio mix, reflecting approximately 1% of outstanding loans at year-end 2014. These loans predominantly are direct loans to established bank customers and primarily include the financing of automobiles, boats, and other consumer goods. The character, capacity, collateral, and conditions are evaluated using policy restraints. Installment loans are made for terms of up to five years.

Installment lending underwriting criteria and procedures for such financing include:

- Required financial statement of the applicant for loans in excess of $20,000;
- Past experience of the customer with the bank and other creditors of the applicant;
- Monthly debt payments of the borrower to gross monthly income should not exceed 45% with stable employment;
- Secured and unsecured loans are made with a definite repayment plan which coincides with the purpose of the loan;
- Borrower's unsecured debt must not exceed 25% of the borrower's net worth; and
- Verification of borrower's credit and income.

Lease Financing

Lease financing is an insignificant component of the Company's portfolio, representing less than 1% of outstanding loans at year-end 2014. The board of directors of the Company's Leasing One subsidiary has reduced the staff and curtailed new leasing transactions for the foreseeable future. Servicing existing leases and terming out residuals are the extent of its ongoing activity at the present time.

Lease financing underwriting criteria is documented by policy. Underwriting criteria and procedures for such financing include:

- Lessee must be a commercial entity;
- Lessee must be in business for a minimum of two years;
- Leased equipment must be of essential use to lessee's business;
- Residual positions taken will not exceed 20% of original equipment cost;
- Leasing terms generally not to exceed five years; used equipment and computers not to exceed three years;
- Personal and/or corporate financial statements or tax returns required for all financing requests. Submission of updated financial statements annually;
- Credit reports must be clear of judgments and bankruptcies and chronic delinquency paying habits; and
- Bank and trade references must report satisfactory references.

Hybrid Loans

The Company and its subsidiary banks have a policy of not underwriting, originating, selling or holding hybrid loans. The Company does not currently hold hybrid loans. Hybrid loans include payment option adjustable rate mortgages, negative amortization loans, and stated income/stated asset loans.

Appraisals

The values of real estate in the Company's markets have largely stabilized in 2014, but overall levels have generally declined since the economic downturn which accelerated in 2008. The level of net loan charge-offs have decreased in the last several years compared to the spikes which occurred between 2009 to 2011. These spikes were driven mainly by slower sales and excess inventory related to loans secured by real estate. The slower sales and excess inventory decreased the cash flow and financial prospects of many borrowers, particularly those in the real estate development and related industries, and reduced the estimated fair value of the collateral securing these loans.

The Company uses independent third party state certified or licensed appraisers. These appraisers take into account local market conditions when preparing their estimate of a property's fair value. The Company evaluates appraisals it receives from independent third parties subsequent to the appraisal date by monitoring transactions in its markets and comparing them to its other projects that are similar in nature. The Company's internal audit department reviews appraisals on a test basis to determine that assumptions used in appraisals remain valid and are not stale. New appraisals are obtained if market conditions significantly impact collateral values for those loans that are identified as impaired. Internal audit reviews appraisals related to all of the Company's impaired loans and repossessed properties at least annually.

The Company considers appraisals it receives on one property as a means to extrapolate the estimated value for other collateral of similar characteristics if that property may not otherwise have a need for an appraisal. Should a borrower's financial condition continue to deteriorate, an updated appraisal on that specific collateral will be obtained.

Appraisals obtained for construction and development lending purposes are performed by state licensed or state certified appraisers who are credentialed and on the Company's approved list. Plans and specifications are provided to the appraiser by bank personnel not directly involved in the credit approval process. The appraisals conform to the standards of appraisal practices established by the Appraisal Standards Board in effect at the time of the appraisal. This includes net present value accounting for construction and development loans on an "as completed" and "as is" basis.

Appraisal reviews are conducted internally by bank personnel familiar with the local market and who are not directly involved in the credit approval process and externally by state licensed and certified appraisers. Bank personnel do not increase the valuation from the appraisal but may, in some instances, make a reduction. Upon completion, a follow up site visit by the appraiser is completed to verify the property was improved in accordance with the original plans and specifications and recertify, if appropriate, the original estimate of “as completed” market value. Circumstances where management may make adjustments to appraisals include the following:

As discussed above, construction and development appraisals are on an “as completed” basis. If work remains to be completed on a financed project, management will reduce the estimated value in the appraisal by the estimated cost to complete the work and, if required by the loan balance, establish reserves allocated to the loan or write down the loan based on the need to complete such work.

If an appraisal for given collateral is still valid (e.g. less than one year old, etc.), but due to market conditions and the bank’s familiarity with comparable property sales in the market the appraised value appears high, management may adjust downward from the last appraisal its estimate of the value of the collateral and, in turn, establish reserves allocated to the loan or write down the loan to reflect this downward adjustment.

Certain appraisals, such as for subdivision development and for other projects expected to take over one year to liquidate, are required to include estimated costs to sell. For others, management adjusts the appraised value by the estimated selling costs when they are either absent or not required. Additional reserves or direct write downs are made to the loan to reflect these adjustments.

Loan to value ratios are typically well under 100% at inception, which gives the Company a cushion as collateral values fall. However, when updated appraisals reveal collateral exposure (i.e. the value of the collateral for a nonperforming loan is less than originally estimated and no longer supports the outstanding loan amount), negotiations ensue with the borrower aimed at providing additional collateral support for the credit. This may be in many forms as determined by the financial holdings of the borrower. If not available, third party support for the credit is pursued (e.g., guarantors or equity investors). If negotiations fail to provide additional adequate collateral support, reserves are allocated to the loan or the loan is written down to the fair value of the collateral less the estimated costs to sell.

When a construction loan or development loan is downgraded, a new appraisal is ordered contemporaneously with the downgrade. The appraisers are instructed to give a fair value based upon both an “as is” basis and an “as completed” basis. The twofold purpose is to facilitate management’s decision making process in determining the cost benefits of completing a project compared with marketing the project as is.

The carrying value of a downgraded loan or nonperforming asset wherein the underlying collateral is an incomplete project is based on an updated appraisal at the “as is” value. The current appraisal is a compilation of the most recent sales available and therefore includes the risk premium established by market conditions. When comparable sales are not deemed to be reliable or the adjustments are not satisfactory, management will make appropriate adjustments to the fair value which includes a risk premium (discount) deducted using the discounted cash flow framework. The reserve or write down is expended upon completion of the appraisal and other relevant information assessment.

Interest Reserves

Interest reserves represent funds loaned to a borrower for the payment of interest during the development phase on certain construction and development loans. Interest reserves were a common industry practice when banks were more actively lending and the predictability of a sale or stabilization of the project had a high probability. The interest reserve is a component of the loan proceeds which is determined at the loan’s inception after a full evaluation of the sources and uses of funds for the project, and is intended to match the project’s debt service requirements with its expected cash flows. In all construction lending projects, the Company monitors the project to determine if it is being completed as planned and if sales/stabilization projections are being met.

For present and future construction and development loan requests, borrowers must show sufficient cash reserves and significant excess cash flow from all sources in addition to other underwriting criteria measures. A project’s viability is a major consideration as well, along with the probability of its stabilization and/or sale. Due to the general lack of risk-appropriate opportunities currently in our markets combined with our low desire for this segment of the lending portfolio, interest reserves are not commonplace.

Supervision and Regulation

The Company and its subsidiaries are subject to comprehensive supervision and regulation that affect virtually all aspects of their operations. The laws and regulations are primarily intended for the protection of depositors, borrowers, and federal deposit insurance funds, and, to a lesser extent, for the protection of stockholders and creditors. Changes in applicable laws, regulations, or in the policies of banking and other government regulators may have a material adverse effect on our current or future business. The following discussion is a summary of certain of the more important aspects of the relevant statutory and regulatory provisions and does not purport to be complete nor does it address all applicable statutes and regulations.

Supervisory Authorities

The Company is a bank holding company, registered with and regulated by the Federal Reserve. All four of its subsidiary banks are Kentucky state-chartered banks. Two of the Company's subsidiary banks are members of their regional Federal Reserve Bank. The Company and its subsidiary banks are subject to supervision, regulation, and examination by the Federal Reserve, Federal Deposit Insurance Corporation ("FDIC"), and the Kentucky Department of Financial Institutions ("KDFI"). The Company and its subsidiary banks are required to file regular reports with the FRB, the FDIC, and the KDFI. The regulatory authorities routinely examine the Company and its subsidiary banks to monitor compliance with laws and regulations, financial condition, adequacy of capital and reserves, quality and documentation of loans, payment of dividends, adequacy of systems and controls, credit underwriting, asset liability management, and the establishment of branches.

The Company is also subject to disclosure and other regulatory requirements of the Securities Act of 1933 and the Securities Exchange Act of 1934 (as amended), as administered by the Securities and Exchange Commission. Regulatory authorities may initiate enforcement proceeding against the Company for violations of laws or regulations, or for engaging in unsafe and unsound practices. Enforcement powers available to the regulatory agencies include the ability to assess civil monetary penalties, issuing cease and desist and similar orders, and initiating injunctive actions.

Capital

The FRB, the FDIC, and the KDFI require the Company and its subsidiary banks to meet certain ratios of capital to assets in order to conduct their activities. To be well-capitalized under current rules, the institutions must generally maintain a Total Risk-based Capital ratio of 10% or greater, a Tier 1 Risk-based Capital ratio of 6% or greater, and a Tier 1 Leverage ratio of 5% or more. For the purposes of these tests, Tier 1 Capital consists of common equity and related surplus, retained earnings, and a limited amount of qualifying preferred stock, less goodwill (net of certain deferred tax liabilities) and certain core deposit intangibles. Tier 2 Capital consists of non-qualifying preferred stock, certain types of debt and a limited amount of other items. Total Capital is the sum of Tier 1 and Tier 2 Capital.

In measuring the adequacy of capital, assets are generally weighted for risk. Certain assets, such as cash and U.S. government securities, have a risk weighting of zero. Others, such as commercial and consumer loans, are risk weighted at 100%. Risk weightings are also assigned for off-balance sheet items such as loan commitments. The various items are multiplied by the appropriate risk-weighting to determine risk-adjusted assets for the capital calculations. For the leverage ratio mentioned above, average quarterly assets (as defined) are used and are not risk-weighted.

If an institution fails to remain well-capitalized, it will be subject to a series of restrictions that increase as the capital condition worsens. For instance, federal law generally prohibits a depository institution from making any capital distribution, including the payment of a dividend or paying any management fee to its holding company, if the depository institution would be undercapitalized as a result. Undercapitalized depository institutions may not accept brokered deposits absent a waiver from the FDIC, are subject to growth limitations, and are required to submit a capital restoration plan for approval, which must be guaranteed by the institution's parent holding company. Significantly undercapitalized depository institutions may be subject to a number of requirements and restrictions, including orders to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets, and cessation of receipt of deposits from correspondent banks. Critically undercapitalized institutions are subject to the appointment of a receiver or conservator.

In December 2010, the Basel Committee on Banking Supervision issued final rules related to global regulatory standards on bank capital adequacy and liquidity (commonly referred to as "Basel III") previously agreed on by the Group of Governors and Heads of Supervision (the oversight body of the Basel Committee). U.S. federal banking agencies adopted final rules during 2013 to bring U.S. banking organizations into compliance with Basel III. Under the new rules, which are effective in 2015, the Company will be subject to new capital requirements that include: (i) creation of a new required ratio for common equity Tier 1 ("CET1") capital, (ii) an increase to the minimum Tier 1 capital ratio, (iii) changes to risk-weightings of certain assets for purposes of the risk-based capital ratios, (iv) creation of an additional capital conservation buffer in excess of the required minimum capital ratios, and (v) changes to what qualifies as capital for purposes of meeting these capital requirements. Under the new rules, the Company will be required to maintain additional levels of Tier 1 common equity over the minimum risk-based capital levels before it may pay dividends or pay discretionary bonuses.

Under Basel III, the Company will be required to maintain a minimum CET1 ratio of 4.5% of risk-weighted assets. CET1 consists of common stock, related surplus, and retained earnings less certain deductions that primarily include goodwill, other intangible assets, and deferred tax assets. These deductions to CET1 will be phased-in over a four-year period beginning at 40% on January 1, 2015 and an additional 20% per year thereafter. The minimum Tier 1 capital ratio will increase to 6% from 4%, while the total capital ratio and leverage ratio remains unchanged at 8% and 4%, respectively. Changes to risk-weighted assets include: i) 150% risk weighting for non-residential mortgage loans past due more than 90 days or classified as nonaccrual; ii) 150% risk weighting (from 100%) for certain high volatility commercial real estate acquisition, development, and construction loans; iii) a 20% (from 0%) credit conversion factor for the unused portion of commitments with an original maturity of one year or less (except those unconditionally cancellable by the Company); and, iv) a 250% (from 100%) risk weighting for mortgage servicing and deferred tax assets that are not deducted from CET1.

In order to avoid restrictions on distributions, including dividend payments and discretionary bonus payments to its executives, the Company will be required to maintain a capital conservation buffer of an additional 2.5% of risk-weighted assets once fully phased in. The capital conservation buffer is designed to create incentives for banking organizations to conserve capital during periods of economic stress. The addition of the capital conservation buffer effectively results in minimum ratios of 7%, 8.5%, and 10.5% for CET1, Tier 1 capital, and total capital, respectively, in order to avoid restrictions on distributions and discretionary bonus payments to executives. The capital conservation buffer is set to be phased in over a four year period beginning in 2016 by increments of 0.625% annually until reaching 2.5%.

The new capital requirements include changes to how regulatory capital is defined for purposes of calculating each of the capital ratios. Under current capital standards, the effects of accumulated other comprehensive income items included in capital (primarily unrealized gains and losses on available for sale investment securities) are excluded for the purposes of determining regulatory capital ratios. Under the new capital rules, the effects of certain accumulated other comprehensive income items are not excluded; however, non-advanced approaches banking organizations, including the Company, can make a one-time permanent election to continue excluding these items comparable to their current treatment. The Company expects to make this election in order to avoid potentially significant fluctuations in its capital levels which can occur from the impact of changing market interest rates on the fair value of the Company’s investment securities portfolio.

The new capital rules prohibit including certain hybrid and preferred securities in Tier 1 capital. However, the rules grandfather these non-qualifying capital instruments (subject to 25% of Tier 1 capital) of bank holding companies with total consolidated assets of less than $15 billion as of December 31, 2009. Non-qualifying capital instruments under the final rule include trust preferred securities and cumulative perpetual preferred stock issued before May 19, 2010, which are currently included in Tier 1 capital. As a result, beginning in 2015, the Company’s non-qualifying capital instruments will be subject to a limit of 25% of Tier 1 capital elements, excluding the non-qualifying capital instruments and after all regulatory capital deductions and adjustments applied to Tier 1 capital. Non-qualifying capital instruments excluded from Tier 1 capital under the 25% limitation may be included as a component of Tier 2 capital.

The Company has completed a pro forma analysis of its capital ratios under the new capital rules discussed above. Such analysis indicates the Company remains well-capitalized under the new rules, which require a CET1 ratio of 6.5%, a Tier 1 capital ratio of 8%, a total capital ratio of 10%, and a leverage ratio of 5%. The analysis also shows the Company meets the minimum capital ratios and a fully phased-in capital conservation buffer.

Expansion and Activity Limitations

With prior regulatory approval, the Company may acquire other banks or bank holding companies and its subsidiaries may merge with other banks. Acquisitions of banks located in other states may be subject to certain deposit-percentage, age, or other restrictions. The Company is restricted to those activities permissible under the Bank Holding Company Act, as amended. Under the Bank Holding Company Act, the Company is generally prohibited from engaging in or acquiring direct or indirect control of more than 5% of the voting shares of any company engaged in activities that are deemed not closely related to banking.

Limitations on Acquisitions of Bank Holding Companies

In general, other companies seeking to acquire control of a bank holding company such as the Company would require the approval of the FRB under the Bank Holding Company Act. In addition, individuals or groups of individuals seeking to acquire control of a bank holding company such as the Company would need to file a prior notice with the FRB (which the FRB may disapprove under certain circumstances) under the Change in Bank Control Act. Control is conclusively presumed to exist if an individual or company acquires 25% or more of any class of voting securities of the bank holding company. Control may exist under the Change in Bank Control Act if the individual or company acquires 10% or more of any class of voting securities of the bank holding company and no shareholder holds a larger percentage of the subject class of voting securities.

Deposit Insurance

Each of the Company's subsidiary banks are members of the FDIC, and their deposits are insured by the FDIC's Deposit Insurance Fund ("DIF") up to prescribed limits of $250 thousand per depositor. The Company's subsidiary banks are subject to quarterly FDIC deposit insurance assessments to maintain the DIF. The FDIC utilizes a risk-based assessment system that imposes insurance premiums based upon a risk matrix that takes into account a bank's capital level and supervisory rating.

The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") required changes to a number of components of the FDIC insurance assessment that was effective April 1, 2011. The Dodd-Frank Act required the FDIC to adopt a new DIF restoration plan to increases its reserve ratio to 1.35% from 1.15% of insured deposits by 2020. Under the restoration plan, the FDIC adopted regulations that redefined the assessment base as average consolidated assets less average tangible equity (as defined) during the assessment period. Since the new assessment base resulted in a larger overall base when compared to the previous domestic deposits base methodology, overall assessment rates were lowered and the secured liability adjustment was eliminated from the rate calculation in an attempt to make the new assessments revenue neutral. The new regulations retain the risk category system for depository institutions with less than $10 billion in assets. Under this system, each institution is assigned to one of four risk categories based upon the institution's capital and supervisory evaluation. At least semi-annually, the FDIC will update its loss and income projections for the DIF and, if needed, increase or decrease assessment rates. In establishing assessments, the FDIC is required to offset the effect of the higher reserve ratio against insured depository institutions with total consolidated assets of less than $10 billion.

To determine the Company's deposit insurance premiums, each of its subsidiary banks compute their respective assessment base, composed of average consolidated assets less average tangible equity (as defined), then applying the applicable assessment rate. Assessment rates range from 2.5 to 9 basis points for banks designated in the lowest risk category and up to 30 to 45 basis points for banks designated in the highest risk category. The range of assessment rates applicable to each risk category varies depending on the level of the banks unsecured debt and brokered deposits. Graduated assessment rate decreases are set to phase in when the DIF reserve ratio exceeds 1.15%, 2.0%, and 2.5%.

The FDIC may terminate insurance for depository institutions upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound financial condition, or has violated an applicable law, rule, regulation, order, or condition imposed by the FDIC.

In addition to deposit insurance assessments, all FDIC insured institutions are required to pay assessments to the FDIC to fund interest payments on bonds issued by the Financing Corporation ("FICO"), a mixed-ownership government corporation established by the Competitive Equality Banking Act of 1987 possessing assessment powers in addition to the FDIC. The FDIC acts as a collection agent for FICO, whose sole purpose was to function as a financing vehicle for the now defunct Federal Savings & Loan Insurance Corporation. FICO assessment rates are determined quarterly and will continue until the FICO bonds mature in 2017 through 2019.

Other Statutes and Regulations

The Company and its subsidiary banks are subject to numerous other statutes and regulations affecting their activities. Some of the more important are summarized below.

Anti-Money Laundering. Financial institutions are required to establish anti-money laundering programs that must include the development of internal policies, procedures, and controls; the designation of a compliance officer; an ongoing employee training program; and an independent audit function to test the performance of the programs. The Company and its subsidiary banks are also subject to prohibitions against specified financial transactions and account relationships as well as enhanced due diligence and "know your customer" standards in their dealings with foreign financial institutions and foreign customers. Financial institutions must take reasonable steps to conduct enhanced scrutiny of account relationships in order to guard against money laundering and to report any suspicious transactions. Recent laws provide law enforcement authorities with increased access to financial information maintained by banks.

Sections 23A and 23B of the Federal Reserve Act. The Company's subsidiary banks are limited in their ability to lend funds or engage in transactions with the Company or other nonbank affiliates of the Company, and all transactions must be on an arm's-length basis and on terms at least as favorable to the subsidiary bank as prevailing at the time for transactions with unaffiliated companies.

Dividends. The Parent Company's principal source of cash flow, including cash flow to pay dividends to its shareholders, is the dividends that it receives from its subsidiary banks. Statutory and regulatory limitations apply to the subsidiary banks' payments of dividends to the Parent Company as well as to the Parent Company's payment of dividends to its shareholders. A depository institution may not pay any dividend if payment would cause it to become undercapitalized or if it already is undercapitalized. The federal banking agencies may prevent the payment of a dividend if they determine that the payment would be an unsafe and unsound banking practice. Moreover, the federal agencies have issued policy statements that provide bank holding companies and insured banks should generally only pay dividends out of current operating earnings. Certain of the Company's bank subsidiaries are subject to regulatory orders that restrict the payment of dividends. For further information please refer to the caption "*Recent Regulatory Events and Increased Capital Requirements"* below.

The Company's outstanding Series A preferred stock was issued during the first quarter of 2009 and includes restrictions on the Company's ability to pay dividends to its common shareholders. The Company is unable to declare dividend payments on shares of its common stock if it is in arrears on the dividends on its Series A preferred stock.

Community Reinvestment Act. The Company's subsidiary banks are subject to the provisions of the Community Reinvestment Act of 1977 ("CRA"), as amended, and the federal banking agencies' related regulations, stating that all banks have a continuing and affirmative obligation, consistent with safe and sound operations, to help meet the credit needs of the communities they serve. The CRA requires a depository institution's primary federal regulator, in connection with its examination of the institution or its evaluation of certain regulatory applications, to evaluate the institution's record in assessing and meeting the credit needs of the community served by that institution, including low and moderate-income neighborhoods. The regulatory agency's assessment of the institution's record is made available to the public. Failure of an institution to receive at least a "satisfactory" rating on a CRA examination could prevent a bank or its parent company from engaging in certain activities such as establishing de novo braches and branch relocations or acquiring other financial institutions.

Insurance Regulation. The Company's subsidiaries that may underwrite or sell insurance products are subject to regulation by the Kentucky Department of Insurance.

Consumer Regulation. The activities of the Company and its bank subsidiaries are subject to a variety of statutes and regulations designed to protect consumers. These laws and regulations:

- limit the interest and other charges collected or contracted for by all of the Company's subsidiary banks;
- govern disclosures of credit terms to consumer borrowers;
- require financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
- prohibit discrimination on the basis of race, creed, or other prohibited factors in extending credit;
- require all of the Company's subsidiary banks to safeguard the personal non-public information of its customers, provide annual notices to consumers regarding the usage and sharing of such information and limit disclosure of such information to third parties except under specific circumstances; and
- govern the manner in which consumer debts may be collected by collection agencies.

The deposit operations of the Company's subsidiary banks are also subject to laws and regulations that:

- require disclosure of the interest rate and other terms of consumer deposit accounts;
- impose a duty to maintain the confidentiality of consumer financial records and prescribe procedures for complying with administrative subpoenas of financial records; and
- govern automatic deposits to and withdrawals from deposit accounts and customers' rights and liabilities arising from the use of automated teller machines and other electronic banking services.

Emergency Economic Stabilization Act of 2008 ("EESA"). EESA was signed into law during 2008 as a measure to stabilize and provide liquidity to the U.S. financial markets. Under EESA, the Troubled Asset Relief Program ("TARP") was created. TARP granted the U.S. Treasury ("Treasury") authority to, among other things, invest in financial institutions and purchase troubled assets in an aggregate amount up to $700 billion.

In connection with TARP, the Capital Purchase Program ("CPP") was launched on October 14, 2008. Under the CPP, the Treasury announced a plan to use up to $250 billion of TARP funds to purchase equity stakes in certain eligible financial institutions, including the Company. The Company received $30.0 million of equity capital under the CPP in January 2009. In the transaction, the Company issued 30,000 shares of fixed-rate cumulative perpetual preferred stock to the Treasury. The terms of the preferred shares required the Company to pay a 5% cumulative dividend during the first five years the shares were outstanding, resetting to 9% thereafter, and includes certain restrictions on dividend payments of lower ranking equity. The Company repurchased 20,000 of its outstanding preferred shares during 2014 for $20.0 million.

During June 2012, the Treasury conducted an auction as part of ongoing efforts to wind down and recover its remaining CPP investments. The auction included preferred stock positions held by the Treasury of seven banks participating in the CPP, including the $30.0 million investment in the Company's Series A preferred stock. The Treasury was successful in selling all of its investment in the Company's Series A preferred stock to private investors through a registered public offering. The Company received no proceeds as part of the transaction. Since the Treasury no longer owns the preferred stock, the executive compensation and other restrictions put in place by the Treasury no longer apply.

As required by the CPP, the Company also issued a warrant to the Treasury to purchase common shares equal to 15% of the value of the preferred stock. The warrant allowed the Treasury to purchase 223,992 shares of Company common stock at an exercise price of $20.09 per share. In July 2012, the Company repurchased the warrant from the Treasury at a mutually agreed upon price of $75 thousand. The repurchase of the warrant had no impact on the Company's results of operations, although cash and shareholders' equity declined by the amount of the purchase price. Upon settlement of the warrant repurchase, the Treasury has no remaining equity stake in the Company.

Dodd-Frank Act. The Dodd-Frank Act was signed into law in July 2010. The Dodd-Frank Act implements far-reaching changes to the regulation of the financial services industry, including provisions that:

- centralize responsibility for consumer financial protection by creating the Consumer Financial Protection Bureau, a new agency responsible for implementing, examining, and enforcing compliance with federal consumer financial laws;
- apply the same leverage and risk-based capital requirements that apply to insured depository institutions to bank holding companies;
- require the federal banking regulators to seek to make their capital requirements countercyclical, so that capital requirements increase in times of economic expansion and decreases in times of economic contraction;
- change the assessment base for federal deposit insurance from the amount of insured deposits to consolidated assets less tangible capital;
- provide for new disclosure and other requirements relating to executive compensation and corporate governance;
- make permanent the $250 thousand limit for federal deposit insurance;
- repeal the federal prohibitions on the payment of interest on commercial demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts;
- increase the authority of the Federal Reserve to examine non-bank subsidiaries; and
- codify and expand the "source of strength" doctrine as a statutory requirement. The source of strength doctrine represents the long held policy view by the Federal Reserve that a bank holding company should serve as a source of financial strength for its subsidiary banks. The Parent Company, under this requirement, is expected to commit resources to support a distressed subsidiary bank.

Volcker Rule. The Dodd-Frank Act prohibits insured depository institutions and their holding companies from engaging in proprietary trading except in limited circumstances, and prohibits certain ownership interests in and relationships with private equity and hedge funds (commonly referred to as the "Volcker Rule"). On December 10, 2013, U.S. financial regulators, including the Federal Reserve, adopted final rules to implement the Volcker Rule. The Final Rules were effective April 1, 2014, but the conformance period to bring activities and investments into compliance was extended to July 21, 2015. The Company currently does not have any impermissible holdings under the rule, and expects no material financial impact or changes to its operations as a result.

Recent Regulatory Events and Increased Capital Requirements

The Company's subsidiary banks are subject to capital-based regulatory requirements. The Company has historically managed its banks' capital levels with the goal of meeting the criteria established by its regulators to be "well-capitalized." Historically, to be well-capitalized, a depository institution needed to have a Tier 1 Leverage ratio of at least 5%, a Tier 1 Risk-based Capital ratio of 6%, and a Total Risk-based Capital ratio of 10%. As of December 31, 2014, each of the Company's four subsidiary banks satisfied these capital ratios.

Although each of the Company's subsidiary banks met the definition of well-capitalized as of December 31, 2014, some of their capital levels experienced decreases during the earlier years of the economic downturn that began in late 2007. Because of the turmoil in the banking markets and continued difficulty many banks were experiencing with their loan portfolios, bank regulatory agencies have increasingly required higher capital reserves as a cushion for dealing with deterioration in their loan portfolios. Primarily as a result of examinations that took place starting in 2009, the Company's banking regulators have required certain of its bank subsidiaries to increase their minimum capital ratios, which resulted in capital injections from the Parent Company. Capital requirements and other supervisory actions resulting from the regulatory examinations are summarized below. For a more complete discussion, please refer to the section captioned *"Capital Resources"* under Item 7 *"Management's Discussion and Analysis of Financial Condition and Result of Operations"* part of this Form 10-K.

Parent Company. Primarily due to the regulatory actions and capital requirements at certain of the Company's subsidiary banks as further discussed below, the Federal Reserve Bank of St. Louis ("FRB St. Louis") and the KDFI entered into a Memorandum of Understanding ("Memorandum") with the Parent Company during the fourth quarter of 2009. Pursuant to the Memorandum, the Company agreed that it would develop an acceptable capital plan to ensure that the consolidated organization remains well-capitalized and each of its subsidiary banks meet the capital requirements imposed by their regulator as summarized below. The 2009 Memorandum was terminated in March 2014 as a result of continued satisfactory compliance, most notably from the progress made in lowering nonperforming assets and increasing capital levels.

The Company is no longer required to receive permission from its banking regulators to make interest payments on its trust preferred securities or to pay dividends on its common and preferred stock. However, the Company's goal is to redeem all of its outstanding preferred stock before considering the payment of a dividend on its common stock. The Company redeemed a total of 20,000 shares, or two-thirds, of its outstanding preferred stock during 2014 in two separate partial redemptions of 10,000 shares each. The redemption amount was equal to the stated liquidation value of $1 thousand per share or $20.0 million in the aggregate, plus accrued dividends. The Company intends to redeem its remaining 10,000 shares of preferred stock in 2015, although this action requires approval by our banking regulators. The timing and amount of any further redemption by the Company of its remaining outstanding preferred stock will be disclosed when assured.

United Bank. In November of 2009, the FDIC and the KDFI entered into a Cease and Desist Order ("C&D") with United Bank primarily as a result of its level of nonperforming assets. The C&D was terminated in December 2011 coincident with the issuance of a Consent Order ("Consent Order") entered into between the parties. The Consent Order is substantially the same as the C&D, with the primary exception being that United Bank must achieve and maintain a Tier 1 Leverage ratio of 9.0% and a Total Risk-based Capital ratio of 13.0%. During the first quarter of 2012, the Parent Company injected from its reserves $2.5 million in capital into United Bank in order for it to comply with the Consent Order. During January 2014, the formal Consent Order entered into during 2011 with United Bank was terminated and replaced with a stepped-down enforcement action in the form of an informal Memorandum, which includes many of the same provisions covered by the Consent Order. At December 31, 2014, United Bank had a Tier 1 Leverage ratio of 11.08% and a Total Risk-based Capital ratio of 19.26%. The Parent Company injected from its reserves $18.9 million of capital into United Bank between the fourth quarter of 2009 and the first quarter of 2012.

Other components in the regulatory order with United Bank include oversight and reporting obligations to its regulators in terms of complying with the Memorandum. It also includes requirements in the level of reporting by management to its board of directors of its financial results, budgeting, and liquidity analysis, as well as restricting the bank from extending additional credit to borrowers with credits classified as substandard, doubtful or special mention in the report of examination. There is also a requirement to obtain written consent prior to declaring or paying a dividend and to develop a written contingency plan if the bank is unable to meet the capital levels established in the Memorandum.

The Company received written notification in March 2015 that the FDIC and KDFI, as a result of their recent examination, terminated the Memorandum that was entered into with United Bank effective immediately. In connection with the termination of the Memorandum, the Board of Directors of United Bank agreed to adopt a resolution which includes many of the same provisions as the Memorandum, including the requirement to seek approval from the FDIC and KDFI prior to the payment of dividends. However, the requirement for maintaining a minimum Tier 1 Leverage ratio of 9.0% and a Total Risk-based Capital ratio of 13.0% no longer applies.

Citizens Northern. The FDIC and the KDFI entered into a Memorandum with Citizens Northern in September of 2010. The Memorandum was terminated July 7, 2013 upon the issuance of an updated Memorandum. The updated Memorandum contains many of the same provisions included in the terminated Memorandum, with a new requirement that Citizens Northern maintain a Tier 1 leverage ratio at or above 9.0%. In addition, the updated Memorandum requires having and retaining qualified management in the areas of loan administration and collection. It also requires Citizens Northern to address credit underwriting and administration weaknesses identified in the most recent examination of the bank by the FDIC and the KDFI. At December 31, 2014, Citizens Northern had a Tier 1 Leverage ratio of 10.11% and a Total Risk-based Capital ratio of 15.71%.

Other parts of the regulatory order include the development and documentation of plans for reducing problem loans, providing progress reports on compliance with the Memorandum, and for the development and implementation of a written profit plan and strategic plans. It also restricts the bank from extending additional credit to borrowers with credits classified as substandard, doubtful or special mention in the report of examination.

Regulators continue to monitor the Company’s progress and compliance with the regulatory agreements through periodic on-site examinations, regular communications, and quarterly data analysis. The Company believes it is adequately addressing all issues of the regulatory agreements to which it is subject. However, only the respective regulatory agencies can determine if compliance with the applicable regulatory agreements has been met. The Company believes that its subsidiary banks are in compliance with the requirements identified in the regulatory agreements as of December 31, 2014.

The Parent Company maintains cash available to fund a certain amount of additional injections of capital to its bank subsidiaries as determined by management or if required by its regulators. If needed, further amounts in excess of available cash may be funded by future public or private sales of securities, although the Parent Company is currently under no directive by its regulators to raise any additional capital.

References under the caption "*Supervision and Regulation*" to applicable statutes and regulations are brief summaries of portions thereof which do not purport to be complete and which are qualified in their entirety by reference thereto.

Competition

The Company and its subsidiaries face vigorous competition for banking services from various types of businesses other than commercial banks and savings and loan associations. These include, but are not limited to, credit unions, mortgage lenders, finance companies, insurance companies, stock and bond brokers, financial planning firms, and department stores, which compete for one or more lines of banking business. The Company also competes for commercial and retail business not only with banks in Central and Northern Kentucky, but with banking organizations from Ohio, Indiana, Tennessee, Pennsylvania, and North Carolina which have banking subsidiaries located in Kentucky. These competing businesses may possess greater resources and offer a greater number of branch locations, higher lending limits, and may offer other services not provided by the Company. In addition, the Company's competitors that are not depository institutions are generally not subject to the extensive regulations that apply to the Company and its subsidiary banks. The Company has attempted to offset some of the advantages of its competitors by arranging participations with other banks for loans above its legal lending limits, expanding into additional markets and product lines, and entering into third party arrangements to better compete for its targeted customer base. Competition from other providers of financial services may reduce or limit the Company's profitability and market share.

The Company competes primarily on the basis of quality of services, interest rates and fees charged on loans, and the rates of interest paid on deposit funds. The business of the Company is not dependent upon any one customer or on a few customers, and the loss of any one or a few customers would not have a material adverse effect on the Company.

No material portion of the business of the Company is seasonal. No material portion of the business of the Company is subject to renegotiation of profits or termination of contracts or subcontracts at the election of the government, though certain contracts are subject to such renegotiation or termination.

The Company is not engaged in operations in foreign countries.

Employees

As of December 31, 2014, the Company had 510 full-time equivalent employees. Employees are offered a variety of benefits. A salary savings plan, group life insurance, hospitalization, dental, vision, and major medical insurance along with postretirement health insurance benefits are available to eligible personnel. Employees are not represented by a union. Management and employee relations are considered good.

The Company previously maintained a Stock Option Plan (“Plan”), which granted certain eligible employees the option to purchase a limited number of the Company’s common stock. The Plan included the conditions and terms that the grantee must meet in order to exercise the options. No options have been granted under the Plan since 2004 and all outstanding options expired during the fourth quarter of 2014. There were no options exercised since 2008.

In 2004, the Company’s Board of Directors adopted an Employee Stock Purchase Plan (“ESPP”). The ESPP was subsequently approved by the Company’s shareholders and became effective July 1, 2004. Under the ESPP, at the discretion of the Board of Directors, employees of the Company and its subsidiaries can purchase Company common stock at a discounted price and without payment of brokerage costs or other fees and in the process benefit from the favorable tax treatment afforded such plans pursuant to Section 423 of the Internal Revenue Code.

Available Information

The Company makes available free of charge through its website (www.farmerscapital.com) its Code of Ethics and other filings with the Securities and Exchange Commission (“SEC”), including its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after electronically filing such material with the SEC.

Item 1A. Risk Factors

Investing in the Company's common stock is subject to risks inherent to the Company's business. The material risks and uncertainties that management believes affect the Company are described below. Before making an investment decision, you should carefully consider the risks and uncertainties described below together with all of the other information included or incorporated by reference in this report. The risks and uncertainties described below are not the only ones facing the Company. Additional risks and uncertainties that management is not aware of or focused on or that management currently deems immaterial may also impair the Company's business operations. This report is qualified in its entirety by these risk factors.

If any of the following risks actually occur, the Company's financial condition and results of operations could be materially and adversely affected. If this were to happen, the market price of the Company's common stock could decline significantly, and shareholders could lose all or part of their investment.

The Company operates in a highly regulated environment and may be adversely affected by changes in federal and state laws and regulations.

The Company is subject to extensive regulation, supervision, and examination by federal and state banking authorities. Any change in applicable regulations or laws could have a substantial adverse impact on the Company and its operations. Additional legislation and regulations that could significantly affect the Company's powers, authority, and operations may be enacted or adopted in the future, which could have a material adverse effect on the Company's results of operations and financial condition. Further, in the performance of their supervisory duties and enforcement powers, the Company's banking regulators have significant discretion and authority to prevent or remedy practices they deem as unsafe or unsound or violations of law. The exercise of regulatory authority may have a negative impact on the Company's operations, which may be material to its results of operations and financial condition.

The Company presently is subject to, and in the future may become subject to, additional supervisory actions and/or enhanced regulation that could have a material negative effect on its business, operating flexibility, financial condition and the value of its common stock.

Under federal and state laws and regulations pertaining to the safety and soundness of insured depository institutions, the KDFI (for state-chartered banks), the Federal Reserve (for bank holding companies), and the FDIC as the insurer of bank deposits, have the authority to compel or restrict certain actions on the Company's part if they determine that the Company has insufficient capital or is otherwise operating in a manner that may be deemed to be inconsistent with safe and sound banking practices. Under this authority, bank regulators can require the Company to enter into informal or formal enforcement orders, including board resolutions, memoranda of understanding, written agreements and consent or cease and desist orders, pursuant to which the Company would be required to take identified corrective actions to address cited concerns and to refrain from taking certain actions.

If the Company is unable to comply with the terms of its current or future regulatory orders to which it may become subject, then it could become subject to additional, heightened supervisory actions and orders, possibly including cease and desist orders, prompt corrective actions, and/or other regulatory enforcement actions. If the Company's regulators were to take such additional supervisory actions, then we could, among other things, become subject to significant restrictions on our ability to develop any new business, as well as restrictions on our existing business, and we could be required to raise additional capital, dispose of certain assets and liabilities within a prescribed period of time, or both. If one or more of the Company's banks were unable to comply with regulatory requirements, such banks could ultimately face failure. The terms of any such supervisory action could have a material negative effect on our business, operating flexibility, financial condition and the value of our common stock.

Our nonperforming assets adversely affect our results of operations and financial condition and take significant management time to resolve.

The Company's level of nonperforming assets (which include performing restructured loans) continue to improve, but remain elevated. Nonperforming assets adversely affect the Company's net income in several ways. The Company does not record interest income on nonaccrual loans or other real estate owned, thereby adversely affecting interest income. When the Company repossesses collateral in foreclosures and similar proceedings, it is required to record the property at its fair value less estimated selling costs, which typically decreases net income.

Nonperforming loans and other real estate owned also increase our risk profile and the amount of capital the Company's regulators believe is appropriate in light of such risks. While the Company seeks to reduce its problem loans through workouts, restructurings, and otherwise, decreases in the value of these assets, the underlying collateral, or our borrowers' performance or financial conditions have adversely affected, and may continue to adversely affect, the Company's results of operations and financial condition. Moreover, the resolution of nonperforming assets requires significant time commitments from management of our banks, which can be detrimental to the performance of their other responsibilities. There can be no assurance that the Company will not experience further increases in nonperforming loans in the future. If economic conditions do not improve or worsen in our markets, the Company could continue to incur additional losses relating to an increase in nonperforming assets.

Losses from loan defaults may exceed the allowance established for that purpose, which will have an adverse effect on the Company's financial condition.

Volatility and deterioration in the broader economy increases the Company's risk of credit losses, which could have a material adverse effect on its operating results. If a significant number of loans in the Company's portfolio are not repaid, it would have an adverse effect on its earnings and overall financial condition. The Company's bank subsidiaries each maintain an allowance for loan losses to provide for losses inherent in the loan portfolio. The allowance for loan losses reflects management's best estimate of probable incurred credit losses in their loan portfolio at the balance sheet date. This evaluation is primarily based upon a review of the bank's historical loan loss experience, known risks contained in the bank's loan portfolio, composition and growth of the bank's loan portfolio, and economic factors. Additionally, a bank's regulators may require additional provision for the loan portfolio in connection with their examinations, agreements, or orders. The determination of an appropriate level of loan loss allowance is an inherently difficult process and is based on numerous assumptions. As a result, the Company's allowance for loan losses may be inadequate to cover actual losses in its loan portfolio. Consequently, the Company risks having additional future provision for loan losses that may materially affect its earnings.

If the Company's local markets experience a prolonged recession or economic downturn, it may be required to make further increases in its allowance for loan losses and to charge off additional loans, which would adversely affect its results of operations and capital.

Substantially all of the Company’s loans are to businesses and individuals located in Kentucky. A continuing or prolonged decline in the Central and Northern Kentucky economies could negatively impact demand for the Company’s products and services, the ability of customers to repay their loans, collateral values securing loans, and the stability of funding sources. This could result in a material adverse effect on the Company’s financial condition, results of operations and prospects. Further, substantially all of the Company’s investments in municipal bonds are issued by political subdivisions or agencies located in Kentucky.

Generally, the Company’s nonperforming loans and assets reflect operating difficulties of individual borrowers; however, the overall economic decline and slow growth of recent years has become a significant contributing factor to the increased levels of nonperforming loans. Sluggish sales and excess inventory in the residential housing market continue to exist and has been the primary cause of elevated delinquencies and foreclosures in recent years. If trends in the housing and real estate markets worsen, the Company expects that it will experience an increase in delinquencies and credit losses. As a result, the Company may be required to increase its provision for loan losses and charge off additional loans in the future, which could adversely affect the Company’s financial condition and results of operations, perhaps materially. If additional provisions and charge-offs cause the Company to experience losses, it may be required to contribute additional capital to its bank subsidiaries to maintain capital ratios required by regulators.

The Company's exposure to credit risk is increased by its real estate development lending.

Real estate development lending has historically been considered to be higher credit risk than that of other types of lending, such as for single-family residential properties. At year-end 2014, 11% of the outstanding balance of real estate development loans was classified as impaired. Real estate development loans typically involve larger loan balances to a single borrower or related borrowers. These loans can be affected by adverse conditions in real estate markets or the economy in general because commercial real estate borrowers' ability to repay their loans depends on successful development and, in most cases, sale of the underlying property. These loans also involve greater risk because they generally are not fully amortized over the loan period, but have a balloon payment due at maturity of the loan. A borrower's ability to make a balloon payment typically depends on being able to either refinance the loan or timely sell the underlying property. In the current economic environment, the ability of borrowers to refinance or sell newly developed property or vacant land remains challenging. If the real estate markets were to worsen or not improve, the Company likely will experience increased credit losses and require additional provisions to our allowance for loan losses, which would adversely impact the Company's earnings and financial condition.

The Company's investment securities portfolio is comparatively larger than other community banks and it is more dependent on its investment portfolio to generate net income.

The Company relies more heavily on its investment securities portfolio as a source of interest income than many other community banks because its loan portfolio makes up a smaller proportion of its earning assets. If the Company is not able to successfully manage the interest rate spread on the investment portfolio, its net interest income will decrease, which would adversely affect its results of operations and negatively impact net income. Investment securities tend to have a lower risk than loans, and as such, generally provide a lower yield. For 2014, average investment securities made up 35.0% of the Company's average total assets. Interest income on investment securities accounted for 22.2% of total interest income for 2014.

The Company periodically sells investment securities at irregular intervals in the normal course of business to execute its current asset/liability management strategies. This will result in the realization of either a net gain or loss. Moreover, proceeds from sales may be reinvested in investment securities with lower yields, which could reduce future earnings from investment securities. The Company monitors its investment securities portfolio for deteriorating values and for other-than-temporary impairment. Any material other-than-temporary impairment charges would likewise have an adverse effect on the Company's results of operations and could lead to additional losses.

The Company cannot accurately predict the effect of the current economy on its future results of operations or the market price of its stock.

The national economy and the financial services sector in particular continue to face challenges stemming from the economic recession of 2007 to 2009. The Company cannot accurately predict the severity or duration of the current economic slowdown, which has adversely impacted its performance and the markets it serves. Any further deterioration in the economies of the nation as a whole or in the Company’s local markets would have an adverse effect, which could be material, on the Company’s financial condition, results of operations, and prospects and could also cause the market price of the Company’s stock to decline. While it is impossible to predict how long these conditions may exist, the economic slowdown could continue to present risks for some time for our industry and the Company.

Interest rate volatility could significantly harm the Company’s results of operations.

The Company’s results of operations are affected by the monetary and fiscal policies of the federal government, the policies of its regulators, and the prevailing interest rates in the United States and the Company’s markets. In addition, it is increasingly common for the Company’s competitors, who may be aggressively seeking to attract deposits as a result of liquidity concerns arising from changing economic or other conditions, to pay rates on deposits that are much higher than normal market rates. A significant component of the Company’s earnings is net interest income, which is the difference between the income from interest earning assets, such as loans, and the expense on interest bearing liabilities, such as deposits. A change in market interest rates could adversely affect the Company’s earnings if market interest rates change such that the interest it pays on deposits and borrowings increases faster than the interest it collects on loans and investments; or, alternatively, if interest rates earned on earning assets decline faster than those rates paid on interest paying liabilities. Consequently, as with most financial institutions, the Company is sensitive to interest rate fluctuations. Changes in market interest rates may also affect the level of voluntary prepayments on loans and mortgage-back investment securities resulting in the receipt of funds that may be reinvested at a lower rate.

The FDIC periodically amends its deposit insurance rate assessment structure, which can increase costs to the Company.

Under the Federal Deposit Insurance Act, as amended by the Dodd-Frank Act, the FDIC must establish and implement a plan to restore the deposit insurance fund's designated reserve ratio to 1.35% of insured deposits by 2020. The FDIC must continue to assess and consider the appropriate level of the reserve ratio annually by considering each of the following: risk of loss to the insurance fund; economic conditions affecting the banking industry; the prevention of sharp swings in the assessment rates; and any other factors the FDIC deems important. The FDIC's current fund management strategy includes a targeted long-term reserve ratio of 2.0%.

The Dodd-Frank Act required changes to a number of components of the FDIC insurance assessment. While these changes have resulted in a lower amount of deposit insurance assessments for the Company, future changes in assessment rates or methodology could adversely impact the Company's future earnings and liquidity in a material amount.

Any future losses may require the Company to raise additional capital; however, such capital may not be available to us on favorable terms or at all.

The Company is required by federal and state regulatory authorities to maintain certain levels of capital to support its operations. Furthermore, as a result of regularly scheduled regulatory examinations, two of the Company's subsidiary banks were required to maintain capital levels significantly above the well-capitalized benchmark at year-end 2014. The Company's ability to raise additional capital, if needed, will depend on conditions in the capital markets at that time and on the Company's future financial condition and performance. Accordingly, the Company cannot make assurances with respect to its ability to raise additional capital on favorable terms, or at all. If the Company cannot raise additional capital when needed, its ability to further expand its operations through internal growth and acquisitions could be materially impaired and its financial condition and liquidity could be materially and adversely affected. The Parent Company is currently under no directive by its regulators to raise any additional capital.

The tightening of available liquidity could limit the Company's ability to replace deposits and fund loan demand, which could adversely affect its earnings and capital levels.

Liquidity is crucial to the Company's business. A tightening of the credit and liquidity markets and the Company's inability to obtain adequate funding to replace deposits may negatively affect its earnings and capital levels. In addition to deposit growth, maturity of investment securities, and loan payments from borrowers, the Company relies from time to time on advances from the Federal Home Loan Bank and other wholesale funding sources to fund loans and replace deposits. In the event of a downturn in the economy, these additional funding sources could be negatively affected which could limit the funds available to the Company. The Company’s liquidity position could be significantly constrained if it were unable to access funds from the Federal Home Loan Bank or other wholesale funding sources.

The Company’s financial condition and outlook may be adversely affected by damage to its reputation.

The Company’s financial condition and outlook is highly dependent upon perceptions of its business practices and reputation. Its ability to attract and retain customers and employees could be adversely affected to the extent its reputation is damaged. Negative public opinion could result from its actual or alleged conduct in any number of activities, including regulatory actions taken against the Company, lending practices, corporate governance, regulatory compliance, mergers of its subsidiaries, or sharing or inadequate protection of customer information. Damage to the Company’s reputation could give rise to loss of customers and legal risks, which could have an adverse impact on its financial condition.

The Company faces strong competition from financial services companies and other companies that offer banking services.

The Company conducts most of its operations in Central and Northern Kentucky. The banking and financial services businesses in these areas are highly competitive and increased competition in its primary market areas may adversely impact the level of its loans and deposits. Ultimately, the Company may not be able to compete successfully against current and future competitors. These competitors include national banks, regional banks, and other community banks. The Company also faces competition from other types of financial institutions, including savings and loan associations, finance companies, brokerage firms, insurance companies, credit unions, mortgage banks, and other financial intermediaries. The Company's competitors include major financial companies whose greater resources may afford them a marketplace advantage by enabling them to maintain numerous locations and mount extensive promotional and advertising campaigns. Areas of competition include interest rates for loans and deposits, efforts to obtain loan and deposit customers, and a range in quality of products and services provided, including new technology-driven products and services. If the Company is unable to attract and retain banking customers, it may be unable to increase its loans and level of deposits.

The price of the Company's common stock may fluctuate significantly, and this may make it difficult to resell the stock when you want or at prices you find attractive.

The Company cannot predict how its common stock will trade in the future. The market value of its common stock will likely continue to fluctuate in response to a number of factors including the following, most of which are beyond our control, as well as the other factors described in this "*Risk Factors*" section:

- general economic conditions and conditions in the financial markets;
- changes in global financial markets, such as interest or foreign exchange rates, stock, commodity or real estate valuations or volatility, and other geopolitical events;
- conditions in our local and national credit, mortgage, and housing markets;
- developments with respect to financial institutions generally, including government regulation;
- our dividend practice; and
- actual and anticipated quarterly fluctuations in our operating results and earnings.

The market value of the Company's common stock may also be impacted by conditions affecting the financial markets in general, including price and trading fluctuations. These conditions may result in: (1) volatility in the level of, and fluctuations in, the market prices of stocks generally and, in turn, the Company's common stock and (2) sales of substantial amounts of the Company's common stock in the market, in each case that could be unrelated or disproportionate to changes in the Company's operating performance. These broad market fluctuations may adversely affect the market value of the Company's common stock.

There may be future sales of additional common stock or other dilution of the Company’s equity, which may adversely affect the market price of the Company’s common stock.

The Company is not restricted from issuing additional common or preferred stock, including any securities that are convertible into or exchangeable for, or that represent the right to receive, common stock or preferred stock or any substantially similar securities. The market price of the Company’s common stock could decline as a result of sales by the Company of a large number of shares of common stock or preferred stock or similar securities in the market or from the perception that such sales could occur.

The Company’s board of directors is authorized generally to cause it to issue additional common and preferred stock without any action on the part of the Company’s shareholders, except as may be required under the listing requirements of the NASDAQ Stock Market. In addition, the board has the power, without shareholder approval, to set the terms of any series of preferred stock that may be issued, including voting rights, dividend rights, preferences, and other terms. This could include preferences over the common stock with respect to dividends or upon liquidation. If the Company issues preferred stock in the future that has a preference over the common stock with respect to the payment of dividends or upon liquidation, or if the Company issues preferred stock with voting rights that dilute the voting power of the common stock, the rights of holders of the common stock or the market price of the common stock could be adversely affected. The Parent Company is currently under no directive by its regulators to raise any additional capital.

You may not receive dividends on the Company's common stock.

Holders of the Company's common stock are entitled to receive dividends only when, as, and if its board of directors declares them and as permitted by its regulators. Although the Company historically (up through 2009) declared quarterly cash dividends on its common stock, it is not required to do so.

As a result of the termination in March 2014 of its agreement with its banking regulators, the Company is no longer required to receive permission from its regulators to make interest payments on its trust preferred securities or to pay dividends on its common and preferred stock. The Company's current goal, however, is to redeem all of its outstanding preferred stock before considering the payment of a dividend on its common stock. The Company redeemed 20,000 shares, or two-thirds, of its original outstanding preferred stock during 2014. The Company intends to redeem its remaining 10,000 shares of preferred stock in 2015, although this action requires approval by our banking regulators. The timing and amount of any further redemption by the Company of its remaining outstanding preferred stock will be disclosed when assured.

Dividends declared and discount accretion on the Company's Series A preferred stock reduce the net income available to common stockholders and reduce earnings per common share. Moreover, under the terms of the Company's articles of incorporation, it is unable to declare dividend payments on shares of its common stock if it is in arrears on the dividends on the Series A preferred stock. If the Company is in arrears on interest payments on its trust preferred securities, it may not pay dividends on its common stock until such interest obligations are brought current.

The Company's ability to pay dividends depends upon the results of operations of its subsidiary banks and certain regulatory considerations.

The Parent Company is a bank holding company that conducts substantially all of its operations through its subsidiary banks. As a result, the Company's ability to make dividend payments on its common stock depends primarily on certain federal and state regulatory considerations and the receipt of dividends and other distributions from its bank subsidiaries. There are also restrictions on the ability of two of our subsidiary banks to pay dividends or make other payments to the Parent Company related to current regulatory agreements that are in effect, thus further restricting the Parent Company's ability to make payments to its shareholders.

The trading volume in the Company's common stock is less than that of many other similar companies.

The Company's common stock is listed for trading on the NASDAQ Global Select Stock Market. As of December 31, 2014, the 50-day average trading volume of the Company's common stock on NASDAQ was 9,982 shares or .13% of the total common shares outstanding of 7,489,388. An efficient public trading market is dependent upon the existence in the marketplace of willing buyers and willing sellers of a stock at any given time. The Company has no control over such individual decisions of investors and general economic and market conditions. Given the lower trading volume of the Company's common stock, larger sales volumes of its common stock could cause the value of its common stock to decrease. Moreover, due to its lower trading volume, it may take longer to liquidate your position in the Company's common stock without detrimentally affecting the price.

There can be no assurance when the Company's remaining Series A preferred stock can be redeemed.

Subject to consultation with, and approval from its banking regulators, the Company intends to repurchase the remaining 10,000 shares of its Series A preferred stock. However, there can be no assurance when the shares can be repurchased, if at all. Until such time as the Series A preferred stock is repurchased, the Company will remain subject to the terms and conditions of the instrument, which, among other things, limit the Company's ability to repurchase or redeem common stock.

Holders of the Company's Series A preferred stock have rights that are senior to those of the Company's common stockholders.

The Company's Series A preferred stock is senior to the Company's shares of common stock, and holders of the Series A preferred stock have certain rights and preferences that are senior to holders of the Company's common stock. The restrictions on the Company's ability to declare and pay dividends to common stockholders are discussed above. In addition, the Company and its subsidiaries may not purchase, redeem, or otherwise acquire for consideration any shares of the Company's common stock unless the Company has paid in full all accrued dividends on the Series A preferred stock for all prior dividend periods, other than in certain circumstances. Furthermore, the Series A preferred stock is entitled to a liquidation preference over shares of the Company's common stock in the event of liquidation, dissolution, or winding up.

Holders of the Company's Series A preferred stock have limited voting rights.

Except (1) in connection with the election of two directors to the Company's board of directors if its dividends on the Series A preferred stock are in arrears and we have missed six quarterly dividends and (2) as otherwise required by law, holders of the Company's Series A preferred stock have limited voting rights. In addition to any other vote or consent of shareholders required by law or the Company's articles of incorporation, the vote or consent of holders owning at least 66 2/3% of the shares of Series A preferred stock outstanding is required for (1) any authorization or issuance of shares ranking senior to the Series A preferred stock; (2) any amendment to the rights of the Series A preferred stock that adversely affects the rights, preferences, privileges, or voting power of the Series A preferred stock; or (3) consummation of any merger, share exchange, or similar transaction unless the shares of Series A preferred stock remain outstanding or are converted into or exchanged for preference securities of the surviving entity other than the Company and have such rights, preferences, privileges and voting power as are not materially less favorable than those of the holders of the Series A preferred stock.

The Company's common stock constitutes equity and is subordinate to its existing and future indebtedness and its Series A preferred stock, and is effectively subordinated to all the indebtedness and other non-common

equity claims against its subsidiaries.

Shares of the Company’s common stock represent equity interests in the Parent Company and do not constitute indebtedness. Accordingly, the shares of the Company’s common stock rank junior to all of its indebtedness and to other non-equity claims on Farmers Capital Bank Corporation with respect to assets available to satisfy such claims. Additionally, dividends to holders of the Company’s common stock are subject to the prior dividend and liquidation rights of the holders of the Company’s Series A preferred stock and any additional preferred stock we may issue. The Series A preferred stock has a liquidation preference at December 31, 2014 of $1 thousand per share, or $10.0 million in the aggregate, plus any accrued and unpaid dividends.

The Company’s right to participate in any distribution of assets of any of its subsidiaries upon the subsidiary’s liquidation or otherwise, and thus the ability of the Company’s common stockholders to benefit indirectly from such distribution, will be subject to the prior claims of creditors of that subsidiary. As a result, holders of the Company’s common stock are effectively subordinated to all existing and future liabilities and obligations of its subsidiaries, including claims of depositors.

The current economic environment exposes the Company to higher credit losses and expenses and may result in lower earnings or increase the likelihood of losses.

Although the Company remains well-capitalized, it continues to operate in a very challenging and uncertain economic environment. Financial institutions, including the Company, continue to be adversely effected by difficult economic conditions that have impacted not only local markets, but on a national and global scale. Substantial deterioration in real estate and other financial markets in recent years, although improving, have and may continue to adversely impact the Company's financial performance. Declines in real estate values and home sales volumes, along with historically low labor participation rates and other economic stresses, can decrease the value of collateral securing loans extended to borrowers, particularly that of real estate loans. A decrease in the value of real estate securing loans may make it more difficult for the Company to recover amounts it is owed in the event of default by a borrower.

Current economic conditions may result in a higher degree of financial stress on the Company's borrowers and their customers which could impair the Company's ability to collect payments on loans, potentially increasing loan delinquencies, nonperforming assets, foreclosures, and losses. Current market forces have and may in the future cause the value of investment securities or other assets held by the Company to deteriorate, resulting in impairment charges, higher losses, and lower regulatory capital levels.

Market volatility could adversely impact the Company's results of operations, liquidity position, and access to additional capital.

The capital and credit markets experienced heavy volatility and disruptions during much of the most recent economic downturn, with unprecedented levels of volatility and other disruptions. In many cases, this led to downward pressure on stock prices and credit availability for certain issuers without regard to those issuers' underlying financial strength. If similar market disruptions and volatility recur, the Company may experience a material adverse effect on its results of operations and liquidity position or on its ability to access additional capital.

Risks associated with unpredictable economic and political conditions may be amplified as a result of limited market area.

Commercial banks and other financial institutions, including the Company, are affected by economic and political conditions, both domestic and international, and by governmental monetary policies. These conditions and other factors beyond the Company's control may adversely affect profitability. In addition, almost all of the Company's primary business area is located in Central and Northern Kentucky. Significant downturns in this economic region may result in a deterioration of the Company's credit quality, reduce demand for credit, and may harm the financial stability of the Company's customers. Due to the Company's regional market area, these negative conditions may have a more noticeable effect on the Company than would be experienced by an institution with a larger, more diverse market area.

The Company's results of operations are significantly affected by the ability of its borrowers to repay their loans.

Lending money is an essential part of the banking business. However, borrowers do not always repay their loans. The risk of non-payment is affected by:

- unanticipated declines in borrower income or cash flow;
- changes in economic and industry conditions;
- the duration of the loan; and
- in the case of a collateralized loan, uncertainties as to the future value of the collateral.

Due to the fact that the outstanding principal balances can be larger for commercial loans than other types of loans, such loans present a greater risk to the Company than other types of loans when non-payment by a borrower occurs.

Consumer loans typically have shorter terms and lower balances with higher yields compared to real estate mortgage loans, but generally carry higher risks of frequency of default than real estate mortgage and commercial loans. Consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be affected by adverse personal circumstances. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount that can be recovered on these loans.

Inability to hire or retain certain key professionals, management, and staff could adversely affect the Company's revenues and net income.

The Company relies on key personnel to manage and operate its business, including major revenue generating functions such as its loan and deposit portfolios. The loss of key staff may adversely affect the Company's ability to maintain and manage these portfolios effectively, which could negatively affect our revenues. In addition, loss of key personnel could result in increased recruiting and hiring expenses, which could cause a decrease in our net income.

The Company's controls and procedures may fail or be circumvented.

The Company's management regularly reviews and updates its internal controls, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, however well-designed and operated, can provide only reasonable, not absolute, assurances that the objectives of the system of controls are met. Any failure or circumvention of the Company's controls and procedures or failure to comply with regulations related to controls and procedures could have a material and adverse effect on the Company's business, results of operations, and financial condition.

The Company offers online banking services and both sends and receives confidential customer information electronically. This activity is vulnerable to security breaches and computer viruses which could expose the Company to litigation and adversely affect our reputation and overall operations.

The secure transmission of confidential information over the Internet is a significant element of online banking. The Company has implemented administrative, technical, and physical security controls and testing procedures to safeguard its customer information. However, those controls could be circumvented or fail, leaving the Company's computer network or those of its customers vulnerable to unauthorized access, computer viruses, phishing schemes, and other security problems. The Company could be required to commit additional resources to protect against the threat of security breaches and computer viruses, or to remedy problems caused by security breaches or viruses. To the extent that the Company's activities or the activities of its customers involve the storage and transmission of confidential information, security breaches and viruses could expose the Company to litigation and other possible liabilities. The inability to prevent security breaches or computer viruses could also cause existing customers to lose confidence in the Company's systems and could adversely affect its reputation and overall operations.

The Company's operations rely on certain external vendors.

The Company utilizes certain external vendors to provide products and services necessary to maintain its day-to-day operations. The Company is exposed to the risk that such vendors fail to perform under these arrangements. This could result in disruption to the Company’s business and have a material adverse impact on the Company’s results of operations and financial condition. There can be no assurance that the Company’s policies and procedures designed to monitor and mitigate vendor risks will be effective in preventing or limiting the effect of vendor non-performance.

The Company is subject to claims and litigation pertaining to fiduciary responsibility.

The Company’s customers or others may make claims and take legal action against us related to fiduciary responsibilities. If claims and legal action against the Company are not resolved in a favorable manner to the Company, it could result in a material financial liability or damage to our reputation.

The Dodd-Frank Act may increase the Company’s costs of operations which could adversely impact the Company's results of operations, financial condition or liquidity.

The goals of the Dodd-Frank Act include restoring public confidence in the financial system, preventing another financial crisis, and allowing regulators to identify failings in the system before another crisis can occur. As part of the reform, the Dodd-Frank Act created the Financial Stability Oversight Council, with oversight authority for monitoring and regulating systemic risk, and the Bureau of Consumer Financial Protection, which has broad regulatory and enforcement powers over consumer financial products and services. The Dodd-Frank Act also changes the responsibilities of the current federal banking regulators, imposes additional corporate governance and disclosure requirements in areas such as executive compensation and proxy access, and limits or prohibits proprietary trading and hedge fund and private equity activities of banks. It also impacts areas such as deposit insurance, mortgage lending, capital requirements, securitizations, and insurance.

The scope of the Dodd-Frank Act impacts many aspects of the financial services industry and requires the development and adoption of numerous implementing regulations, many of which have yet to be finalized. Consequently, the effects of the Dodd-Frank Act on the financial services industry and the Company will depend, in large part, upon the extent to which regulators exercise the authority granted to them and the approaches taken to implement the regulations. The Company continually assesses the impact of the Dodd-Frank Act on its business and operations and believes that compliance with these new laws and regulations will likely result in higher costs, but the probable impact cannot be measured with a high degree of certainty. Compliance with the new laws and regulations could adversely impact the Company’s results of operations, financial condition, or liquidity, any of which may impact the market price of the Company’s common stock.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Company owns or leases buildings that are used in the normal course of its business. The corporate headquarters is located at 202 W. Main Street, Frankfort, Kentucky, in a building owned by the Company. The Company’s subsidiaries own or lease various other offices in the counties and cities in which they operate. See the Notes to Consolidated Financial Statements contained in Item 8, *“Financial Statement and Supplementary Data,”* of this Form 10-K for information with respect to the amounts at which bank premises and equipment are carried and commitments under long-term leases.

Unless otherwise indicated, the properties listed below are owned by the Company and its subsidiaries as of December 31, 2014.

Corporate Headquarters

202 – 208 W. Main Street, Frankfort, KY

Banking Offices
Farmers Bank:
125 W. Main Street, Frankfort, KY
555 Versailles Road, Frankfort, KY
1401 Louisville Road, Frankfort, KY
154 Versailles Road, Frankfort, KY
1301 US 127 South, Frankfort, KY (leased)
128 S. Main Street, Lawrenceburg, KY
201 West Park Shopping Center, Lawrenceburg, KY
838 N. College Street, Harrodsburg, KY
1035 Ben Ali Drive, Danville, KY
United Bank:
100 United Drive, Versailles, KY
146 N. Locust Street, Versailles, KY
206 N. Gratz, Midway, KY
200 E. Main Street, Georgetown, KY
100 Farmers Bank Drive, Georgetown, KY (leased)
100 N. Bradford Lane, Georgetown, KY
3285 Main Street, Stamping Ground, KY
2509 Sir Barton Way, Lexington, KY
3098 Harrodsburg Road, Lexington, KY (leased)
201 N. Main Street, Nicholasville, KY
995 S. Main Street (Kroger Store), Nicholasville, KY (leased)
986 N. Main Street, Nicholasville, KY
106 S. Lexington Avenue, Wilmore, KY
First Citizens:
425 W. Dixie Avenue, Elizabethtown, KY
3030 Ring Road, Elizabethtown, KY
111 Towne Drive (Kroger Store), Elizabethtown, KY (leased)
645 S. Dixie Blvd., Radcliff, KY
4810 N. Preston Highway, Shepherdsville, KY
157 Eastbrooke Court, Mt. Washington, KY
Citizens Northern:
103 Churchill Drive, Newport, KY
7300 Alexandria Pike, Alexandria, KY
164 Fairfield Avenue, Bellevue, KY
8730 US Highway 42, Florence, KY
34 N. Ft. Thomas Avenue, Ft. Thomas, KY
2911 Alexandria Pike, Highland Heights, KY
2006 Patriot Way, Independence, KY
2774 Town Center Blvd., Crestview Hills, KY (leased)

Data Processing Center

102 Bypass Plaza, Frankfort, KY

Other

201 W. Main Street, Frankfort, KY

The Company considers its properties to be suitable and adequate based on its present needs.

Item 3. Legal Proceedings

As of December 31, 2014, there were various pending legal actions and proceedings against the Company arising from the normal course of business and in which claims for damages are asserted. It is the opinion of management, after discussion with legal counsel, that the disposition or ultimate resolution of such claims and legal actions will not have a material effect upon the consolidated financial statements of the Company.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

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

Beginning January 1, 2014, the Company changed the payment form of its board meeting fees and quarterly fees from 100% cash to 50% in cash and 50% in Company common stock. The shares are issued as part of a plan adopted by the board of directors. Each director has elected to participate by entering an agreement with the Company to accept common stock in lieu of cash for 50% of the director's board meeting and quarterly fees. As the shares are only issued to directors as part of a plan approved by the board, the shares are exempt from the registration requirements of the Securities Act of 1933, as amended (the "1933 Act"), as a sale not involving any public offering under Section 4(2) of the 1933 Act. The value of the shares issued in payment is determined by the closing price of the Company's common stock on the NASDAQ Global Select Market on the business trading day immediately preceding the meeting day for board meeting fees and the business trading day immediately preceding the first meeting of the quarter for each quarterly fee. Attendance for committee meetings will continue to be paid completely in cash. As employee directors are not paid director's fees, only non-employee directors receive stock under this plan.

During 2014, the Company issued a total of 3,788 shares of common stock to its non-employee directors under this plan as compensation for $82 thousand of director fees. The cash retained by the Company by issuing common stock in lieu of paying cash is used for general corporate purposes. There are no brokers involved in the issuance of stock to directors and no commissions or other broker fees are paid.

At various times, the Company's Board of Directors has authorized the purchase of shares of the Company's outstanding common stock. No stated expiration dates have been established under any of the previous authorizations. There were no shares of common stock repurchased by the Company during the quarter ended December 31, 2014. There are 84,971 shares that may still be purchased under the various authorizations, though no shares have been purchased since 2008.

Performance Graph

The following graph sets forth a comparison of the five-year cumulative total returns among the shares of Company Common Stock, the NASDAQ Composite Index ("broad market index"), and Southeastern Banks Under $1 Billion Market-Capitalization ("peer group index"). Cumulative shareholder return is computed by dividing the sum of the cumulative amount of dividends for the measurement period and the difference between the share price at the end and the beginning of the measurement period by the share price at the beginning of the measurement period.

The broad market index includes over 3,000 domestic and international based common shares listed on The NASDAQ Stock Market. The peer group index consists of 37 banking companies in the Southeastern United States. The Company is included among those in the peer group index.

	2009	2010	2011	2012	2013	2014
Farmers Capital Bank Corporation	$100.00	$47.75	$43.93	$119.86	$212.82	$227.89
NASDAQ Composite	100.00	117.61	118.70	139.00	196.83	223.74
Southeastern Banks Under $1 Billion Market-Capitalization	100.00	118.15	121.31	138.43	196.85	224.92

Corporate Address

The headquarters of Farmers Capital Bank Corporation is located at:

202 West Main Street

Frankfort, Kentucky 40601

Direct correspondence to:

Farmers Capital Bank Corporation

P.O. Box 309

Frankfort, Kentucky 40602-0309

Phone: (502) 227-1668

www.farmerscapital.com

Annual Meeting

The annual meeting of shareholders of Farmers Capital Bank Corporation will be held Tuesday, May 12, 2015 at 11:00 a.m. at the main office of Farmers Bank & Capital Trust Company, Frankfort, Kentucky.

Form 10-K

For a free copy of Farmers Capital Bank Corporation's Annual Report on Form 10-K filed with the Securities and Exchange Commission, please write:

Mark A. Hampton, Executive Vice President, Chief Financial Officer, and Secretary

Farmers Capital Bank Corporation

P.O. Box 309

Frankfort, Kentucky 40602-0309

Phone: (502) 227-1668

Web Site Access to Filings

All reports filed electronically by the Company with the United States Securities and Exchange Commission, including annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports, are available at no cost on the Company’s website at www.farmerscapital.com.

NASDAQ Market Participants
J.J.B. Hilliard, W.L. Lyons, LLC
(502) 588-8400
(800) 444-1854

Raymond James & Associates, Inc.
(800) 248-8863

UBS Securities, LLC
(859) 269-6900
(502) 589-4000

The Transfer Agent and Registrar for Farmers Capital Bank Corporation is American Stock Transfer & Trust Company, LLC.

American Stock Transfer & Trust Company, LLC

Shareholder Relations

59 Maiden Lane - Plaza Level

New York, NY 10038

Phone: (800) 937-5449

Fax: (718) 236-2641

Email: Info@amstock.com

Website: www.amstock.com

Additional information is set forth under the captions *"Shareholder Information"* and *"Common Stock Price"* on page 73 under Part II, Item 7 and Note 18 *"Regulatory Matters"* in the notes to the Company's 2014 audited consolidated financial statements on pages 116 to 119 of this Form 10-K and is hereby incorporated by reference.

Item 6. Selected Financial Data

Selected Financial Highlights
December 31,

(In thousands, except per share data)	2014	2013	2012	2011	2010
Results of Operations					
Interest income	$64,352	$66,733	$71,222	$78,349	$89,751
Interest expense	10,153	11,995	18,258	24,670	34,948
Net interest income	54,199	54,738	52,964	53,679	54,803
Provision for loan losses	(4,364)	(2,600)	2,772	13,487	17,233
Noninterest income	23,273	22,116	24,654	24,391	34,110
Noninterest expense	59,278	61,573	59,787	62,492	62,711
Net income	16,459	13,446	12,149	2,738	6,932
Dividends and accretion on preferred shares	1,927	1,951	1,922	1,896	1,871
Net income available to common shareholders	14,532	11,495	10,227	842	5,061
Per Common Share Data					
Basic and diluted net income	$1.94	$1.54	$1.37	$.11	$.68
Cash dividends declared	-	-	-	-	-
Book value	21.75	18.73	18.54	17.18	16.35
Tangible book value[1]	21.69	18.61	18.35	16.86	15.87
Selected Ratios					
Percentage of net income to:					
Average shareholders' equity (ROE)	9.30%	7.97%	7.38%	1.77%	4.55%
Average total assets (ROA)	.92	.74	.65	.14	.33
Percentage of common dividends declared to net income	-	-	-	-	-
Percentage of average shareholders' equity to average total assets	9.84	9.34	8.85	8.05	7.32
Total shareholders' equity	$172,929	$170,055	$168,021	$157,057	$149,896
Total assets	1,782,606	1,809,555	1,807,232	1,883,590	1,935,693
Long term borrowings	168,694	176,850	178,267	239,664	252,209
Senior perpetual preferred stock	10,000	29,988	29,537	29,115	28,719
Weighted average common shares outstanding - basic and diluted	7,483	7,474	7,457	7,424	7,390

[1]Represents total common equity less intangible assets divided by the number of common shares outstanding at the end of the period.

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

Glossary of Financial Terms

Allowance for loan losses

A valuation allowance to offset credit losses specifically identified in the loan portfolio, as well as management's best estimate of probable incurred losses in the remainder of the portfolio at the balance sheet date. Management estimates the allowance balance required using past loan loss experience, an assessment of the financial condition of individual borrowers, a determination of the value and adequacy of underlying collateral, the condition of the local economy, an analysis of the levels and trends of the loan portfolio, and a review of delinquent and classified loans. Actual losses could differ significantly from the amounts estimated by management.

Dividend payout ratio

Cash dividends paid on common shares, divided by net income.

Basis points

Each basis point is equal to one hundredth of one percent. Basis points are calculated by multiplying percentage points times 100. For example: 3.7 percentage points equals 370 basis points.

Interest rate sensitivity

The relationship between interest sensitive earning assets and interest bearing liabilities.

Net charge-offs

The amount of total loans charged off net of recoveries of loans that have been previously charged off.

Net interest income

Total interest income less total interest expense.

Net interest margin

Taxable equivalent net interest income expressed as a percentage of average earning assets.

Net interest spread

The difference between the taxable equivalent yield on earning assets and the rate paid on interest bearing funds.

Other real estate owned

Real estate not used for banking purposes. For example, real estate acquired through foreclosure.

Provision for loan losses

The charge against current income needed to maintain an adequate allowance for loan losses.

Return on average assets (ROA)

Net income (loss) divided by average total assets. Measures the relative profitability of the resources utilized by the Company.

Return on average equity (ROE)

Net income (loss) divided by average shareholders' equity. Measures the relative profitability of the shareholders' investment in the Company.

Tax equivalent basis (TE)

Income from tax-exempt loans and investment securities has been increased by an amount equivalent to the taxes that would have been paid if this income were taxable at statutory rates. In order to provide comparisons of yields and margins for all earning assets, the interest income earned on tax-exempt assets is increased to make them fully equivalent to other taxable interest income investments.

Weighted average number of common shares outstanding

The number of shares determined by relating (a) the portion of time within a reporting period that common shares have been outstanding to (b) the total time in that period.

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following pages present management's discussion and analysis of the consolidated financial condition and results of operations of Farmers Capital Bank Corporation (the "Company" or "Parent Company"), a bank holding company, and its bank and nonbank subsidiaries. Bank subsidiaries include Farmers Bank & Capital Trust Company ("Farmers Bank") in Frankfort, KY, United Bank & Trust Company ("United Bank") in Versailles, KY, First Citizens Bank ("First Citizens") in Elizabethtown, KY, and Citizens Bank of Northern Kentucky, Inc. ("Citizens Northern") in Newport, KY.

At year-end 2014, Farmers Bank had three primary subsidiaries, which include EG Properties, Inc., Leasing One Corporation ("Leasing One"), and Farmers Capital Insurance Corporation ("Farmers Insurance"). EG Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of Farmers Bank. Leasing One is a commercial leasing company in Frankfort, KY, and Farmers Insurance is an insurance agency in Frankfort, KY. United Bank has one direct subsidiary, EGT Properties, Inc. EGT Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of United Bank. First Citizens has one subsidiary, HBJ Properties, LLC. HBJ Properties, LLC is involved in real estate management and liquidation for certain repossessed properties of First Citizens. Citizens Northern has one direct subsidiary, ENKY Properties, Inc., which is involved in real estate management and liquidation for certain repossessed properties of Citizens Northern.

The Company had three active nonbank subsidiaries in 2014, FCB Services, Inc. ("FCB Services"), FFKT Insurance Services, Inc. ("FFKT Insurance"), and EKT Properties, Inc. ("EKT"). FCB Services is a data processing subsidiary located in Frankfort, KY that provides services to the Company's banks as well as unaffiliated entities. FFKT Insurance is a captive property and casualty insurance company insuring primarily deductible exposures and uncovered liability related to properties of the Company. EKT, which was dissolved effective December 31, 2014, was formed to manage and liquidate certain real estate properties repossessed by the Company. The Company has three subsidiaries organized as Delaware statutory trusts that are not consolidated into its financial statements. These trusts were formed for the purpose of issuing trust preferred securities. All significant intercompany transactions and balances are eliminated in consolidation.

For a complete list of the Company's subsidiaries, please refer to the discussion under the heading *"Organization"* included in Part 1, Item 1 of this Form 10-K. The following discussion should be read in conjunction with the audited consolidated financial statements and related footnotes that follow.

Forward-Looking Statements

This report contains forward-looking statements with the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), under the Private Securities Litigation Reform Act of 1995 that involve risks and uncertainties. Statements in this report that are not statements of historical fact are forward-looking statements. In general, forward-looking statements relate to a discussion of future financial results or projections, future economic performance, future operational plans and objectives, and statements regarding the underlying assumptions of such statements. Although management of the Company believes that the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate, and therefore, there can be no assurance that the forward-looking statements included herein will prove to be accurate.

Various risks and uncertainties may cause actual results to differ materially from those indicated by the Company's forward-looking statements. In addition to the risks described under Part 1, Item 1A *"Risk Factors"* in this report, factors that could cause actual results to differ from the results discussed in the forward-looking statements include, but are not limited to: economic conditions (both generally and more specifically in the markets in which the Company and its subsidiaries operate) and lower interest margins; competition for the Company's customers from other providers of financial services; deposit outflows or reduced demand for financial services and loan products; government legislation, regulation, and changes in monetary and fiscal policies (which changes from time to time and over which the Company has no control); changes in interest rates; changes in prepayment speeds of loans or investment securities; inflation; material unforeseen changes in the liquidity, results of operations, or financial condition of the Company's customers; changes in the level of non-performing assets and charge-offs; changes in the number of common shares outstanding; the capability of the Company to successfully enter into a definitive agreement for and close anticipated transactions; unexpected claims or litigation against the Company; expected insurance or other recoveries; technological or operational difficulties; the impact of new accounting pronouncements and changes in policies and practices that may be adopted by regulatory agencies; acts of war or terrorism; the ability of the Parent Company to receive dividends from its subsidiaries; the impact of larger or similar financial institutions encountering difficulties, which may adversely affect the banking industry or the Company; the Company or its subsidiary banks' ability to maintain required capital levels and adequate funding sources and liquidity; and other risks or uncertainties detailed in the Company's filings with the Securities and Exchange Commission, all of which are difficult to predict and many of which are beyond the control of the Company.

The Company's forward-looking statements are based on information available at the time such statements are made. The Company expressly disclaims any intent or obligation to update any forward-looking statements to reflect changes in underlying assumptions or factors, new information, future events, or other changes.

Application of Critical Accounting Policies

The Company's audited consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and follow general practices applicable to the banking industry. Application of these principles requires management to make estimates, assumptions, and judgments 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 reported period. These estimates, assumptions, and judgments are based on information available as of the date of the financial statements. Certain policies inherently have a greater reliance on the use of estimates, assumptions, and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions, and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility between reporting periods. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by third-party sources, when available. When third-party information is not available, valuation adjustments are estimated in good faith by management primarily through the use of internal cash flow modeling techniques.

The most significant accounting policies followed by the Company are presented in Note 1 of the Company's 2014 audited consolidated financial statements. These policies, along with the disclosures presented in other financial statement notes and in this Management's Discussion and Analysis of Financial Condition and Results of Operations, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, management has identified the determination of the allowance for loan losses and fair value measurements to be the accounting areas that require the most subjective or complex judgments, and as such could be most subject to revision as new information becomes available.

Allowance for Loan Losses

The allowance for loan losses represents credit losses specifically identified in the loan portfolio, as well as management's estimate of probable incurred credit losses in the loan portfolio at the balance sheet date. Determining the amount of the allowance for loan losses and the related provision for loan losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant changes. The loan portfolio also represents the largest asset group on the consolidated balance sheets. Additional information related to the allowance for loan losses that describes the methodology and risk factors can be found under the captions *"Asset Quality"* and *"Nonperforming Assets"* in this Management's Discussion and Analysis of Financial Condition and Results of Operations, as well as Notes 1 and 4 of the Company’s 2014 audited consolidated financial statements.

Fair Value Measurements

The carrying value of certain financial assets and liabilities of the Company is impacted by the application of fair value measurements, either directly or indirectly. Fair value is the price that would be received to sell an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. In certain cases, an asset or liability is measured and reported at fair value on a recurring basis, such as investment securities classified as available for sale. In other cases, management must rely on estimates or judgments to determine if an asset or liability not measured at fair value warrants an impairment write-down or whether a valuation reserve should be established.

The Company estimates the fair value of a financial instrument using a variety of valuation methods. Where financial instruments are actively traded and have quoted market prices, quoted market prices are used for fair value. Active markets are those where transaction volumes are sufficient to provide objective pricing information with reasonably narrow bid/ask spreads and where quoted prices do not vary widely. When the financial instruments are not actively traded, other observable market inputs such as quoted prices of securities with similar characteristics may be used, if available, to determine fair value. Inactive markets are characterized by low transaction volumes, price quotations that vary substantially among market participants, or in which minimal information is released publicly.

When observable market prices do not exist, the Company estimates fair value primarily by using cash flow and other financial modeling methods. The valuation methods may also consider factors such as liquidity and concentration concerns. Other factors such as model assumptions, market dislocations, and unexpected correlations can affect estimates of fair value. Changes in these underlying factors, assumptions, or estimates in any of these areas could materially impact the amount of revenue or loss recorded.

Additional information regarding fair value measurements can be found in Notes 1 and 19 of the Company's 2014 audited consolidated financial statements. The following is a summary of the Company's more significant assets that may be affected by fair value measurements, as well as a brief description of the current accounting practices and valuation methodologies employed by the Company:

<u>Available For Sale Investment Securities</u>

Investment securities classified as available for sale are measured and reported at fair value on a recurring basis. Available for sale investment securities are valued primarily by independent third party pricing services under the market valuation approach that include, but are not limited to, the following inputs:

Mutual funds and equity securities are priced utilizing real-time data feeds from active market exchanges for identical securities; and

Government-sponsored agency debt securities, obligations of states and political subdivisions, mortgage-backed securities, corporate bonds, and other similar investment securities are priced with available market information through processes using benchmark yields, matrix pricing, prepayment speeds, cash flows, live trading data, and market spreads sourced from new issues, dealer quotes, and trade prices, among others sources.

At December 31, 2014, all of the Company’s available for sale investment securities were measured using observable market data.

Other Real Estate Owned

Other real estate owned (“OREO”) includes properties acquired by the Company through, or in lieu of, actual loan foreclosures and initially carried at fair value less estimated costs to sell. Fair value is generally based on third party appraisals of the property that includes comparable sales data. The carrying value of each OREO property is updated at least annually and more frequently when market conditions significantly impact the value of the property. If the carrying amount exceeds fair value less estimated costs to sell, an impairment loss is recorded through expense. OREO is subsequently accounted for at the lower of carrying amount or fair value less estimated costs to sell. At December 31, 2014, OREO was $32.0 million compared to $37.8 million at year-end 2013.

Impaired Loans

Loans are considered impaired when it is probable that the Company will be unable to collect all amounts due under the contractual terms of the loan agreement. Impaired loans are measured at the present value of expected future cash flows, discounted at the loan's effective interest rate, at the loan's observable market price, or at the fair value of the collateral based on recent appraisals if the loan is collateral dependent. If the value of an impaired loan is less than the unpaid balance, the difference is credited to the allowance for loan losses with a corresponding charge to provision for loan losses. Loan losses are charged against the allowance for loan losses when management believes the uncollectibility of a loan is confirmed.

Appraisals used in connection with valuing collateral-dependent loans may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Appraisers take absorption rates into consideration and adjustments are routinely made in the appraisal process to identify differences between the comparable sales and income data available. Such adjustments consist mainly of estimated costs to sell that are not included in certain appraisals or to update appraised collateral values as a result of market declines of similar properties for which a newer appraisal is available. These adjustments can be significant. Impaired loans were $44.0 million and $58.3 million at year-end 2014 and 2013, respectively.

EXECUTIVE LEVEL OVERVIEW

The Company offers a variety of financial products and services at its 36 banking locations in 23 communities throughout Central and Northern Kentucky. The Company has four separately chartered commercial banks that operate under a community banking philosophy. This philosophy focuses primarily on understanding the banking needs of those in our local and surrounding communities and providing them with competitively priced products and a high level of personalized service. The most significant products and services the Company offers include consumer and business lending, checking, savings, and other deposit accounts, automated teller machines, electronic bill payments, and providing trust services and other traditional banking products and services. The primary goals of the Company are to continually improve profitability and shareholder value, increase and maintain a strong capital position, provide excellent service to our customers through our community banking structure, and to provide a challenging and rewarding work environment for our employees.

The Company generates a significant amount of its revenue, cash flows, and net income from interest income and net interest income. The ability to properly manage net interest income under changing market environments is crucial to the success of the Company. Managing credit risk also has a significant influence on the operating results of the Company. While the overall economy expanded during 2014 based on GDP and certain other measures, the Company continues to face headwinds related to the level of nonperforming assets that built up following the deep recession of 2007 to 2009. The Company has focused a significant amount of effort to reduce its nonperforming assets over the last several years which has led to a significant decline when compared with its peak during 2010. Nonperforming assets have decreased in each of the last nine consecutive quarters. Unemployment rates continue to improve, but labor force participation rates hover near 30-year lows. Many of those newly hired consist of part-time workers.

The Company remains committed to strong credit underwriting standards, which have at times hindered the opportunity to increase loans. Average loans decreased $38.2 million or 3.8% during 2014 and have been accelerated by early payoffs of several larger balance credits, primarily related to commercial real estate. Many of these early payoffs were from nonbank competitors willing to offer nonrecourse and other terms that are significantly below our current underwriting standards. Although loans have declined, the overall credit quality of the portfolio continued to improve as a result of strategies to strengthen credit underwriting. Improving credit quality is the primary driver of the decrease in the allowance for loan losses and related provision expense.

While the Company continues to operate in a challenging economic and business environment, 2015 will include a focus on further reducing nonperforming assets. The Company is renewing business development efforts to increase organic loan growth and seeking to add experienced bankers to its lending teams. The Company redeemed 20,000 shares of its outstanding preferred stock in 2014, made up of two separate redemptions of 10,000 shares each. We intend to redeem the remaining 10,000 shares in 2015, although this action is dependent upon receiving approval by our banking regulators.

RESULTS OF OPERATIONS

The Company reported net income of $16.5 million for 2014 an increase of $3.0 million or 22.4% compared to $13.4 million for 2013. On a per common share basis, net income was $1.94 and $1.54 for 2014 and 2013, respectively. Selected income statement amounts and related information is presented in the table below.

(In thousands, except per share data) Years Ended December 31,	2014	2013	Increase (Decrease)
Interest income	$64,352	$66,733	$ (2,381)
Interest expense	10,153	11,995	(1,842)
Net interest income	54,199	54,738	(539)
Provision for loan losses	(4,364)	(2,600)	(1,764)
Net interest income after provision for loan losses	58,563	57,338	1,225
Noninterest income	23,273	22,116	1,157
Noninterest expenses	59,278	61,573	(2,295)
Income before income taxes	22,558	17,881	4,677
Income tax expense	6,099	4,435	1,664
Net income	$16,459	$13,446	$ 3,013
Less preferred stock dividends and discount accretion	1,927	1,951	(24)
Net income available to common shareholders	$14,532	$11,495	$ 3,037
Basic and diluted net income per common share	$1.94	$1.54	$ .40
Weighted average common shares outstanding – basic and diluted	7,483	7,474	9
Return on average assets	.92 %	.74 %	18 bp
Return on average equity	9.30 %	7.97 %	133 bp

bp = basis points.

The more significant components related to the Company’s results of operations are included below.

Interest Income

Interest income results from interest earned on earning assets, which primarily includes loans and investment securities. Interest income is affected by volume (average balance), the composition of earning assets, and the related rates earned on those assets. Total interest income for 2014 was $64.4 million, a decrease of $2.4 million or 3.6% compared to $66.7 million for 2013. The decrease in interest income was driven by lower interest from loans of $3.6 million or 6.7%, which was negatively impacted by both volume declines and a lower average rate earned. Interest income on investment securities increased $1.2 million or 9.2%, driven by higher volume. The decrease in loan volume has been accelerated by early payoffs of several larger balance commercial real estate credits. Volume declines also relate to the Company’s focus in recent years to strengthening is credit underwriting standards, which has improved the overall credit quality of the loan portfolio. As high quality loan demand has decreased, available funds have been redirected to investment securities or cash equivalents or to manage liquidity. Interest rates on loans continue to decrease, driven by a slow-growth economy and competitive factors combined with the Company's overall strategy to be more selective in pricing both its loans and deposits.

The overall interest rate environment at year-end 2014, as measured by the Treasury yield curve, remains at very low levels when compared with historical trends. The yield curve generally flattened in the comparable periods. Compared with year-end 2013, yields for three and six-month maturities were little changed. Two and three-year maturities increased 30 and 33 points, respectively. Yields on longer-term maturities decreased 84 and 121 basis points for the ten and thirty-year maturity periods, respectively. At year-end 2014, the short-term federal funds target interest rate remained between zero and 0.25%, unchanged since December 2008. The Federal Reserve Board ("Federal Reserve") has indicated that it will assess progress toward its objective of maximum employment and two percent inflation when determining how long to maintain this target rate. At December 31, 2014, the national and Kentucky unemployment rates were 5.6% and 5.7%, respectively. The national inflation rate was 0.8% at year-end 2014.

Interest Expense

Interest expense results from incurring interest on interest bearing liabilities, which are made up of interest bearing deposits, federal funds purchased, securities sold under agreements to repurchase, and other borrowed funds. Interest expense is affected by volume, composition of interest bearing liabilities, and the related rates paid on those liabilities. Total interest expense was $10.2 million for 2014, a decrease of $1.8 million or 15.4% compared to $12.0 million for 2013. The decrease in interest expense is attributed primarily to lower interest on deposits of $1.7 million or 28.2%. Both rate declines and lower volume contributed to the decrease, with a significant amount of the decrease related to time deposits. The Company has continued to aggressively reprice higher-rate maturing time deposits downward to lower market rates or to allow them to mature without renewal. Interest expense on long-term borrowings decreased $153 thousand or 2.6%, primarily due to principal repayments of $8.2 million on Federal Home Loan Bank ("FHLB") borrowings.

Net Interest Income

Net interest income is the most significant component of the Company's operating earnings. Net interest income is the excess of the interest income earned on earning assets over the interest paid for funds to support those assets. The two most common metrics used to analyze net interest income are net interest spread and net interest margin. Net interest spread represents the difference between the taxable equivalent yields on earning assets and the rates paid on interest bearing liabilities. Net interest margin represents the percentage of taxable equivalent net interest income to average earning assets. Net interest margin will exceed net interest spread because of the existence of noninterest bearing sources of funds, principally demand deposits and shareholders' equity, which are also available to fund earning assets. Changes in net interest income and margin result from the interaction between the volume and composition of earning assets, their related yields, and the associated cost and composition of the interest bearing liabilities. Accordingly, portfolio size, composition, and the related yields earned and the average rates paid have a significant impact on net interest spread and margin. The table following this discussion represents the major components of interest earning assets and interest bearing liabilities on a tax equivalent basis. To compare the tax-exempt asset yields to taxable yields, amounts in the table are adjusted to pretax equivalents based on the marginal corporate Federal tax rate of 35%.

Tax equivalent net interest income was $55.8 million for 2014, a decrease of $567 thousand or 1.0% compared to $56.4 million for 2013. Net interest margin was 3.36% for 2014, a decrease of four basis points from 3.40% for the prior year. The decrease in net interest margin was driven by a three basis point decline in net interest spread, which was 3.20% for 2014 compared to 3.23% for 2013.

The Company actively monitors and proactively manages the rate sensitive components of both its assets and liabilities in a continuously changing and difficult market environment. Competition in the Company's market areas continues to be intense, and market interest rates remain very low by historical measures. The Federal Reserve has maintained the short-term federal funds target rate at historic lows since December 2008, and has also indicated that it can be patient in beginning to normalize its stance on monetary policy.

Similar to the short-term federal funds target rate, the prime interest rate has not changed since December 2008. The Company uses the prime interest rate as part of its pricing model primarily on variable rate commercial real estate loans. The prime interest rate can have a significant impact on the Company's interest income on loans that reprice based on changes to this rate. The Company's variable interest rate loans contain provisions that limit the amount of increase or decrease in the interest rate during the life of a loan. This will limit the increase or decrease in interest income on loans that have interest rates tied to the prime interest rate. For 2014, the average yield earned on loans was 5.2%, which exceeded the prime interest rate of 3.25% at year-end. Predicting the direction and timing of future interest rates is uncertain.

For 2014, the average rate for two of the Company's most significant components of net interest income, loans and time deposits, both declined. The average rate earned on the Company's loan portfolio for 2014 declined 16 basis points to 5.2% and the average rate paid on time deposits decreased 20 basis points to 0.8% compared to 2013. The Company expects its net interest margin to remain flat or trend slightly down in the near term based on internal modeling using expectations about future market interest rates, loan volume, the maturity structure of the Company's earning assets and liabilities, and other factors. Future results, however, could be significantly different than expectations.

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

Years Ended December 31,	2014			2013			2012		
(In thousands)	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Earning Assets									
Investment securities									
Taxable	$509,087	$11,737	2.31 %	$477,626	$10,575	2.21 %	$532,197	$12,872	2.42 %
Nontaxable[1]	119,659	3,792	3.17	109,861	3,726	3.39	88,369	3,313	3.75
Interest bearing deposits with banks, federal funds sold and securities purchased under agreements to resell	63,863	143	.22	66,686	154	.23	66,757	160	.24
Loans [1,2,3]	968,489	50,318	5.20	1,006,662	53,944	5.36	1,035,959	56,639	5.47
Total earning assets	1,661,098	$65,990	3.97 %	1,660,835	$68,399	4.12 %	1,723,282	$72,984	4.24 %
Allowance for loan losses	(17,547)			(22,968)			(26,772)		
Total earning assets, net of allowance for loan losses	1,643,551			1,637,867			1,696,510		
Nonearning Assets									
Cash and due from banks	23,839			23,435			25,165		
Premises and equipment, net	35,745			36,319			37,612		
Other assets	95,190			108,037			100,659		
Total assets	$1,798,325			$1,805,658			$1,859,946		
Interest Bearing Liabilities									
Deposits									
Interest bearing demand	$320,947	$187	.06 %	$306,945	$216	.07 %	$281,076	$240	.09 %
Savings	357,156	580	.16	333,457	635	.19	311,724	626	.20
Time	433,756	3,486	.80	505,738	5,071	1.00	588,544	8,373	1.42
Federal funds purchased and other short-term borrowings	30,428	54	.18	29,440	74	.25	26,134	96	.37
	173,253	5,846	3.37	176,891	5,999	3.39	223,722	8,923	3.99

Securities sold under agreements to repurchase and other long-term borrowings									
Total interest bearing liabilities	1,315,540	$10,153	.77 %	1,352,471	$11,995	.89 %	1,431,200	$18,258	1.28 %
Noninterest Bearing Liabilities									
Demand deposits	281,025			256,518			238,443		
Other liabilities	24,872			27,979			25,697		
Total liabilities	1,621,437			1,636,968			1,695,340		
Shareholders' equity	176,888			168,690			164,606		
Total liabilities and shareholders' equity	$1,798,325			$1,805,658			$1,859,946		
Net interest income		55,837			56,404			54,726	
TE basis adjustment		(1,638)			(1,666)			(1,762)	
Net interest income		$54,199			$54,738			$52,964	
Net interest spread			3.20 %			3.23 %			2.96 %
Impact of noninterest bearing sources of funds			.16			.17			.22
Net interest margin			3.36 %			3.40 %			3.18 %

[1]Income and yield stated at a fully tax equivalent basis using the marginal corporate Federal tax rate of 35%.

[2]Loan balances include principal balances on nonaccrual loans.

[3]Loan fees included in interest income amounted to $1.3 million, $1.3 million, and $1.1 million for 2014, 2013, and 2012, respectively.

The following table is an analysis of the change in net interest income.

Analysis of Changes in Net Interest Income (tax equivalent basis)

(In thousands)	Variance 2014/2013[1]	Variance Attributed to Volume	Rate	Variance 2013/2012[1]	Variance Attributed to Volume	Rate
Interest Income						
Taxable investment securities	$ 1,162	$688	$474	$ (2,297)	$(1,244)	$(1,053)
Nontaxable investment securities[2]	66	318	(252)	413	752	(339)
Interest bearing deposits with banks, federal funds sold and securities purchased under agreements to resell	(11)	(5)	(6)	(6)	-	(6)
Loans[2]	(3,626)	(2,029)	(1,597)	(2,695)	(1,575)	(1,120)
Total interest income	(2,409)	(1,028)	(1,381)	(4,585)	(2,067)	(2,518)
Interest Expense						
Interest bearing demand deposits	(29)	8	(37)	(24)	26	(50)
Savings deposits	(55)	45	(100)	9	41	(32)
Time deposits	(1,585)	(659)	(926)	(3,302)	(1,064)	(2,238)
Federal funds purchased and other short-term borrowings	(20)	2	(22)	(22)	11	(33)
Securities sold under agreements to repurchase and other long-term borrowings	(153)	(119)	(34)	(2,924)	(1,702)	(1,222)
Total interest expense	(1,842)	(723)	(1,119)	(6,263)	(2,688)	(3,575)
Net interest income	$ (567)	$(305)	$(262)	$ 1,678	$621	$1,057
Percentage change	100.0 %	53.8 %	46.2 %	100.0 %	37.0 %	63.0 %

[1]The changes which are not solely due to rate or volume are allocated on a percentage basis using the absolute values of rate and volume variances as a basis for allocation.

[2]Income stated at fully tax equivalent basis using the marginal corporate Federal tax rate of 35%.

Provision for Loan Losses

The Company recorded a credit to the provision for loan losses in the amount of $4.4 million and $2.6 million for 2014 and 2013, respectively. The allowance for loan losses as a percentage of outstanding loans (net of unearned income) was 1.50% at December 31, 2014 compared to 2.06% at year-end 2013. The decrease in the provision for loan losses is attributed to continued improvement in the credit quality of the loan portfolio and a decline in loans outstanding. Further information about improvements in the Company's overall credit quality is included under the captions *"Allowance for Loan Losses"* and *"Nonperforming Loans"* that follows.

Net charge-offs were $2.2 million and $1.3 million for 2014 and 2013, respectively, up $977 thousand or 77.1%. The percentage increase is magnified by the relatively small prior year base amount. Net charge-offs were 0.23% of average loans outstanding for 2014 compared to 0.13% for the prior year.

Noninterest Income

The components of noninterest income are as follows for the periods indicated:

(Dollars in thousands) Years Ended December 31,	2014	2013	Increase (Decrease)	%
Service charges and fees on deposits	$7,801	$8,196	$ (395)	(4.8)%
Allotment processing fees	5,014	4,922	92	1.9
Other service charges, commissions, and fees	5,248	4,983	265	5.3
Trust income	2,568	1,993	575	28.9
Investment securities losses, net	(63)	(50)	(13)	26.0
Gain on sale of mortgage loans, net	490	1,036	(546)	(52.7)
Income from company-owned life insurance	1,231	962	269	28.0
Other	984	74	910	NM
Total noninterest income	$23,273	$22,116	$ 1,157	5.2 %

NM – not meaningful.

The more significant items impacting noninterest income are included below.

Service charges and fees on deposits decreased primarily due to lower overdraft fees of $325 thousand or 6.6%, reflecting a decrease in volume attributed in part to overall trends in consumer behavior.

Allotment processing fees are up 1.9% in the comparison. However, as disclosed in a current report on Form 8-K during December 2014 and summarized below, the Company anticipates allotment processing volumes will decline beginning in 2015.

The Company processes payments to unaffiliated third parties that are initiated under the U.S. military's allotment system. It processes payments by active duty and retired service members and civilians made to third party lenders that are paid through the military allotment system. The Company does not provide credit to individuals under the program.

The military discretionary allotment system in place prior to 2015 allowed service members to automatically direct a portion of their paycheck to financial institutions or people of their choosing to pay for various items or services. As announced by the U.S. Department of Defense ("DOD") in November 2014, starting January 1, 2015, active duty service members will no longer be able to enter into new contracts to purchase, lease, or rent tangible consumer items such as vehicles, appliances, and electronics using the military allotment system for payment. Contracts existing prior to January 1, 2015 are not affected. Payments for the purpose of savings, insurance premiums, mortgage and rent payments, support for dependents, or investments are also not affected. The new restrictions do not apply to military retirees or civilians.

Under the new DOD policy, we believe lending activity to service members by third party lenders will decline significantly as more restrictions are applied to the allotment repayment system. As a result, we anticipate new processing volume in 2015 will decrease, resulting in a decrease in our consolidated gross revenue of approximately $1.4 million or 1.5% for 2015 compared to 2014. We estimate that our consolidated net income could decline by approximately $810 thousand in 2015 when compared to 2014, after taking into account anticipated reductions in controllable allotment operating expenses and the impact of federal income taxes. However, the ultimate impact to revenue and net income is difficult to accurately predict, as third party lenders and other allotment payment recipients for whom we process continue to assess the impact of this newly implemented policy change.

The increase in other service charges, commissions, and fees is attributed primarily to higher interchange fees of $143 thousand or 5.1%. The increase in interchange fees relates to higher debit card transaction volumes. Loan servicing income is up $30 thousand or 6.3% as the mortgage loan servicing portfolio edged up during the year.

Trust fees for the current year were boosted by unusually large nonrecurring estate fees of $412 thousand during the last half of 2014. Overall, trust assets at year-end 2014 were up $19.9 million or 3.4% from a year ago.

The net loss on investment securities for 2014 includes $95 thousand attributed to a municipal bond issuer participating in the Build America Bond ("BAB") program. The issuer exercised its extraordinary redemption privilege, which was triggered by Federal budget sequestration events. Since the carrying value of the bond exceeded the par value due to unamortized premium, the Company recorded a loss on this investment during 2014. The prior year includes a $57 thousand loss attributed to premium amortization related to a single municipal bond of an issuer participating in the BAB program. The remaining unamortized premium of BAB investments at December 31, 2014 was $28 thousand, with the related carrying amount of the investments totaling $1.8 million.

The decrease in net gains on the sale of mortgage loans is due to lower origination and refinancing activity. The volume of loans sold in 2014 decreased $21.2 million or 42.4% compared to 2013. Mortgage refinancing and home purchases rose sharply during the middle to late 2012, fueled by interest rate declines. While mortgage interest rates remain relatively low, they have since increased and consumer demand has diminished.

The increase in income from company-owned life insurance was driven by a $276 thousand tax-free death benefit that exceeded the cash surrender value during the current-year third quarter.

The increase in other income relates mainly to the Company's equity interest in its tax credit partnerships. The Company recorded income of $358 thousand related to these partnerships for 2014 compared with a loss of $304 thousand in the prior year. The Company liquidated its interest in one of the partnerships during December 2014. The cumulative share of losses from the two remaining partnerships at year-end 2014 exceeded the amount invested, resulting in a carrying value of the partnerships of zero.

Noninterest Expense

The components of noninterest expense are as follows for the periods indicated:

(Dollars in thousands) Years Ended December 31,	2014	2013	Increase (Decrease)	%
Salaries and employee benefits	$29,763	$29,681	$ 82	0.3 %
Occupancy expenses, net	4,881	4,767	114	2.4
Equipment expenses	2,498	2,398	100	4.2
Data processing and communication expenses	4,031	3,946	85	2.2
Bank franchise tax	2,421	2,354	67	2.8
Amortization of intangibles	405	540	(135)	(25.0)
Deposit insurance expense	1,746	2,265	(519)	(22.9)
Other real estate expenses, net	5,318	6,999	(1,681)	(24.0)
Legal expenses	856	780	76	9.7
Other	7,359	7,843	(484)	(6.2)
Total noninterest expense	$59,278	$61,573	$ (2,295)	(3.7)%

The more significant items impacting noninterest expenses are included below.

Salaries and employee benefits were relatively unchanged in the comparison. Salary and related payroll taxes increased $614 thousand or 2.6%, but were partially offset by a $529 thousand or 9.0% decrease in benefit expenses. The decrease in benefit expenses was due both to lower claims related to the Company's self-funded health insurance plan and lower actuary-determined benefit expenses related to postretirement medical costs. Claims related to the self-funded health insurance for 2013 were unusually high in comparison to recent years. Postretirement benefit expenses decreased mainly due to lower service cost and amortization related to a net actuarial gain, each of which was influenced by the change to the discount rates used to determine the periodic benefit costs in the comparative years. The Company had 510 full time equivalent employees at year-end 2014, down from 519 a year earlier.

Amortization of intangible assets declined as a result of actuarial determined reductions related to core deposit and customer relationship intangible assets arising from previous business acquisitions. Intangible assets were $449 thousand at year-end 2014 and are scheduled to fully amortize by year-end 2015.

The decrease to deposit insurance expense for 2014 is primarily a result of the improved risk rating by the Federal Deposit Insurance Corporation ("FDIC") at the Company's bank subsidiaries. The improved ratings reduced the assessment rate used to determine the amount payable for deposit insurance.

The decrease in other real estate expenses was driven by lower impairment charges of $2.9 million or 52.4%. The decrease in impairment charges was partially offset by an increase in the net loss on property sales of $594 thousand and higher development, operating, and maintenance expenses of $617 thousand. The increase in development, operating, and maintenance expenses were primarily related to increasing the marketability of two real estate construction projects to better position them for sale.

The increase in legal expenses is attributed to several ongoing cases which are at various stages of the legal process and in which the Company may be either the plaintiff or defendant in actions arising from the ordinary course of business.

The decrease in other noninterest expense is attributed to ongoing cost saving efforts involving numerous line items and relatively small-dollar amounts along with lower costs associated with a downward trend in foreclosures and problem loans. The most significant decrease in noninterest expense relates to lower internet banking related expenses of $260 thousand or 31.1%.

Income Taxes

Income tax expense was $6.1 million for 2014, an increase of $1.7 million or 37.5% compared to $4.4 million for 2013. The effective income tax rates were 27.0% and 24.8% for 2014 and 2013, respectively. The increase in income tax expense and the effective tax rate for 2014 is attributed primarily to higher pretax income, which was driven by a higher proportion of taxable versus tax-exempt sources of revenue. The effective income tax rates are lower than the U.S. statutory federal rate of 35% primarily as a result of tax-exempt interest income from loans and investment securities, income from life insurance policies, and premium income associated with the Company's captive insurance subsidiary.

FINANCIAL CONDITION

Total assets of the Company were $1.8 billion at year-end 2014, down $26.9 million or 1.5% compared with year-end 2013. The overall financial condition of the Company, however, continued to improve. Total nonperforming assets were $67.9 million at year-end. While still elevated, nonperforming assets continued to decline during 2014, marking a decrease in nine consecutive quarters and resulting in the lowest level since the third quarter of 2009. While net interest margin tightened four basis points to 3.36%, loan quality metrics continued to improve throughout the year. Loan volume declined during the year, as generating high quality loans meeting our strong underwriting criteria remains a challenge. Regulatory capital levels remain significantly above the "well-capitalized" threshold, even after the redemption of $20.0 million, or two-thirds, of the Company's preferred stock during the year.

Temporary Investments

Temporary investments consist of interest bearing deposits in other banks and federal funds sold and securities purchased under agreements to resell. The Company uses these funds in the management of liquidity and interest rate sensitivity or as a short-term holding prior to subsequent movement into other investments with higher yields or for other purposes. At December 31, 2014, temporary investments were $74.1 million, an increase of $28.8 million or 63.6% compared to $45.3 million at year-end 2013.

Investment Securities

The investment securities portfolio is comprised primarily of residential mortgage-backed securities, tax-exempt securities of states and political subdivisions, and debt securities issued by U.S. government-sponsored agencies. Substantially all of the Company's investment securities are designated as available for sale. Total investment securities had a carrying amount of $630 million at year-end 2014, an increase of $16.5 million or 2.7% compared to $614 million at year-end 2013. Proceeds received from maturing or called investment securities not needed to fund higher-earning loans are either reinvested in similar investments or used to manage liquidity, such as for deposit outflows or other payment obligations. The Company periodically sells investment securities in response to its overall asset/liability management strategy to lock in gains, increase yield, restructure expected future cash flows, and/or enhance its capital position.

The increase in investment securities was driven primarily by a $13.5 million increase in the market value adjustment related to securities classified as available for sale. The increase in the value of the available for sale securities portfolio is attributed to a general shift upward in bond prices, primarily for the five-year and longer maturity periods. Bond prices, mainly on the longer dated maturities, began to rise during the first quarter of 2014 and the overall yield curve flattened at year-end 2014 compared to a year earlier. In general, as market interest rates decrease, the value of fixed rate investments increase. Net purchases of investment securities were $7.0 million for 2014. Net premium amortization was $4.0 million for 2014 compared to $5.0 million for 2013.

At year-end 2014, investment securities included $5.9 million amortized cost amounts of single-issuer trust preferred capital securities of a U.S. based global financial services firm with an estimated fair value of $5.5 million, up from $4.8 million at year-end 2013. These securities reached a twelve-month high price point during the third quarter, and at year-end remained near its high price point for the year. The investment continues to perform according to contractual terms and is rated as investment grade by major rating agencies. The issuer of the securities announced in the first quarter of 2014 an increase in per share common dividend payments and authorization of a common equity repurchase plan. The Company does not intend to sell its investment in these securities, nor does the Company believe it is likely that it will be required to sell these securities prior to their anticipated recovery. The Company believes these securities are not impaired due to reasons of credit quality or other factors, but rather the unrealized loss is primarily attributed to general uncertainties in both international and domestic economies and continuing market volatility. The Company believes that it will collect all amounts due according to the contractual terms of these securities and that the fair values of these securities will continue to recover as they approach their maturity dates.

The Company attributes the unrealized losses in other sectors of the investment securities portfolio to changes in market interest rates and volatility, and thus identifies them as temporary. As discussed further above, market interest rates generally decreased throughout 2014, particularly those associated with longer dated maturities. Investment securities with an unrealized loss at December 31, 2014 are performing according to their contractual terms, and the Company does not expect to incur a loss on these securities unless they are sold prior to maturity. The Company does not have the intent to sell these securities nor does it believe it is likely that it will be required to sell these securities prior to their anticipated recovery. The Company does not consider any of the securities to be impaired due to reasons of credit quality or other factors. All investment securities in the Company’s portfolio are currently performing.

Funds made available from sold, matured, or called bonds are redirected to fund higher yielding loan growth when available, reinvested to purchase additional investment securities, or otherwise employed to improve the composition of the balance sheet and liquidity. The purchase of nontaxable obligations of states and political subdivisions is one of the primary means of managing the Company’s tax position. The impact of the alternative minimum tax related to the Company’s ability to acquire tax-free obligations at an attractive yield is routinely monitored. The Company does not have direct exposure to the subprime mortgage market. The Company does not originate subprime mortgages nor has it invested in bonds that are secured by such mortgages.

The following table summarizes the carrying values of investment securities on December 31, 2014, 2013, and 2012. The investment securities are divided into available for sale and held to maturity securities. Available for sale securities are carried at estimated fair value and held to maturity securities are carried at amortized cost. Corporate debt securities consist primarily of debt issued by a large global financial services firm. Mutual funds and equity securities are attributed to the Company’s captive insurance subsidiary.

December 31,	2014		2013		2012	
	Available	Held to	Available	Held to	Available	Held to
(In thousands)	for Sale	Maturity	for Sale	Maturity	for Sale	Maturity
Obligations of U.S. government-sponsored entities	$109,448	$ -	$93,750	$ -	$76,095	$ -

Obligations of states and political subdivisions	135,766	3,728	131,970	765	118,755	820
Mortgage-backed securities – residential	370,489	-	378,077	-	370,439	-
Mortgage-backed securities – commercial	2,512	-	689	-	-	-
Corporate debt securities	6,307	-	6,257	-	5,826	-
Mutual funds and equity securities	1,866	-	2,077	-	1,993	-
Total	$626,388	$ 3,728	$612,820	$ 765	$573,108	$ 820

The following table presents an analysis of the contractual maturity and tax equivalent weighted average interest rates of investment securities at December 31, 2014. Available for sale securities are stated at estimated fair value and held to maturity securities are stated at amortized cost. Mortgage-backed securities are included in maturity categories based on their stated maturity dates. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations. Mutual funds and equity securities are attributed to the Company's captive insurance subsidiary. These investments have no stated maturity date and are not included in the maturity schedule that follows.

Available for Sale

	Within One Year		After One But Within Five Years		After Five But Within Ten Years		After Ten Years	
(In thousands)	Amount	Rate	Amount	Rate	Amount	Rate	Amount	Rate
Obligations of U.S. government-sponsored entities	$-	- %	$71,392	1.1 %	$36,219	2.2 %	$1,837	2.9 %
Obligations of states and political subdivisions	7,763	2.4	72,990	2.6	46,753	3.3	8,260	5.2
Mortgage-backed securities – residential	-	-	-	-	72,106	1.6	298,383	2.7
Mortgage-backed securities – commercial	-	-	-	-	723	2.3	1,789	1.4
Corporate debt securities	207	3.1	551	3.8	24	4.0	5,525	2.0
Total	$7,970	2.4 %	$144,933	1.9 %	$155,825	2.3 %	$315,794	2.8 %

Held to Maturity

	Within One Year		After One But Within Five Years		After Five But Within Ten Years		After Ten Years	
(In thousands)	Amount	Rate	Amount	Rate	Amount	Rate	Amount	Rate
Obligations of states and political subdivisions	$ -	- %	$ -	- %	$705	4.4 %	$3,023	3.7 %

The calculation of the weighted average interest rates for each category is based on the weighted average amortized cost of the securities. The weighted average tax rates on exempt state and political subdivisions are computed based on the marginal corporate Federal tax rate of 35%.

Loans

Loans, net of unearned income, were $932 million at December 31, 2014, a decrease of $67.9 million or 6.8% compared to year-end 2013. High quality loan demand remains weak, and the Company continues a measured and cautious approach to loan originations while working to further reduce its level of nonperforming assets in an improving, but slow-growth economy. Generating high quality loans continues to be a challenge, and the decrease in outstanding loans has been accelerated by early payoffs of several larger balance credits. The large early payoffs relate primarily to nonbank competitors willing to offer nonrecourse and other terms that are significantly below the Company's underwriting standards. Other significant factors contributing to the decrease in loans include the migration of nonaccrual loans to OREO in the amount of $8.3 million and principal paydowns on nonaccrual and performing restructured loans of $7.8 million and $1.1 million, respectively.

The composition of the loan portfolio is summarized in the table that follows. Based on economic forecasts and other available information, the Company expects further improvements to the local and regional economy during 2015. An improving economy, particularly where the labor force participation rates increase, could slow the rate of decline experienced in outstanding loan balances in recent years or result in incremental loan growth.

December 31, (In thousands)	2014	%	2013	%	2012	%	2011	%	2010	%
Commercial, financial, and agricultural	$85,028	9.1 %	$92,827	9.3 %	$87,440	8.7 %	$93,807	8.7 %	$108,959	9.1 %
Real estate mortgage – construction and land development	97,045	10.4	101,352	10.1	102,454	10.2	119,989	11.2	154,208	12.9
Real estate mortgage – residential	361,022	38.7	371,582	37.2	368,762	36.7	397,357	37.1	424,995	35.6
Real estate mortgage – farmland and other commercial enterprises	375,277	40.3	418,147	41.8	425,477	42.3	432,438	40.3	461,182	38.7
Installment	13,413	1.5	15,092	1.5	18,247	1.8	21,365	2.0	28,532	2.4
Lease financing	158	-	883	.1	2,615	.3	7,152	.7	14,964	1.3
Total	$931,943	100.0%	$999,883	100.0%	$1,004,995	100.0%	$1,072,108	100.0%	$1,192,840	100.0%

On an average basis, loans represented 58.3% of earning assets for 2014, a decrease of 231 basis points compared to 60.6% for 2013. As loan demand changes, available funds are reallocated between temporary investments or investment securities, which typically involve a decrease in credit risk and result in lower yields. The Company does not have direct exposure to the subprime mortgage market. The Company does not originate subprime mortgages nor has it invested in bonds that are secured by such mortgages. Subprime mortgage lending is defined by the Company generally as lending to a borrower that would not qualify for a mortgage loan at prevailing market rates or whereby the underwriting decision is based on limited or no documentation of the ability to repay.

The following table presents the amount of commercial, financial, and agricultural loans and loans secured by real estate outstanding at December 31, 2014 which, based on remaining scheduled repayments of principal, are due in the periods indicated.

Loan Maturities

(In thousands)	Within One Year	After One But Within Five Years	After Five Years	Total
Commercial, financial, and agricultural	$21,818	$30,480	$32,730	$85,028
Real estate mortgage – construction and land development	50,332	28,900	17,813	97,045
Real estate mortgage – residential	28,242	88,206	244,574	361,022
Real estate mortgage – farmland and other commercial enterprises	47,921	163,372	163,984	375,277
Total	$148,313	$310,958	$459,101	$918,372

The table below presents the amount of commercial, financial, and agricultural loans and loans secured by real estate outstanding at December 31, 2014 that are due after one year, classified according to sensitivity to changes in interest rates.

Interest Sensitivity

(In thousands)	Fixed Rate	Variable Rate
Due after one but within five years	$283,008	$27,950
Due after five years	89,493	369,608
Total	$372,501	$397,558

Asset Quality

The Company's loan portfolio is subject to varying degrees of credit risk. Credit risk is mitigated by diversification within the portfolio, limiting exposure to any single customer or industry, rigorous lending policies and underwriting criteria, and collateral requirements. The Company maintains policies and procedures to ensure that the granting of credit is done in a sound and consistent manner. This includes policies on a company-wide basis that require certain minimum standards to be maintained by its subsidiary banks. However, the policies also permit the subsidiary companies authority to adopt standards that are no less stringent than those included in the company-wide policies. Credit decisions are made at the subsidiary bank level under guidelines established by policy. The Company's internal audit department performs loan reviews at each subsidiary bank during the year. This review evaluates loan administration, credit quality, documentation, compliance with Company loan standards, and the adequacy of the allowance for loan losses on a consolidated and subsidiary basis.

The provision for loan losses represents charges or credits made to earnings to maintain an allowance for loan losses at a level considered adequate to provide for probable incurred credit losses at the balance sheet date. The allowance for loan losses is a valuation allowance increased by the provision for loan losses and decreased by net charge-offs. Loan losses are charged against the allowance when management believes the uncollectibility of a loan is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses and related provision for loan losses generally fluctuate relative to the level of nonperforming and impaired loans, but other factors impact the amount of the allowance. The Company estimates the adequacy of the allowance using a risk-rated methodology based on the Company's past loan loss experience, known and inherent risks in the loan portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral securing loans, composition of the loan portfolio, current economic conditions, and other relevant factors. This evaluation is inherently subjective as it requires significant judgment and the use of estimates that may be susceptible to change.

The allowance for loan losses consists of specific and general components. The specific component relates to loans that are individually classified as impaired. The general component covers non-impaired loans and is based on historical loss experience adjusted for current risk factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off. Actual loan losses could differ significantly from the amounts estimated by management.

The Company's risk-rated methodology includes segregating non-impaired watch list and past due loans from the general portfolio and allocating a loss percentage to these loans depending on their status. For example, watch list loans, which may be identified by the internal loan review risk-rating process or by regulatory examiner classification, are assigned a certain loss percentage while loans past due 30 days or more are assigned a separate loss percentage. Each of these loss rates considers past experience as well as current factors. The remainder of the general loan portfolio is segregated into portfolio segments having similar risk characteristics identified as follows: real estate loans, commercial loans, and consumer loans. Each of these portfolio segments is assigned a loss percentage based on their respective sixteen quarter rolling historical loss rates, adjusted for qualitative risk factors.

The qualitative risk factors used in the methodology are consistent with the guidance in the most recent Interagency Policy Statement on the Allowance for Loan Losses issued. Each factor is supported by a detailed analysis performed at each subsidiary bank and is both measureable and supportable. Some factors include a minimum allocation in some instances where loss levels are extremely low and it is determined to be prudent from a safety and soundness perspective. Qualitative risk factors that are used in the methodology include the following for each loan portfolio segment:

Delinquency trends	Management experience risk
Trends in net charge-offs	Concentration of credit risk
Trends in loan volume	Economic conditions risk
Lending philosophy risk	

A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

While the overall economy improved in 2014, the Company continues to face headwinds related to its level of nonperforming assets that built up following the deep recession of 2007 to 2009. The economic decline resulted in significant deterioration in the Company's credit quality and collateral values, primarily in residential real estate lending. Credit quality has improved significantly over the last few years, as loan underwriting standards have been strengthened and nonperforming asset levels have declined nearly 50% from the peak that occurred in 2010. Many key economic measures are improving, although overall economic growth remains slow. Foreclosure rates in Kentucky are at the lowest rate since 2007. Housing starts have stabilized and have moderately increased since bottoming out in 2009. At year-end 2014, the national and Kentucky unemployment rate was 5.6% and 5.7%, respectively. Unemployment rates have improved significantly from a year ago, but labor force participation rates remain near 30-year lows. Many of those newly hired consist of part-time workers.

The continued improvement in the credit quality of the loan portfolio has further reduced the level of nonperforming assets, which have marked nine consecutive quarterly declines and are the lowest since 2009. Nonperforming loans were $35.9 million at year-end, a decrease of $72.0 million or 66.7% since peaking at $108 million in the first quarter of 2010. The Company includes accruing restructured loans as a component of its nonperforming loans. Such loans were $24.4 million at year-end 2014 and account for 68.0% of nonperforming loans. Of the $24.4 million in accruing restructured loans, $20.3 million consist of three larger-balance credit relationships secured by various types of real estate collateral. Nonaccrual loans were $11.5 million at year-end 2014, down $12.3 million or 51.7% for the year. Despite improvement, nonperforming assets remain elevated at 3.8% of total assets. High levels of nonperforming assets generally result in loan charge-offs, provisions for loan losses, and impairment charges on repossessed real estate. The Company works with its loan customers on an individual case-by-case basis in order to maximize loan repayments on its challenged credits and typically does not restructure those that are past due.

Impaired loans are those in which the Company does not expect to receive full payment under the contractual terms. Impaired loans are measured at the present value of expected future cash flows discounted at the loan's effective interest rate, at the loan's observable market price, or at the fair value of the collateral taking into consideration estimated costs to sell if the loan is collateral dependent. Collateral values are updated in accordance with policy guidelines by obtaining independent third party appraisals and monitoring sales activity of similar properties in our market area.

At year-end 2014, the Company had $3.4 million in specific reserves allocated to impaired loans. Of this total, $1.3 million or 38.9% is attributed to a group of loans to a single creditor totaling $7.9 million secured by a combination of a real estate development and residential real estate properties. This group of collateral dependent loans is classified as performing restructured loans at year-end 2014.

The Company recorded a credit to the provision for loan losses of $4.4 million in 2014, or $1.8 million higher than the $2.6 million recorded in 2013. The increased credit is due to further improvement in the credit quality of the loan portfolio combined with a $67.9 million or 6.8% decline in loans outstanding. Historical loss rates, adjusted for current risk factors, have improved due to lower recent charge-off activity that has replaced higher levels that had been included in the early part of the Company’s look-back period used in its allowance for loan losses methodology. The decrease in historical loss rates and charge-off activity is due primarily to stabilizing real estate values, which serves as collateral for nearly 90% of the Company’s loan portfolio. The rapid declines in real estate values experienced beginning in 2008 and continuing through 2011 have leveled off significantly, and the allowance for loan losses reflects this improvement. The Company has also implemented stronger credit underwriting standards in recent years, which has improved overall credit quality measures.

Certain credit quality measures are summarized in the table that follows for the periods indicated. Each of these measures is at the best level in the last three years.

(In thousands) December 31,	2014	2013	2012	Three-year High[1]	Three-year Low[1]
Nonperforming loans	$35,937	$50,537	$53,860	$78,959	$ 35,937
Nonaccrual loans	11,508	23,838	27,408	61,358	11,508
Loans past due 30-89 days and still accruing	1,352	1,460	5,140	11,940	1,352
Loans graded substandard or below	52,313	75,688	90,855	135,337	52,313
Impaired loans	43,955	58,339	63,889	100,726	43,955
Loans, net of unearned income	931,943	999,883	1,004,995	1,046,561	931,943

[1]Based on quarter-end balances over the previous three years.

Net charge-offs were $2.2 million for 2014, an increase of $977 thousand or 77.1% compared to 2013. The percentage increase in net charge-offs is magnified by the relatively small prior year base amount. Net charge-offs were 0.23% of average loans outstanding for 2014 compared to 0.13% for the prior year. Net charge-offs for the current and prior year are each well below the $14.2 million peak which occurred in the early part of the post-recession period of 2009. The allowance for loan losses as a percentage of outstanding loans was 1.50% and 2.06% at year-end 2014 and 2013, respectively. As a percentage of nonperforming loans, the allowance for loan losses was 38.9% and 40.7% at year-end 2014 and 2013, respectively.

The relatively low amount of the allowance for loan losses as a percentage of nonperforming loans is due mainly to the makeup of nonperforming loans, where performing restructured loans represent 68.0% of total nonperforming loans outstanding at year-end 2014. The allowance attributed to credits that are restructured with lower interest rates generally represents the difference in the present value of future cash flows calculated at the loan's original effective interest rate and the new lower rate. This typically results in a reserve for loan losses that is less severe than for other loans that are collateral dependent. The allowance specifically allocated to impaired loans was $3.4 million or 7.7% of such loans at year-end 2014 compared with $4.1 million or 7.0% a year earlier.

The allowance for loan losses as a percentage of nonaccrual loans was 121% and 86.3% at year-end 2014 and 2013, respectively. Charge-offs on nonaccrual loans have occurred mainly as a result of the Company's ongoing effort to appropriately value the collateral securing these loans through timely appraisals and evaluating the overall financial condition of the borrower.

The table below summarizes the loan loss experience for the past five years.

Allowance For Loan Losses

Years Ended December 31, (In thousands)	2014	2013	2012	2011	2010
Balance of allowance for loan losses at beginning of year	$20,577	$24,445	$28,264	$28,784	$23,364
Loans charged off:					
Commercial, financial, and agricultural	1,630	257	216	1,113	869
Real estate mortgage - construction and land development	50	251	2,549	6,785	7,599
Real estate mortgage - residential	956	908	2,508	4,225	1,521
Real estate mortgage - farmland and other commercial enterprises	870	274	1,823	2,768	1,557
Installment	214	281	441	452	709
Lease financing	32	-	99	10	135
Total loans charged off	3,752	1,971	7,636	15,353	12,390
Recoveries of loans previously charged off:					
Commercial, financial, and agricultural	782	143	105	211	181
Real estate mortgage - construction and land development	292	70	102	6	2
Real estate mortgage - residential	185	200	246	192	42
Real estate mortgage - farmland and other commercial enterprises	147	57	318	43	28
Installment	97	221	234	245	286
Lease financing	4	12	40	649	38
Total recoveries	1,507	703	1,045	1,346	577
Net loans charged off	2,245	1,268	6,591	14,007	11,813
Amount (credited) charged to provision for loan losses	(4,364)	(2,600)	2,772	13,487	17,233
Balance at end of year	$13,968	$20,577	$24,445	$28,264	$28,784
Average loans net of unearned income	$968,489	$1,006,662	$1,035,959	$1,130,273	$1,236,202
Ratio of net charge-offs during year to average loans, net of unearned income	0.23 %	0.13 %	0.64 %	1.24 %	.96 %

The following table presents an estimate of the allocation of the allowance for loan losses by type for the dates indicated. Although specific allocations exist, the entire allowance is available to absorb losses in any particular category.

December 31, (In thousands)	2014		2013		2012		2011		2010	
	Amount	% of Respective	Amount	% of Respective	Amount	% of Respective	Amount	% of Respective	Amount	% of Respective

		Loan Category			Loan Category			Loan Category			Loan Category			Loan Category	
Commercial, financial, and agricultural	$1,146	1.35	%	$1,389	1.50	%	$1,475	1.69	%	$3,268	3.48	%	$2,876	2.64	%
Real estate mortgage – construction and land development	1,809	1.86		2,567	2.53		3,498	3.41		6,089	5.07		10,367	6.72	
Real estate mortgage – residential	4,778	1.32		6,200	1.67		6,184	1.68		11,111	2.80		10,017	2.36	
Real estate mortgage – farmland and other commercial enterprises	5,955	1.59		9,949	2.38		12,572	2.95		6,338	1.47		4,143	.90	
Installment	273	2.04		452	2.99		678	3.72		1,218	5.70		997	3.49	
Lease financing	7	4.43		20	2.27		38	1.45		240	3.36		384	2.57	
Total	$13,968	1.50	%	$20,577	2.06	%	$24,445	2.43	%	$28,264	2.64	%	$28,784	2.41	%

Additional information concerning the Company’s asset quality is presented under the caption *“Nonperforming Assets”* which follows and *“Investment Securities”* beginning on page 49.

Nonperforming Assets

The Company's nonperforming assets consist of nonperforming loans, OREO, and other foreclosed assets. Nonperforming loans include nonaccrual loans, performing restructured loans, and loans 90 days or more past due and still accruing interest. Nonaccrual loans are considered to be an indicator of potential future losses. The accrual of interest on loans is discontinued when it is determined that the collection of interest or principal is doubtful, or when a default of interest or principal has existed for 90 days or more, unless such loan is well secured and in the process of collection. Restructured loans occur when a lender, because of economic or legal reasons related to a borrower's financial difficulty, grants a concession to the borrower that it would not otherwise consider. Restructured loans typically include a reduction of the stated interest rate or an extension of the maturity date. The Company gives careful consideration to identifying which of its challenged credits merit a restructuring of terms that it believes will result in maximum loan repayments and mitigate possible losses. Cash flow projections are carefully scrutinized prior to restructuring any credits; past due credits are typically not granted concessions. There were no new credits restructured during 2014.

Nonperforming assets were $67.9 million at year-end 2014, a decrease of $20.4 million or 23.1% compared to $88.4 million at year-end 2013. Such assets have been reduced to the lowest level since peaking at $135 million in the first quarter of 2010. Nonperforming assets increased sharply during 2009 mainly as a result of prolonged weaknesses in the overall economy.

Nonperforming assets by category are presented in the table below for the dates indicated.

December 31, (In thousands)	2014		2013		2012		2011		2010	
Loans accounted for on nonaccrual basis	$11,508		$23,838		$27,408		$59,755		$53,971	
Loans past due 90 days or more and still accruing	-		444		103		1		42	
Restructured loans	24,429		26,255		26,349		19,125		36,978	
Total nonperforming loans	35,937		50,537		53,860		78,881		90,991	
Other real estate owned	31,960		37,826		52,562		38,157		30,545	
Other foreclosed assets	52		-		-		36		34	
Total nonperforming assets	$67,949		$88,363		$106,422		$117,074		$121,570	
Ratio of total nonperforming loans to total loans (net of unearned income)	3.9	%	5.1	%	5.4	%	7.4	%	7.6	%
Ratio of total nonperforming assets to total assets	3.8		4.9		5.9		6.2		6.3	

Additional details related to nonperforming loans were as follows at year-end 2014 and 2013:

Nonperforming Loans

December 31, (In thousands)	2014	2013
Nonaccrual Loans		
Commercial, financial, and agriculture	$88	$160
Real estate mortgage - construction and land development	3,744	5,821
Real estate mortgage - residential	3,474	5,154
Real estate mortgage - farmland and other commercial enterprises	4,202	12,677
Installment	-	4
Lease financing	-	22
Total nonaccrual loans	$11,508	$23,838
Restructured Loans		
Real estate mortgage - construction and land development	$3,742	$4,391
Real estate mortgage - residential	4,674	4,826
Real estate mortgage - farmland and other commercial enterprises	16,004	16,987
Installment	9	51
Total restructured loans	$24,429	$26,255
Past Due 90 Days or More and Still Accruing		
Real estate mortgage - residential	$-	$10
Real estate mortgage - farmland and other commercial enterprises	-	434
Total past due 90 days or more and still accruing	$-	$444
Total nonperforming loans	$35,937	$50,537

The most significant components of nonperforming loans include nonaccrual and restructured loans. Activity during 2014 related to these two components was as follows:

(In thousands)	Nonaccrual Loans	Restructured Loans
Balance at December 31, 2013	$ 23,838	$ 26,255
Loans placed on nonaccrual status	6,178	(450)
Principal paydowns	(7,820)	(1,067)
Transfers to other real estate owned	(8,251)	-
Charge-offs	(1,049)	(37)
Reclassification between nonperforming categories	(7)	7
Reclassified to performing status	(1,381)	(279)
Balance at December 31, 2014	$ 11,508	$ 24,429

The Company gives careful consideration to identifying which of its challenged credits merit a restructuring of terms that it believes will result in maximum loan repayments and mitigate possible losses. From time to time the Company may modify a customer's loan, but such modifications may or may not meet the criteria for classification as a restructured troubled debt. Modifications that do not meet the criteria of a troubled debt include:

- repricing a loan to a current market rate of interest to a borrower with good credit and adequate collateral value in order to retain the customer;
- changing the payment frequency from monthly to quarterly, semi-annually, or annually where the loan is performing, the borrower has good credit and adequate collateral value, and the Company believes valid reasons exist for the change; or
- extending the interest only payment period of a performing loan where the borrower has good credit and adequate collateral value in instances where a project may still be in a phase of development or leasing-up, and where the Company believes completion will occur in the near future, or such extension is otherwise in the Company's best interest.

As modifications are made, management evaluates whether the modification meets the criteria to be classified as a troubled debt. These criteria include two components:

1. The bank makes a concession on the loan terms that it would not otherwise consider, and
2. The borrower is experiencing financial difficulty.

The Company’s loan policy provides guidance to its lending personnel regarding restructured loans to ensure those that are troubled debt are properly identified. Additional attention is given to restructured loans through the oversight of the Chief Credit Officer at the Parent Company to ensure that modifications meeting criteria for restructured loans are identified and properly reported.

The table below sets forth on an aggregate basis at December 31, 2014, the types of non-troubled debt restructurings by loan type, number of loans, average loan balance and modification type:

# of Loans	Loan Type	Average Loan Balance (in thousands)	Range of Loan Balances (in thousands)	Modification Type
91	Real estate mortgage - residential	$ 206	$24 – $4,214	lowered interest rate to market rate to retain loan
35	Real estate mortgage – farmland and other commercial enterprises	580	12 – 4,304	lowered interest rate to market rate to retain loan
3	Commercial	15	5 – 29	lowered interest rate to market rate to retain loan
3	Consumer	10	7 – 13	lowered interest rate to market rate to retain loan

In each of the modifications identified in the table above, management determined the loan was not in troubled condition due to the financial condition of the borrower and related collateral.

The Company has not engaged in loan splitting. Loan splitting is a practice that may occur in work-out situations whereby a loan is divided into two parts – a performing part and a nonperforming part. This benefits a lender by potentially replacing one impaired loan by one smaller good loan and one smaller bad loan. Overall charge-offs and reserve amounts are potentially reduced and the effects of adverse loan classifications may be diminished.

The Company's comprehensive risk-grading and loan review program includes a review of loans to assess risk and assign a grade to those loans, a review of delinquencies, and an assessment of loans for needed charge-offs or placement on nonaccrual status. The Company had loans in the amount of $64.7 million and $79.0 million at year-end 2014 and year-end 2013, respectively, which were performing but considered potential problem loans and are not included in the nonperforming loan totals in the tables above. These loans, however, are considered in establishing an appropriate allowance for loan losses. The balance outstanding for potential problem credits is mainly a result of lingering weaknesses in the overall economy that continue to strain some of the Company's customers. Potential problem loans include a variety of borrowers and are secured primarily by various types of real estate including commercial, construction properties, and residential real estate developments. The $14.3 million or 18.1% decrease since year-end in the level of potential problem loans is attributed primarily to an overall improvement in credit quality similar to that of the overall portfolio. At December 31, 2014, the five largest potential problem credits were $13.9 million in the aggregate compared to $16.7 million at year-end 2013 and secured by various types of real estate including commercial, construction properties, and residential real estate development.

Potential problem loans are identified on the Company's watch list and consist of loans that require close monitoring by management. Credits may be considered as a potential problem loan for reasons that are temporary or correctable, such as for a deficiency in loan documentation or absence of current financial statements of the borrower. Potential problem loans may also include credits where adverse circumstances are identified that may affect the borrower's ability to comply with the contractual terms of the loan. Other factors which might indicate the existence of a potential problem loan include the delinquency of a scheduled loan payment, deterioration in a borrower's financial condition identified in a review of periodic financial statements, a decrease in the value of the collateral securing the loan, or a change in the economic environment in which the borrower operates. Certain loans on the Company's watch list are also considered impaired and specific allowances related to these loans are established in accordance with the appropriate accounting guidance.

Other real estate owned includes real estate properties acquired by the Company through, or in lieu of, actual loan foreclosures. At year-end 2014, OREO was $32.0 million, a decrease of $5.9 million or 15.5% compared to $37.8 million at year-end 2013. OREO has declined $20.6 million or 39.2% from its peak of $52.6 million, which occurred at year-end 2012.

OREO activity for 2014 was as follows:

(In thousands)	Amount
Balance at December 31, 2013	$37,826
Transfers from loans and other increases	8,874
Proceeds from sales	(11,336)
Net loss on sales	(776)
Write downs and other decreases, net	(2,628)
Balance at December 31, 2014	$31,960

The reduction in OREO was driven by property sales and impairment charges of $12.1 million and $2.6 million, respectively, which more than offset new acquisitions. Five larger-balance properties with a carrying value of $7.6 million in the aggregate were sold during 2014. This includes three real estate development projects totaling $3.9 million, one commercial real estate properties totaling $3.0 million, and one property secured primarily by residential real estate of $646 thousand. Impairment charges include $847 thousand related to two residential real estate development projects that ended the year with a carrying value of $2.5 million in the aggregate, which represents the projects appraised value less estimated selling costs. The Company's had four OREO properties at year-end 2014 with a carrying amount in excess of $2.0 million each: one consists of a residential real estate development project with a carrying value of $2.0 million, two separate commercial real estate properties totaling $4.7 million in the aggregate, and one commercial rental real estate property of $2.6 million.

Deposits

The Company’s primary source of funding for its lending and investment activities results from its customer deposits, which consist of noninterest and interest bearing demand, savings, and time deposits. A summary of the Company’s deposits is presented in the table that follows. The decrease in time deposits is a result of the Company’s high liquidity position and from its strategy to lower overall funding costs, mainly by allowing higher-rate certificates of deposit to roll off or reprice at significantly lower interest rates. Many of those balances have been moved into interest or noninterest bearing demand accounts or savings accounts by the customer. As rates have decreased throughout the deposit portfolio, many customers have opted to transfer funds from maturing time deposits or investments from other sources into short-term demand or savings accounts. The Company has not sought out or accepted brokered deposits in the past nor does it have plans to do so in the future.

A summary of the Company’s deposits is as follows for the dates indicated:

December 31, (In thousands)	2014	2013	Increase (Decrease)
Noninterest Bearing	$292,788	$277,294	$ 15,494
Interest Bearing			
Demand	335,657	320,503	15,154
Savings	363,185	340,903	22,282
Time	395,531	471,515	(75,984)
Total interest bearing	1,094,373	1,132,921	(38,548)
Total deposits	$1,387,161	$1,410,215	$ (23,054)

A summary of average balances for deposits by type and the related weighted average rates paid is as follows for the periods presented:

Years Ended December 31,	2014			2013			2012		
(In thousands)	Average Balance	Average Rate Paid		Average Balance	Average Rate Paid		Average Balance	Average Rate Paid	
Noninterest bearing demand	$281,025	-	%	$256,518	-	%	$238,443	-	%
Interest bearing demand	320,947	.06		306,945	.07		281,076	.09	
Savings	357,156	.16		333,457	.19		311,724	.20	
Time	433,756	.80		505,738	1.00		588,544	1.42	
Total interest bearing	1,111,859	.38		1,146,140	.52		1,181,344	.78	
Total	$1,392,884	.31	%	$1,402,658	.42	%	$1,419,787	.65	%

Maturities of time deposits of $100,000 or more outstanding at December 31, 2014 are summarized as follows:

(In thousands)	Amount
3 months or less	$26,548
Over 3 through 6 months	22,299
Over 6 through 12 months	30,018
Over 12 months	50,568
Total	$129,433

Short-term Borrowings

Short-term borrowings include funding sources with an original maturity of one year or less. The Company's short-term borrowings consist of federal funds purchased and securities sold under agreements to repurchase, which are generally on an overnight basis. A summary of short-term borrowings is as follows:

(In thousands)	2014	2013	2012
Amount outstanding at year-end	$28,590	$29,123	$24,083
Maximum month-end balance during the year	33,568	32,885	31,632
Average outstanding	30,428	29,440	26,134
Weighted average rate during the year	.18 %	.25 %	.37 %
Weighted average rate at year-end	.16	.25	.29

Long-term Borrowings

Long-term borrowings include funding sources with an original maturity greater than one year. The Company's long-term borrowings are comprised of securities sold under agreements to repurchase, FHLB advances, and subordinated notes payable to unconsolidated trusts. Long-term securities sold under agreements to repurchase primarily represent obligations related to the Company's balance sheet leverage transaction that originated in 2007. In this transaction, the Company borrowed $200 million through multiple fixed rate repurchase agreements and used the proceeds to purchase fixed rate Government National Mortgage Association ("GNMA") bonds that are pledged as collateral. The Company is required to secure the borrowed funds with GNMA bonds valued at 106% of the outstanding principal balance of the borrowings. Principal payments have reduced the outstanding balance of the obligation to $100 million at year-end 2014, with a weighted average interest rate of 3.95%. These borrowings are callable quarterly and mature in November 2017.

The Company has $763 thousand of other long-term repurchase agreements outstanding at year-end 2014 made in the ordinary course of business with commercial customers. These borrowings have a weighted average fixed rate of 1.17% with portions maturing during 2015 and 2016.

FHLB advances to the Company's subsidiary banks are secured by restricted holdings of FHLB stock which participating banks are required to own as well as certain mortgage loans as required by the FHLB. FHLB advances are made pursuant to several different credit programs, which have their own interest rates and range of maturities. Interest rates on FHLB advances are fixed and range between 2.99% and 5.81%, with a weighted average rate of 3.99%. Remaining maturities of FHLB advances extend over multiple time periods through 2020, with a weighted average remaining term of 2.8 years. FHLB advances are generally used to increase the Company's lending activities and to aid the efforts of asset and liability management by utilizing various repayment options offered by the FHLB. Long-term advances from the FHLB totaled $19.0 million and $27.1 million at December 31, 2014 and 2013, respectively. This represents a decrease of $8.2 million or 30.1% and is attributed to scheduled repayment activity.

In 2005 and 2007, the Company completed a total of three private offerings of trust preferred securities through separate Delaware statutory trusts (the “Trusts”) sponsored by the Company in the aggregate amount of $47.5 million. The combined $25.0 million proceeds from the first two trusts (“Trusts I and II”) established in 2005 were used to fund the acquisition of Citizens Bancorp. Proceeds from the third trust (“Trust III”) were used primarily to acquire Company shares through a tender offer during 2007. The Company owns all of the common securities of each of the three Trusts.

The Trusts used the proceeds from the sale of preferred securities, plus capital of $1.5 million contributed by the Company to establish the trusts, to purchase the Company's subordinated notes in amounts and bearing terms that parallel the amounts and terms of the respective preferred securities. Amounts and general terms related to the Trusts at year-end 2014 are summarized in the table below.

(Dollars in thousands)	Trust I	Trust II	Trust III
Subordinated notes payable	$ 10,310	$ 15,464	$ 23,196
Interest rate terms	3-month LIBOR +150 BP	3-month LIBOR +165 BP	3-month LIBOR +132 BP
Interest rate in effect at year-end	1.76 %	1.91 %	1.55 %
Stated maturity date	September 30, 2035	September 30, 2035	November 1, 2037

The subordinated notes of the Trusts are redeemable in whole or in part, without penalty, at the Company's option and are junior in right of payment of all present and future senior indebtedness of the Company. The weighted average interest rate in effect as of the last determination date in both 2014 and 2013 was 1.71%.

Contractual Obligations

The Company's contractual obligations to make future payments as of December 31, 2014 are as follows:

	Payments Due by Period				
Contractual Obligations (In thousands)	Total	One Year or Less	One to Three Years	Three to Five Years	More Than Five Years
Time deposits	$395,531	$233,322	$134,004	$24,948	$3,257
Long-term FHLB debt	18,961	-	15,000	3,025	936
Subordinated notes payable	48,970	-	-	-	48,970
Long-term securities sold under agreements to repurchase	100,763	254	100,509	-	-
Unfunded postretirement benefit obligations	5,513	391	859	986	3,277
Operating leases	1,375	343	408	197	427
Employment agreements	3,110	938	1,017	770	385
Total	$574,223	$235,248	$251,797	$29,926	$57,252

Long-term FHLB debt represents FHLB advances pursuant to several different credit programs. Long-term FHLB debt, subordinated notes payable, and securities sold under agreements to repurchase are more fully described under the caption *"Long-term Borrowings"* above and in Note 9 of the Company's 2014 audited consolidated financial statements. Payments for borrowings in the table above do not include interest. Postretirement benefit obligations are determined by actuaries and estimated based on various assumptions with payouts projected over the next ten years. Estimates can vary significantly each year due to changes in significant assumptions. Operating leases include standard business equipment used in the Company's day-to-day business as well as the lease of certain branch sites. Operating lease terms generally range from one to five years, with the ability to extend certain branch site leases at the Company's option. Payments related to leases are based on actual payments specified in the contracts. Employment agreements represent annual minimum base salary amounts payable by the Company to five employees. The Company has employment agreements with its Chief Executive Officer, Chief Financial Officer, and three key officers of its subsidiaries.

Guarantees

During 2007, the Parent Company entered into a guarantee agreement whereby it agreed to become unconditionally and irrevocably the guarantor of the obligations of three of its subsidiary banks in connection with the $200 million balance sheet leverage transaction. Principal payments by the bank subsidiaries have reduced the outstanding balance of the obligation to $100 million at year-end 2014, which matures in 2017. The borrowings are required to be secured by GNMA bonds valued at 106% of the amount outstanding, although the banks typically maintain an amount in excess of the required minimum. Should any of the subsidiary banks default on its borrowings under the agreement, the GNMA bonds securing the borrowings would be liquidated to satisfy amounts due. If the value of the GNMA bonds fall below the obligation under the contract, the Parent Company is obligated to cover any such shortfall in absence of the subsidiary banks' ability to do so. The Parent Company believes its subsidiary banks are fully capable of fulfilling their obligations under the borrowing arrangement and that the Parent Company will not be required to make any payments under the guarantee agreement.

Effects of Inflation

The majority of the Company’s assets and liabilities are monetary in nature. Therefore, the Company differs greatly from most commercial and industrial companies that have significant investments in nonmonetary assets, such as fixed assets and inventories. However, inflation does have an important impact on the growth of assets in the banking industry and on the resulting need to increase equity capital at higher than normal rates in order to maintain an appropriate equity to assets ratio. Inflation also affects other noninterest expense, which tends to rise during periods of general inflation.

Market Risk Management

Market risk is the risk of loss arising from adverse changes in market prices and rates. The Company’s market risk is comprised primarily of interest rate risk created by its core banking activities of extending loans and receiving deposits. The Company’s success is largely dependent upon its ability to manage this risk. Interest rate risk is defined as the exposure of the Company’s net interest income to adverse movements in interest rates. Although the Company manages other risks, such as credit and liquidity risk, management considers interest rate risk to be its most significant risk, which could potentially have the largest and a material effect on the Company’s financial condition and results of operations. A sudden and substantial change in interest rates may adversely impact the Company’s earnings to the extent that the interest rates earned on assets and paid on liabilities do not change at the same speed, to the same extent, or on the same basis. Other events that could have an adverse impact on the Company’s performance include changes in general economic and financial conditions, general movements in market interest rates, and changes in consumer preferences. The Company’s primary purpose in managing interest rate risk is to effectively invest the Company’s capital and to manage and preserve the value created by its core banking business.

Management believes the most significant impact on financial and operating results is the Company’s ability to react to changes in interest rates. Management seeks to maintain an essentially balanced position between interest sensitive assets and liabilities in order to protect against the effects of wide interest rate fluctuations.

The Parent Company and each of its subsidiary banks has a Corporate Asset and Liability Management Committee (“ALCO”) which monitors the composition of the balance sheet to ensure comprehensive management of interest rate risk and liquidity. The Parent Company ALCO also provides guidance and support to each ALCO of the Company’s subsidiary banks and is responsible for monitoring risks on a company-wide basis. The Parent Company ALCO has established minimum standards in its asset and liability management policy that each subsidiary bank must adopt. However, the subsidiary banks are permitted to deviate from these standards so long as the deviation is no less stringent than that of the Corporate policy.

The Company uses a simulation model as a tool to monitor and evaluate interest rate risk exposure. The model is designed to measure the sensitivity of net interest income and net income to changing interest rates over future periods. Forecasting net interest income and its sensitivity to changes in interest rates requires the Company to make assumptions about the volume and characteristics of many attributes, including assumptions relating to the replacement of maturing earning assets and liabilities. Other assumptions include, but are not limited to, projected prepayments, projected new volume, and the predicted relationship between changes in market interest rates and changes in customer account balances. These effects are combined with the Company's estimate of the most likely rate environment to produce a forecast for the next twelve months. The forecasted results are then compared to the effect of a gradual 200 basis point increase and decrease in market interest rates on the Company's net interest income and net income. Because assumptions are inherently uncertain, the model cannot precisely estimate net interest income and net income or the effect of interest rate changes on net interest income and net income. Actual results could differ significantly from simulated results.

At December 31, 2014, the model indicated that if rates were to gradually increase by 200 basis points over the next twelve months, then net interest income (TE) and net income would increase 0.63% and 1.77%, respectively, compared to forecasted results. The model indicated that if rates were to gradually decrease by 200 basis points over the next twelve months, then net interest income (TE) and net income would decrease 1.72% and 5.14%, respectively, compared to forecasted results.

In the current low interest rate environment, it is not practical or possible to reduce certain deposit rates by the same magnitude as rates on earning assets. The average rate paid on the Company’s deposits is already below 2%. This situation magnifies the model’s predicted results when modeling a decrease in interest rates, as earning assets with higher yields have more of an opportunity to reprice at lower rates than lower-rate deposits.

LIQUIDITY

Liquidity measures the ability to meet current and future cash flow needs as they become due. For financial institutions, liquidity reflects the capacity to meet loan demand, accommodate possible outflows in deposits, and to react and capitalize on interest rate market opportunities. A financial institution’s ability to meet its current financial obligations is dependent upon the structure of its balance sheet, its ability to liquidate assets, and its access to alternative sources of funds. The Company’s goal is to meet its near-term funding needs by maintaining a level of liquid funds through its asset/liability management. For the longer term, the liquidity position is managed by balancing the maturity structure of the balance sheet. This process allows for an orderly flow of funds over an extended period of time. The Company’s ALCOs, both at the bank subsidiary and consolidated level, meet regularly and monitor the composition of the balance sheet to ensure comprehensive management of interest rate risk and liquidity.

The Company's objective as it relates to liquidity is to ensure that its subsidiary banks have funds available to meet deposit withdrawals and credit demands without unduly penalizing profitability. In order to maintain a proper level of liquidity, the subsidiary banks have several sources of funds available on a daily basis. For assets, those sources of funds include liquid assets that are readily marketable or that can be pledged, or which mature in the near future. These assets primarily include cash and due from banks, federal funds sold, investment securities, and cash flow generated by the repayment of principal and interest on loans and investment securities. For liabilities, sources of funds primarily include the subsidiary banks' core deposits, FHLB and other borrowings, and federal funds purchased and securities sold under agreements to repurchase. While maturities and scheduled amortization of loans and investment securities are generally a predictable source of funds, deposit outflows and mortgage prepayments are influenced significantly by general interest rates, economic conditions, and competition in our local markets.

The Company uses a liquidity ratio metric to help measure its ability to meet its cash flow needs. This ratio is monitored by ALCO at both the bank and consolidated level. The liquidity ratio is based on current and projected levels of sources and uses of funds. This measure is useful in analyzing cash needs and formulating strategies to achieve desired results. For example, a low liquidity ratio could indicate that the Company’s ability to fund loans might become more difficult. A high liquidity ratio could indicate that the Company may have a disproportionate amount of funds in low yielding assets, which is more likely to occur during periods of sluggish loan demand or economic difficulties. The Company’s liquidity position, as measured by its liquidity ratio, increased at year-end 2014 when compared to year-end 2013 and is within its ALCO guidelines. The Company’s liquidity ratio remains elevated mainly as a result of its overall net funding position and weak, quality loan demand. As loans have paid down, payments have been reinvested more into investments securities or other temporary investments. The Company also continues a cautious lending strategy while continuing efforts to reduce its level of nonperforming assets in a slow growing economic environment.

As of December 31, 2014, the Company had $224 million of additional borrowing capacity under various FHLB, federal funds, and other agreements. However, there is no guarantee that these sources of funds will continue to be available to the Company, or that current borrowings can be refinanced upon maturity, although the Company is not aware of any events or uncertainties that are likely to cause a decrease in the Company’s liquidity from these sources.

Liquidity at the Parent Company level is primarily affected by the receipt of dividends from its subsidiary banks, cash balances maintained, and borrowings from nonaffiliated sources. Payment of dividends by the Company’s subsidiary banks is subject to certain regulatory restrictions as set forth in national and state banking laws and regulations. In addition, United Bank and Citizens Northern each must obtain regulatory approval to declare or pay dividends to the Parent Company as a result of increased capital required in connection with prior regulatory exams. The capital ratios at these two banks exceeded those required higher amounts at year-end 2014. Capital ratios at all four of the Company’s subsidiary banks exceed regulatory established “well-capitalized” status at December 31, 2014 under the prompt corrective action regulatory framework. See Note 18 *“Regulatory Matters”* of the Company’s 2014 audited consolidated financial statements for further information regarding the restrictions on dividend payments and increased capital required at certain of the Company’s bank subsidiaries as outlined in prior regulatory agreements.

The Parent Company's primary uses of cash include the payment of dividends to its preferred and common shareholders, injecting capital into subsidiaries, paying interest expense on borrowings, and payments for general operating expenses. The regulatory agreement entered into during 2009 between the Parent Company and its primary banking regulators was terminated in March 2014. As a result, the Company is no longer required to receive permission from its banking regulators to make interest payments on its trust preferred securities or to pay dividends on its common and preferred stock. However, the Company's current goal is to redeem all of its outstanding preferred stock before considering the payment of a dividend on its common stock. The Company redeemed 20,000 shares, or two-thirds, of its original amount of outstanding preferred stock during 2014 in two separate partial redemptions of 10,000 shares each. The Company intends to redeem its remaining 10,000 shares of preferred stock in 2015, although this action requires approval by our banking regulators. The timing and amount of any further redemption by the Company of its remaining outstanding preferred stock will be disclosed when assured. Reference is made to Note 23 *"Preferred Stock"* of the Company's 2014 audited consolidated financial statements and Item 1A *"Risk Factors"* of this Form 10-K for additional information on the Company's restrictions and requirements related to the payment of interest and dividends.

The Parent Company had cash balances of $32.1 million at year-end 2014, a decrease of $4.4 million or 12.0% compared to $36.5 million at year-end 2013. Significant cash receipts of the Parent Company for 2014 include dividend payments from its bank and nonbanking subsidiaries of $15.0 million and $1.5 million, respectively, a return of capital from nonbank subsidiaries in the amount of $1.5 million, and management fees from subsidiaries of $2.9 million. Significant cash payments by the Parent Company in 2014 include $20.0 million to redeem a portion of its outstanding preferred stock, $2.5 million for salaries, payroll taxes, and employee benefits, and $2.0 million for the payment of dividends on outstanding preferred stock.

Liquid assets consist of cash, cash equivalents, and available for sale investment securities. At December 31, 2014, consolidated liquid assets were $727 million, an increase of $46.2 million or 6.8% from year-end 2013. The increase in liquid assets was driven by higher interest bearing deposits with other banks in the amount of $25.4 million or 60.8% and higher available for sale investment securities of $13.6 million or 2.2%. Liquid assets remain elevated mainly as a result of the Company's overall net funding position and weak, high-quality loan demand. The overall funding position of the Company changes as loan demand, deposit levels, and other sources and uses of funds fluctuate.

Net cash provided by operating activities was $29.0 million and $24.0 million for 2014 and 2013, respectively. This represents an increase of $5.0 million or 20.8%, led by an increase in net mortgage loans sold. Net cash flow from investing activities was $57.3 million for 2014 compared with a net use of $53.3 million for 2013. This represents a change of $111 million, driven by net investment securities and loan activity. For investment securities, the Company had net cash outflows of $7.0 million for 2014 compared with net cash outflows of $64.8 million for the prior year. Net cash outflows related to investments represent net purchase activity, where purchases exceeded proceeds received from the sale, maturity, and calls of investment securities. For loans, the Company had net loan repayment activity of $56.7 million for 2014, up $51.2 million from the prior year as overall paydowns more than offset new demand. For 2014, excess cash flows from investment and loan activity were used more to fund deposit runoff, debt repayments, and the redemption of a portion of the Company's preferred stock. In 2013, cash inflows were used more to purchase additional investment securities.

Net cash used in financing activities was $53.6 million for 2014 compared with net cash inflows of $1.7 million for 2013. The net use of cash for 2014 was made up primarily by deposit declines, the redemption of a portion of the Company's preferred stock outstanding in the amount of $20.0 million, and repayments of long-term borrowings. Net outflows related to deposits were $23.1 million for 2014, an increase of $22.5 million compared to $595 thousand for 2013. Net repayments on long-term borrowings were $8.2 million for the current year compared to $1.4 million for 2013.

Information relating to commitments to extend credit is disclosed in Note 15 of the Company's 2014 audited consolidated financial statements. These transactions are entered into in the ordinary course of providing traditional banking services and are considered in managing the Company's liquidity position. The Company does not expect these commitments to significantly affect the liquidity position in future periods. The Company has not entered into any contracts for financial derivative instruments such as futures, swaps, options, or similar instruments.

CAPITAL RESOURCES

Shareholders' equity was $173 million at year-end 2014, an increase of $2.9 million or 1.7% compared to $170 million at year-end 2013. Net income for the period increased shareholders' equity by $16.5 million, partially offset by dividends on preferred stock of $1.9 million. Shareholders' equity also increased as a result of an $8.8 million after-tax increase in the unrealized gain on available for sale investment securities, which is attributed to a decrease in longer-term market interest rates. Generally, as market interest rates fall, the value of fixed rate investments such as those held by the Company, increases. The Company redeemed 20,000 shares of its preferred stock in two separate partial redemptions of 10,000 shares each during the year, resulting in a reduction to shareholders' equity of $20.0 million in total.

On January 9, 2009, the Company issued 30,000 shares of Series A, no par value cumulative perpetual preferred stock. Under the terms of the issuance, the dividend rate increased on February 15, 2014 to 9% from 5%. At year-end 2014, there are 10,000 shares that remain outstanding. The Company's goal is to redeem the outstanding preferred shares as soon as its capital position, earnings, asset quality, and other factors indicate it is warranted. Further redemptions, however, require the approval of banking regulators. The Parent Company is under no directive by its regulators to raise any additional capital.

At December 31, 2014 and 2013, the Company's tangible capital ratio was 9.68% and 9.35%, respectively. The tangible capital ratio is defined as tangible equity as a percentage of tangible assets. Tangible common equity to tangible assets, which further excludes outstanding preferred stock, was 9.12% at year-end 2014, up 142 basis points compared to 7.70% at year-end 2013.

Consistent with the objective of operating a sound financial organization, the Company's goal is to maintain capital ratios well above the regulatory minimum requirements. The Company's capital ratios as of December 31, 2014 and the regulatory minimums were as follows:

	Farmers Capital Bank Corporation		Regulatory Minimum	
Tier 1 Risk-based Capital[1]	19.75	%	4.00	%
Total Risk-based Capital[1]	21.00		8.00	
Tier 1 Leverage Capital[2]	12.04		4.00	

[1]Tier 1 Risk-based and Total Risk-based Capital ratios are computed by dividing Tier 1 or Total Capital, as defined by regulation, by a risk-weighted sum of the assets, with the risk weighting determined by general standards established

by regulation. The safest assets (e.g., government obligations) are assigned a weighting of 0% with riskier assets receiving higher ratings (e.g., ordinary commercial loans are assigned a weighting of 100%).

[2]Tier 1 Leverage ratio is computed by dividing Tier 1 Capital by total quarterly average assets, as defined by regulation.

In July 2013, banking regulators issued final rules to bring U.S. banking organizations into compliance with the Basel III capital framework effective in 2015. The Company has completed a pro forma analysis of its capital ratios under the new capital framework. This analysis indicates the Company remains well-capitalized under the new rules, including meeting the effective minimum capital ratios with a fully phased-in capital conservation buffer. For further information, see discussion in Part I, Item 1 under the caption *"Capital"* beginning on page 15 of this Form 10-K.

The table below represents an analysis of dividend payout ratios and equity to asset ratios for the previous five years.

Years Ended December 31,	2014		2013		2012		2011		2010	
Percentage of common dividends declared to net income	-	%	-	%	-	%	-	%	-	%
Percentage of average shareholders' equity to average total assets	9.84		9.34		8.85		8.05		7.32	

Two of the Company’s subsidiary banks are currently subject to regulatory agreements with their primary banking supervisors as detailed below under the caption “Subsidiary Banks.” The agreement entered into during 2009 between the Parent Company and its primary regulators was terminated in March 2014 as a result of continued satisfactory compliance, most notably from the progress made in lowering nonperforming assets and increasing capital levels. Therefore, the Company is no longer required to receive permission from its banking regulators to make interest payments on its trust preferred securities or to pay dividends on its common and preferred stock. However, the Company’s current goal is to redeem all of its outstanding preferred stock before considering the payment of a dividend on its common stock. The Company redeemed 20,000 shares, or two-thirds, of its original outstanding amount in two separate partial redemptions of 10,000 shares during 2014. The Company intends to redeem its remaining 10,000 shares of preferred stock in 2015, although this action requires approval by our banking regulators. The timing and amount of any further redemption by the Company of its remaining outstanding preferred stock will be disclosed when assured.

Subsidiary Banks

The Company’s subsidiary banks are subject to capital-based regulatory requirements which place banks in one of five categories based upon their capital levels and other supervisory criteria. These five categories are: (1) well-capitalized, (2) adequately capitalized, (3) undercapitalized, (4) significantly undercapitalized, and (5) critically undercapitalized. To be well-capitalized, a bank must have a Tier 1 Leverage ratio of at least 5% and a Total Risk-based Capital ratio of at least 10%. As of December 31, 2014, each of the Company’s four subsidiary banks had the following capital ratios for regulatory purposes:

	Tier 1 Leverage Capital Ratio		Total Risk-based Capital Ratio	
Farmers Bank	9.40	%	18.70	%
United Bank	11.08		19.26	
First Citizens	9.44		14.30	
Citizens Northern	10.11		15.71	

Two of the Company’s subsidiary banks, due to their recent regulatory agreements, were required at year-end 2014 to maintain capital ratios in excess of the well-capitalized level under the prompt corrective action framework. The capital levels and other requirements for these two banks related to their regulatory agreement are discussed below.

United Bank. In November of 2009, the FDIC, the Kentucky Department of Financial Institutions (“KDFI”), and United Bank entered into a Cease and Desist Order (“C&D”) primarily as a result of its level of nonperforming assets. The C&D was terminated in December 2011 coincident with the issuance of a Consent Order (“Consent Order”) entered into between the parties. The Consent Order was substantially the same as the C&D, with the primary exception being that

United Bank must achieve and maintain a Tier 1 Leverage ratio of 9.0% and a Total Risk-based Capital ratio of 13.0%.

During January 2014, the formal Consent Order was terminated and replaced with a stepped-down enforcement action in the form of an informal Memorandum of Understanding (“Memorandum”). While many of the same provisions carried over to the Memorandum, replacing the Consent Order represents important progress for the Company. At December 31, 2014, United Bank had a Tier 1 Leverage ratio of 11.08% and a Total Risk-based Capital ratio of 19.26%.

The terms of the Memorandum require United Bank to:

continue to formulate, adopt and submit to the FDIC and the KDFI for review and comment a written plan of action to lessen the bank's risk position in each asset which was classified "Substandard" or "Doubtful" in the most recent or any subsequent examination or visitation, and which aggregated $1,000,000 or more. Such plan shall include:

a) the dollar levels to which the bank will strive to reduce each line of credit within six and twelve months from the effective date of the Memorandum; and
b) provisions for the submission of monthly written progress reports to the bank's board of directors for review and notation in the board of director's minutes.

within 10 days from the date of the Memorandum, the bank shall eliminate from its books, by collection, charge-off or other proper entries, all assets or portions of assets classified "Loss" in the most recent or any subsequent examination that have not been previously charged off or collected.

while the Memorandum is in effect, the bank shall not extend, directly or indirectly, any additional credit to, or for the benefit of, any borrower who is already obligated in any manner to the bank on any extensions of credit (including any portion thereof) that has been charged off the books of the bank or classified "Loss" in the most recent examination, or any subsequent examination or visitation, so long as such credit remains uncollected.

while the Memorandum is in effect, the bank shall not extend, directly or indirectly, any additional credit to, or for the benefit of, any borrower whose loan or other credit has been classified "Substandard", or "Doubtful", or is listed for Special Mention in the most recent examination, or any subsequent examination or visitation, and is uncollected unless the bank's board of directors has adopted, prior to such extension of credit, a detailed written statement giving the reasons why such extension of credit is in the best interest of the bank.

while the Memorandum is in effect, the bank shall continue its practice of having procedures for managing the bank's sensitivity to interest rate risk. The procedures shall comply with the Joint Agency Statement of Policy on Interest Rate Risk (June 26, 1996), and the Joint Supervisory Statement on Investment Securities and End-user Derivative Activities (April 23, 1998). The bank shall also implement within 60 days of the Memorandum the recommendations to enhance the bank's interest rate risk management policy and practices set forth in the most recent examination.

while the Memorandum remains in effect, the bank shall continue its practice of adopting, implementing, and adhering to a written profit plan and a comprehensive budget for all categories of income and expense for calendar year 2014 and each succeeding year. The plans shall contain formal goals and strategies, consistent with sound banking practices, to reduce discretionary expenses and to improve the bank's overall earnings, and contain a description of the operating assumptions that form the basis for major projected income and expense components. The written profit plan shall address, at a minimum:

a) an identification of the major areas in, and means by which, the board will seek to improve the bank's operating performance;
b) realistic and comprehensive budgets;
c) a budget review process to monitor the income and expenses of the bank to compare actual figures with budgetary projections;
d) a description of the operating assumptions that form the basis for, and adequately support, major projected income and expense components; and
e) periodic salary review.

Copies of the plans and budgets required by this provision shall be submitted to the FDIC and the KDFI.

while the Memorandum is in effect, the bank shall maintain Tier 1 Capital and Total Risk-Based Capital at a level equal to or exceeding 9.0% and 13.0% of the bank's total assets, calculated in accordance with Part 325 of the FDIC Rules and Regulations. If such ratio is less than the aforementioned minimums as of each quarter end, while the Memorandum is in effect, the bank shall, within 30 days of such dates, present to the FDIC and the KDFI a plan for the restoration of these capital ratios.

while the Memorandum is in effect, the bank shall not declare or pay any dividends without the prior written consent of the FDIC and the KDFI.

within 30 days following each calendar quarter after the date of the Memorandum, progress reports covering each of the provisions of the Memorandum shall be submitted to the FDIC and the KDFI, until notification by the supervisory authorities that the reports need no longer be submitted. The board shall review all reports prior to submission and note their considerations in the minutes.

Following is a summary of the activity during 2014 of substandard loans that meet the reporting requirements included in the Memorandum.

Substandard Loans

(Dollars in thousands)		Activity During 2014								
December 31, 2013		Increases		Decreases					December 31, 2014	
Balance	Number of Credits	Additional Credit/New Classifications	Number of New Credits	Principal Payments	Charge Offs	Transfers to OREO	Amounts Upgraded and No Longer Classified as Substandard	Other	Balance	Number of Credits
$28,675	10	$1,875	-	$3,047	$ -	$ 5,078	$ 3,180	$ 74	$19,171	8

At December 31, 2014, United Bank had eight credit relationships with an aggregate outstanding balance of $19.2 million that meet the risk identification criteria established in the Memorandum. The aggregate amount of substandard loans meeting the reporting criteria was below the target level established by United Bank resulting from the Memorandum. Target levels are established based on projections of individual substandard loan amounts and will fluctuate depending on the actual amount of newly classified loans, principal reductions, or repossession activity.

Subsequent to year-end 2014, the Company received written notification that the FDIC and KDFI, as a result of their recent examination, terminated the Memorandum that was entered into with United Bank effective immediately. In connection with the termination of the Memorandum, the Board of Directors of United Bank agreed to adopt a resolution to continue doing the following:

- formulate, adopt, and report a written plan of action to lessen its risk position of assets classified as substandard or doubtful which are $1 million or more;
- not extend credit to any borrower already obligated to the Bank on any extension of credit which has been charged off or classified as loss;
- not extend additional credit to any borrower whose loan has been classified as substandard, doubtful, or special mention, unless documented by the board that the extension is in the best interest of the Bank;
- adopting, implementing, and adhering to a written profit plan and budget;
- not declare or pay any dividends without the prior written consent of the FDIC and KDFI; and
- provide quarterly progress reports to the FDIC and KDFI related to provisions of the resolution

The requirement for United Bank to maintain a minimum Tier 1 Leverage ratio of 9.0% and a Total Risk-based Capital ratio of 13.0% no longer applies.

Citizens Northern. The FDIC and the KDFI entered into a Memorandum with Citizens Northern on September 8, 2010. That Memorandum was terminated July 7, 2013 upon the issuance of an updated Memorandum. The updated Memorandum is substantially the same as the replaced Memorandum, including the requirement to obtain regulatory approval prior to declaring or paying a dividend, but raised the required minimum Tier I Leverage to 9.0% from 8.0%. At year-end 2014, Citizens Northern had a Tier I Leverage ratio of 10.11% and a Total Risk-based Capital ratio of 15.71%.

Under the Memorandum, Citizens Northern agreed to:

have and retain qualified management, with particular emphasis on its loan administration and collection needs. Every member of management shall have the qualifications and experience commensurate with his or her duties and responsibilities. The qualifications of management shall be assessed on management's ability to:

a) affect reasonable improvements to the condition of the institution, including improvements in asset quality and earnings;
b) comply with applicable laws, rules, regulations, and regulatory policies; and
c) comply with the requirements of this Memorandum;

within 60 days from the date of this Memorandum, to formulate, adopt and submit to the Regional Director and the Commissioner for review and comment a written plan of action to lessen the risk position in each asset which was classified "Substandard" in the most recent examination, and which aggregated $250,000 or more. Such plan shall include:

a) dollar levels to which it will strive to reduce each line of credit within six and twelve months from the effective date of this Memorandum; and
b) provisions for the submission of monthly written progress reports to its board of directors for review and notation in the board of director's minutes;

not extend any additional credit to, or for the benefit of, any borrower who is already obligated in any manner on any extension of credit (including any portion thereof) that:

a) has been charged off or classified "Loss" in the most recent examination or in any subsequent review by consultants or by a regulatory body so long as such credit remains uncollected; or
b) has been classified "Substandard" or "Doubtful" in the most recent examination, on the bank's internal watch list, or in any subsequent review by its consultants, and is uncollected, unless the board of directors or loan committee has adopted, prior to such extension of credit, a detailed written statement giving reasons why such extension of credit is in the best interest of the bank. A copy of the statement, including a thorough financial analysis gauging the borrower's financial condition and overall ability to service the existing and new debt, shall be placed in the appropriate loan file and shall be incorporated in the minutes of the applicable loan committee;

within 60 days from the date of this Memorandum, take all steps necessary to correct the credit underwriting and administration weaknesses listed in the most recent examination. Corrective actions will include a revision of procedures for assessing borrower repayment capacity. The revised procedures will include obtaining and evaluating current financial information; considering delinquent property taxes; and incorporating material changes to the balance sheet accounts such as account receivables, inventories, fixed assets, and accounts payable into cash flow analyses for commercial borrowers;

within 30 days from the date of this Memorandum, revise its Allowance for Loan and Lease Losses ("ALLL") methodology consistent with the comments in the most recent examination. Ensure that when assessing impairment under Accounting Standards Codification Topic 310 using the fair value of collateral method, assessments are based on current valuations of the pledged collateral;

(Company Note: The ALLL methodology is structurally sound. The comments referred to in the then-most recent examination referred to above pertain to documentation exceptions for two impaired credit relationships consisting of eight real estate properties with an aggregate outstanding balance of $1.7 million. Documentation supporting certain of these properties was stale as of the examination date. However, appraisals received subsequent to the examination date confirm that the estimated discount applied to the stale appraisals resulted in an allowance that was adequate. Additional procedures for adhering to and monitoring compliance over the ALLL have since been revisited and refined to assure that the ALLL is fully documented and adequately supported in a timely fashion).

prior to submission or publication of all Reports of Condition and income required by the FDIC after the effective date of this Memorandum, the board of directors shall review the adequacy of the ALLL, shall provide an adequate allowance, and shall report such allowance on the Reports of Condition and income. The minutes of the board meeting at which such review is undertaken shall indicate the results of the review, the amount of increase in the allowance recommended, if any, and the basis for determination of the amount of the allowance provided;

within 60 days from the date of this Memorandum, formulate and implement a written Profit Plan. The Profit Plan shall be consistent with the loan, investment and funds management policies. This Plan shall be submitted to the Regional Director and Commissioner for review and comment, and shall address, at a minimum, goals and strategies for improving and sustaining earnings including:

a) an identification of the major areas in, and means by which, the board will seek to improve the operating performance;
b) realistic and comprehensive budgets;
c) a budget review process to monitor the income and expenses to compare actual figures with budgetary projections;
d) a description of the operating assumptions that form the basis for, and adequately support, major projected income and expense components; and
e) periodic salary review;

within 30 days from the date of this Memorandum, take all steps necessary to correct the violations scheduled in the most recent examination. In addition, adopt procedures to assure future compliance with all applicable laws, rules and regulations;

while this Memorandum is in effect, maintain Tier I capital at a level equal to or exceeding 9.0% of the total assets which shall be calculated in accordance with Part 325 of the FDIC Rules and Regulations. If such ratio is less than 9.0% as of March 31, June 30, September 30 or December 31 of each calendar year, while this Memorandum is in effect, within 30 days of such dates, present to the Regional Director and Commissioner a plan for the augmentation of the capital accounts or other measures to bring the ratio to 9.0%;

while this Memorandum is in effect, written consent of the Regional Director and the Commissioner is required to declare or pay any dividends; and

within 30 days following each calendar quarter after the date of this Memorandum, progress reports covering each of the provisions of this Memorandum shall be submitted to the Regional Director and Commissioner until notification by the supervisory authorities that the reports need no longer be submitted. The board of directors shall review all reports prior to submission and note their consideration in the minutes.

Following is a summary of the activity during 2014 of substandard loans that meet the reporting requirements included in the Memorandum.

Substandard Loans

(Dollars in thousands)		Activity During 2014							
December 31, 2013		Increases		Decreases				December 31, 2014	
Balance	Number of Credits	Additional Credit/New Classifications	Number of New Credits	Principal Payments	Charge Offs	Transfers to OREO	Amounts Upgraded and No Longer Classified as Substandard	Balance	Number of Credits
$9,202	10	$1,548	2	$1,161	$ -	$ 1,393	$ 2,285	$5,911	9

At December 31, 2014, Citizens Northern had nine credit relationships with an aggregate outstanding balance of $5.9 million that meet the risk identification criteria established in the Memorandum. There was no related target level established at year-end 2014.

The Company believes it is adequately addressing all issues in the regulatory agreements above and is in compliance with those agreements as of December 31, 2014. However, only the respective regulatory agencies can determine if compliance with the applicable regulatory agreements have been met. Regulators continue to monitor the Company's progress and compliance with the agreements through periodic on-site examinations, regular communications, and quarterly data analysis. The results of these examinations and communications show satisfactory progress toward meeting the requirements included in the regulatory agreements.

The Parent Company maintains cash available to fund a certain amount of additional injections of capital to its bank subsidiaries if required by its regulators. If needed, further amounts in excess of available cash may be funded by future public or private sales of securities, although the Parent Company is currently under no directive by its regulators to raise any additional capital.

Share Buy Back Program

At various times, the Company's Board of Directors has authorized the purchase of shares of the Company's outstanding common stock. No stated expiration dates have been established under any of the previous authorizations. There are 84,971 shares that may still be purchased under the various authorizations, though no shares have been purchased since 2008.

Shareholder Information

As of February 10, 2015, the Company had 2,632 shareholders of record, which includes individual participants in securities positions listings.

Common Stock Price

The Company's common stock is traded on the NASDAQ Stock Market LLC exchange in the Global Select Market tier, with sales prices reported under the symbol: FFKT. The table below lists the high and low sales prices of the Company's common stock for 2014 and 2013.

	High	Low
2014		
Fourth Quarter	$23.65	$21.72

Third Quarter	23.92	21.25
Second Quarter	23.40	17.64
First Quarter	24.54	18.40
2013		
Fourth Quarter	$24.00	$19.14
Third Quarter	26.98	18.62
Second Quarter	23.00	17.50
First Quarter	19.00	11.80

The closing price per share of the Company's common stock on December 31, 2014, the last trading day of the Company's fiscal year, was $23.29. There have been no dividends declared on the Company's common stock since 2009.

Recently Issued Accounting Standards

See Note 1 – *"Summary of Significant Accounting Policies,"* under the caption *"Recently Issued But Not Yet Effective Accounting* Standards*,"* in the Company's 2014 audited consolidated financial statements for further information about recently issued accounting pronouncements and their expected impact on the Company's financial statements.

2013 Compared to 2012

The Company reported net income of $13.4 million or $1.54 per common share in 2013 compared to $12.1 million or $1.37 per common share for 2012. This represents an increase of $1.3 million or $.17 per common share. The increase in net income for 2013 was primarily due to a decrease in the provision for loan losses of $5.4 million or 194% and higher net interest income of $1.8 million or 3.3%. Noninterest income decreased $2.5 million or 10.3%, with noninterest expenses and income taxes increasing $1.8 million or 3.0% and $1.5 million or 52.4%, respectively.

For 2013, the increase in net interest income from 2012 was due to a decrease in interest expense of $6.3 million or 34.3%, partially offset by lower interest income of $4.5 million or 6.3%. Interest expense on deposits and borrowed funds decreased $3.3 million or 35.9% and $2.9 million or 32.7%, respectively. Interest expense on deposits decreased primarily due to the repricing of higher-rate time deposits to lower market interest rates and a lower average balance outstanding. Interest expense on borrowed funds declined primarily due the repayment of a $50.0 million portion of long-term borrowings and the repricing of $23.2 million of subordinated debt from a fixed rate of 6.60% to a variable rate of 3-month LIBOR plus 132 basis points during the fourth quarter of 2012. The decrease in interest income relates to both a decline in yield and volume on earning assets in a low market interest rate environment. Net interest margin was 3.40% for 2013, up 22 basis points from 3.18% for 2012. Net interest spread was 3.23%, up 27 basis points compared to 2.96%.

The Company recorded a credit to the provision for loan losses in the amount of $2.6 million for 2013 compared to a charge of $2.8 million for 2012. The decrease in the provision for loan losses was attributed to an overall improvement in the credit quality of the loan portfolio and a decrease in loan balances outstanding. Nonperforming loans, impaired loans, early stage delinquencies, and watch list loans all improved during 2013. Historical loss rates, adjusted for current risk factors, also improved as lower recent charge-off activity replaced the higher levels that spiked upward starting in 2009.

Nonperforming loans decreased $3.3 million or 6.2% in 2013. The allowance for loan losses was $20.6 million at year-end 2013 and $24.4 million at year-end 2012. As a percentage of loans net of unearned income, the allowance for loan losses decreased 37 basis points to 2.06% at year-end 2013 compared to 2.43% a year earlier.

Noninterest income for 2013 was $22.1 million, a decrease of $2.5 million or 10.3% compared to $24.7 million for 2012. The decrease in noninterest income was driven by investment securities gains/losses, net gains on the sale of mortgage loans, and income from company-owned life insurance. The Company recorded a $50 thousand net loss on the sale of investment securities in 2013 compared with a net gain of $1.2 million for 2012. The net loss for 2013 is mainly attributed to premium amortization related to a single municipal bond that was called by the issuer. The net gain recorded in the prior year is attributed to normal asset/liability management strategies which result in periodic sales at irregular intervals based on then-current strategies. Net gains on the sale of mortgage loans decreased $882 thousand or 46.0% due to lower origination and refinancing activity. The volume of loans sold in 2013 decreased 41.0% compared to the prior year. Mortgage refinancing and home purchases rose sharply during 2012 fueled by interest rate declines. Market rates increased in 2013, which reduced customer demand for home purchases and refinancing. Income from company-owned life insurance decreased $562 thousand or 36.9% mainly because 2012 included a gain in the amount of $529 thousand related to death benefit proceeds occur at infrequent intervals.

Total noninterest expenses were $61.6 million for 2013, an increase of $1.8 million or 3.0% compared to $59.8 million for 2012. The decrease in noninterest expenses was made up primarily by higher other real estate expenses of $1.8 million or 33.8% and higher salaries and employee benefits of $1.5 million or 5.3%. Intangible asset amortization, legal expenses, and deposit insurance expense decreased $474 thousand or 46.7%, $440 thousand or 36.1%, and $425 thousand or 15.8%, respectively.

The increase in other real estate expenses was driven by higher impairment charges of $1.8 million or 46.8%. The increase in salaries and employee benefits was led by a $996 thousand or 20.5% increase in benefit expenses related primarily to higher claims associated with the Company's self-funded health insurance plan.

Intangible asset amortization decreased as a result of actuarial determined reductions related to core deposit and customer relationship intangible assets arising from previous business transactions. The decrease in legal expenses relates primarily to problem loans in the normal course of business. The comparative year also includes $122 thousand related to registering the Company's Series A preferred shares for their sale by the U.S. Treasury to third party investors. Deposit insurance expense decreased as a result of improvements in the risk rating by the FDIC of one of the Company's bank subsidiaries. The better rating reduced the assessment rate applicable in determining the amount payable for deposit insurance.

Income tax expense was $4.4 million for 2013, an increase of $1.5 million or 52.4% compared to $2.9 million for 2012. The effective income tax rates were 24.8% and 19.3% for 2013 and 2012, respectively. The increase in the effective tax rate is attributed primarily to lower tax credits and the relative amount of tax-free income to total income. Tax credits utilized by the Company over a number of years related to Qualified Zone Academy Bonds were fully exhausted during 2012. In addition, the taxable portion of total revenues increased more in proportion to the nontaxable revenues.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

The information required by this item is incorporated by reference to Part II, Item 7 under the caption "*Market Risk Management*" beginning on page 64 of this Form 10-K.

Item 8. Financial Statements and Supplementary Data

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The management of Farmers Capital Bank Corporation has the responsibility for preparing the accompanying consolidated financial statements and for their integrity and objectivity. The statements were prepared in accordance with accounting principles generally accepted in the United States of America. The consolidated financial statements include amounts that are based on management's best estimates and judgments. Management also prepared other information in the annual report and is responsible for its accuracy and consistency with the financial statements.

The Company's 2014 consolidated financial statements have been audited by BKD, LLP ("BKD") independent accountants. Management has made available to BKD all financial records and related data, as well as the minutes of Boards of Directors' meetings. Management believes that all representations made to BKD during the audit were valid and appropriate.

Lloyd C. Hillard, Jr.	Mark A. Hampton
President and Chief Executive Officer	Executive Vice President, Chief Financial Officer, and Secretary

March 11, 2015

Report of Independent Registered Public Accounting Firm

Audit Committee, Board of Directors

and Stockholders

Farmers Capital Bank Corporation

Frankfort, Kentucky

We have audited Farmers Capital Bank Corporation's (Company) internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control – Integrated Framework (2013)* 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 accompanying management report on 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. 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, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control – Integrated Framework (2013)* 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 the Company and our report dated March 11, 2015, expressed an unqualified opinion thereon.

Louisville, Kentucky

March 11, 2015

Report of Independent Registered Public Accounting Firm

Audit Committee, Board of Directors

and Stockholders

Farmers Capital Bank Corporation

Frankfort, Kentucky

We have audited the accompanying consolidated balance sheets of Farmers Capital Bank Corporation (Company) as of December 31, 2014 and December 31, 2013, and the related consolidated statements of income, comprehensive income, changes in shareholders’ equity and cash flows for each of the years in the three-year period ended December 31, 2014. 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 audits 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 audits 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 the Company as of December 31, 2014 and 2013, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2014, 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), the Company’s internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control-Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 11, 2015, expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Louisville, Kentucky

March 11, 2015

Consolidated Balance Sheets

December 31, (In thousands, except share data)	2014	2013
Assets		
Cash and cash equivalents:		
Cash and due from banks	$26,770	$22,925
Interest bearing deposits in other banks	67,152	41,749
Federal funds sold and securities purchased under agreements to resell	6,992	3,579
Total cash and cash equivalents	100,914	68,253
Investment securities:		
Available for sale, amortized cost of $618,429 (2014) and $618,395 (2013)	626,388	612,820
Held to maturity, fair value of $3,923 (2014) and $827 (2013)	3,728	765
Total investment securities	630,116	613,585
Loans, net of unearned income	931,943	999,883
Allowance for loan losses	(13,968)	(20,577)
Loans, net	917,975	979,306
Premises and equipment, net	34,933	36,273
Company-owned life insurance	29,363	28,899
Intangible assets, net	449	854
Other real estate owned	31,960	37,826
Other assets	36,896	44,559
Total assets	$1,782,606	$1,809,555
Liabilities		
Deposits:		
Noninterest bearing	$292,788	$277,294
Interest bearing	1,094,373	1,132,921
Total deposits	1,387,161	1,410,215
Federal funds purchased and other short-term borrowings	28,590	29,123
Securities sold under agreements to repurchase and other long-term borrowings	119,724	127,880
Subordinated notes payable to unconsolidated trusts	48,970	48,970
Dividends payable	113	188
Other liabilities	25,119	23,124
Total liabilities	1,609,677	1,639,500
Commitments and contingencies (Notes 15 and 17)		
Shareholders' Equity		
Preferred stock, no par value 1,000,000 shares authorized; 10,000 and 30,000 Series A shares issued and outstanding at December 31, 2014 and 2013, respectively; Liquidation preference of $10,000 at December 31, 2014	10,000	29,988
Common stock, par value $.125 per share; 14,608,000 shares authorized; 7,489,388 and 7,478,706 shares issued and outstanding at December 31, 2014 and 2013, respectively	936	935
Capital surplus	51,344	51,102
Retained earnings	105,774	91,242
Accumulated other comprehensive income (loss)	4,875	(3,212)
Total shareholders' equity	172,929	170,055
Total liabilities and shareholders' equity	$1,782,606	$1,809,555

See accompanying notes to consolidated financial statements.

Consolidated Statements of Income

(In thousands, except per share data) Years Ended December 31,	2014	2013	2012
Interest Income			
Interest and fees on loans	$49,921	$53,492	$55,942
Interest on investment securities:			
Taxable	11,737	10,575	12,872
Nontaxable	2,551	2,512	2,248
Interest on deposits in other banks	138	150	156
Interest on federal funds sold and securities purchased under agreements to resell	5	4	4
Total interest income	64,352	66,733	71,222
Interest Expense			
Interest on deposits	4,253	5,922	9,239
Interest on federal funds purchased and other short-term borrowings	54	74	96
Interest on securities sold under agreements to repurchase and other long-term borrowings	5,002	5,135	7,044
Interest on subordinated notes payable to unconsolidated trusts	844	864	1,879
Total interest expense	10,153	11,995	18,258
Net interest income	54,199	54,738	52,964
Provision for loan losses	(4,364)	(2,600)	2,772
Net interest income after provision for loan losses	58,563	57,338	50,192
Noninterest Income			
Service charges and fees on deposits	7,801	8,196	8,124
Allotment processing fees	5,014	4,922	5,215
Other service charges, commissions, and fees	5,248	4,983	4,478
Trust income	2,568	1,993	1,909
Investment securities (losses) gains, net	(63)	(50)	1,209
Gains on sale of mortgage loans, net	490	1,036	1,918
Income from company-owned life insurance	1,231	962	1,524
Other	984	74	277
Total noninterest income	23,273	22,116	24,654
Noninterest Expense			
Salaries and employee benefits	29,763	29,681	28,190
Occupancy expenses, net	4,881	4,767	4,757
Equipment expenses	2,498	2,398	2,364
Data processing and communications expenses	4,031	3,946	4,271
Bank franchise tax	2,421	2,354	2,381
Amortization of intangibles	405	540	1,014
Deposit insurance expense	1,746	2,265	2,690
Other real estate expenses, net	5,318	6,999	5,232
Legal expenses	856	780	1,220
Other	7,359	7,843	7,668
Total noninterest expense	59,278	61,573	59,787
Income before income taxes	22,558	17,881	15,059
Income tax expense	6,099	4,435	2,910
Net income	16,459	13,446	12,149

Less preferred stock dividends and discount accretion	1,927	1,951	1,922
Net income available to common shareholders	$14,532	$11,495	$10,227
Per Common Share			
Net income – basic and diluted	$1.94	$1.54	$1.37
Cash dividends declared	-	-	-
Weighted Average Common Shares Outstanding			
Basic and diluted	7,483	7,474	7,457

See accompanying notes to consolidated financial statements.

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Consolidated Statements of Comprehensive Income

(In thousands) Years Ended December 31,	2014	2013	2012
Net income	$16,459	$13,446	$12,149
Other comprehensive income (loss):			
Unrealized holding gain (loss) on available for sale securities arising during the period on securities held at end of period, net of tax of $4,703, $(6,996), and $543, respectively	8,734	(12,992)	1,009
Reclassification adjustment for prior period unrealized (gain) loss previously reported in other comprehensive income recognized during current period, net of tax of $(34), $23, and $330, respectively	63	(42)	(612)
Change in unfunded portion of postretirement benefit obligations, net of tax of $(382), $1,589, and $(92), respectively	(710)	2,953	(171)
Other comprehensive income (loss)	8,087	(10,081)	226
Comprehensive income	$24,546	$3,365	$12,375

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity

(In thousands, except per share data) Years Ended December 31, 2014, 2013, and 2012	Preferred Stock	Common Stock Shares	Common Stock Amount	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance at January 1, 2012	$29,115	7,446	$ 931	$50,848	$69,520	$ 6,643	$ 157,057
Net income	-	-	-	-	12,149	-	12,149
Other comprehensive income	-	-	-	-	-	226	226
Cash dividends declared - preferred, $50.00 per share	-	-	-	-	(1,500)	-	(1,500)
Preferred stock discount accretion	422	-	-	-	(422)	-	-
Repurchase of common stock warrant	-	-	-	(75)	-	-	(75)
Shares issued pursuant to employee stock purchase plan	-	24	3	125	-	-	128
Expense related to employee stock purchase plan	-	-	-	36	-	-	36
Balance at December 31, 2012	29,537	7,470	934	50,934	79,747	6,869	168,021
Net income	-	-	-	-	13,446	-	13,446
Other comprehensive loss	-	-	-	-	-	(10,081)	(10,081)
Cash dividends declared - preferred, $50.00 per share	-	-	-	-	(1,500)	-	(1,500)
Preferred stock discount accretion	451	-	-	-	(451)	-	-
Shares issued pursuant to employee stock purchase plan	-	9	1	132	-	-	133
Expense related to employee stock purchase plan	-	-	-	36	-	-	36
Balance at December 31, 2013	29,988	7,479	935	51,102	91,242	(3,212)	170,055
Net income	-	-	-	-	16,459	-	16,459
Other comprehensive income	-	-	-	-	-	8,087	8,087
Cash dividends declared - preferred, $85.13 per share	-	-	-	-	(1,915)	-	(1,915)
Preferred stock discount accretion	12	-	-	-	(12)	-	-
Redemption of preferred stock	(20,000)	-	-	-	-	-	(20,000)
Shares issued under director compensation plan	-	3	-	82	-	-	82
Shares issued pursuant to employee stock purchase plan	-	7	1	128	-	-	129
Expense related to employee stock purchase plan	-	-	-	32	-	-	32
Balance at December 31, 2014	$10,000	7,489	$ 936	$51,344	$105,774	$ 4,875	$ 172,929

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Years Ended December 31, (In thousands)	2014	2013	2012
Cash Flows from Operating Activities			
Net income	$16,459	$13,446	$12,149
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	4,065	4,114	4,543
Net premium amortization of investment securities:			
Available for sale	3,919	5,027	5,312
Held to maturity	42	-	-
Provision for loan losses	(4,364)	(2,600)	2,772
Deferred income tax expense (benefit)	3,931	(473)	(1,043)
Noncash employee stock purchase plan expense	32	36	36
Noncash director fee compensation	82	-	-
Mortgage loans originated for sale	(25,498)	(52,016)	(84,496)
Proceeds from sale of mortgage loans	29,254	50,957	86,563
Gains on sale of mortgage loans, net	(490)	(1,036)	(1,918)
(Gain) loss on disposal and write downs of premises and equipment, net	(5)	7	257
Net loss on sale and write downs of other real estate	3,404	5,702	4,084
Net loss (gain) on sale of available for sale investment securities	63	50	(1,209)
Increase in cash surrender value of company-owned life insurance	(926)	(926)	(961)
Death benefits in excess of cash surrender value on company-owned life insurance	(276)	-	(529)
Decrease in accrued interest receivable	276	173	545
(Increase) decrease in other assets	(1,860)	(241)	1,296
Decrease in accrued interest payable	(193)	(233)	(1,005)
Increase in other liabilities	1,096	2,036	2,014
Net cash provided by operating activities	29,011	24,023	28,410
Cash Flows from Investing Activities			
Proceeds from maturities and calls of investment securities:			
Available for sale	88,905	123,231	219,141
Held to maturity	60	55	55
Proceeds from sale of available for sale investment securities	12,967	2,233	135,193
Purchase of investment securities:			
Available for sale	(105,888)	(190,306)	(333,116)
Held to maturity	(3,065)	-	-
Proceeds from sale of restricted stock investments, net	148	-	-
Principal collected on loans originated for investment, net	56,695	5,540	29,818
Proceeds from death benefits of company-owned life insurance	738	-	1,051
Purchases of premises and equipment	(2,138)	(3,525)	(1,675)
Proceeds from sale of other real estate	8,811	9,458	12,278
Proceeds from disposals of premises and equipment	21	28	429
Net cash provided by (used in) investing activities	57,254	(53,286)	63,174
Cash Flows from Financing Activities			
Net decrease in deposits	(23,054)	(595)	(24,255)
Net (decrease) increase in federal funds purchased and other short-term borrowings	(533)	5,040	(2,939)

Proceeds from securities sold under agreements to repurchase and other long-term borrowings	9	754	-
Repayments of securities sold under agreements to repurchase and other long-term borrowings	(8,165)	(2,171)	(61,397)
Redemption of preferred stock	(20,000)	-	-
Dividends paid, preferred stock	(1,990)	(1,500)	(1,500)
Repurchase of common stock warrant	-	-	(75)
Shares issued under employee stock purchase plan	129	133	128
Net cash (used in) provided by financing activities	(53,604)	1,661	(90,038)
Net increase (decrease) in cash and cash equivalents	32,661	(27,602)	1,546
Cash and cash equivalents at beginning of year	68,253	95,855	94,309
Cash and cash equivalents at end of year	$100,914	$68,253	$95,855
Supplemental Disclosures			
Cash paid during the year for:			
Interest	$10,346	$12,228	$19,263
Income taxes	2,850	6,150	3,800
Transfers from loans to other real estate	8,259	6,110	33,913
Transfers from premises to other real estate	-	-	212
Sale and financing of other real estate	2,525	5,711	3,358

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

The accounting and reporting policies of Farmers Capital Bank Corporation and subsidiaries conform to accounting principles generally accepted in the United States of America ("U.S. GAAP") and general practices applicable to the banking industry. Significant accounting policies are summarized below.

Principles of Consolidation and Nature of Operations

The consolidated financial statements include the accounts of Farmers Capital Bank Corporation (the "Company" or "Parent Company"), a bank holding company, and its bank and nonbank subsidiaries. Bank subsidiaries include Farmers Bank & Capital Trust Company ("Farmers Bank") in Frankfort, KY, United Bank & Trust Company ("United Bank") in Versailles, KY, First Citizens Bank ("First Citizens") in Elizabethtown, KY, and Citizens Bank of Northern Kentucky, Inc. ("Citizens Northern") in Newport, KY.

Farmers Bank's significant subsidiaries include EG Properties, Inc., Leasing One Corporation ("Leasing One"), and Farmers Capital Insurance Corporation ("Farmers Insurance"). EG Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of Farmers Bank. Leasing One is a commercial leasing company in Frankfort, KY, and Farmers Insurance is an insurance agency in Frankfort, KY. United Bank has one wholly-owned subsidiary, EGT Properties, Inc. EGT Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of United Bank. First Citizens has one wholly-owned subsidiary, HBJ Properties, LLC. HBJ Properties, LLC is involved in real estate management and liquidation for certain repossessed properties of First Citizens. Citizens Northern has one wholly-owned subsidiary, ENKY Properties, Inc. ENKY Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of Citizens Northern.

The Company has two active nonbank subsidiaries, FCB Services, Inc. ("FCB Services") and FFKT Insurance Services, Inc. ("FFKT Insurance"). FCB Services is a data processing subsidiary located in Frankfort, KY that provides services to the Company's banks as well as unaffiliated entities. FFKT Insurance is a captive property and casualty insurance company insuring primarily deductible exposures and uncovered liability related to properties of the Company. EKT Properties, Inc., a company formed to manage and liquidate certain real estate properties repossessed by the Company, was dissolved effective at year end 2014. The Company has three subsidiaries organized as Delaware statutory trusts that are not consolidated into its financial statements. These trusts were formed for the purpose of issuing trust preferred securities. All significant intercompany transactions and balances are eliminated in consolidation.

The Company provides financial services at its 36 locations in 23 communities throughout Central and Northern Kentucky to individual, business, agriculture, government, and educational customers. Its primary deposit products are checking, savings, and term certificate accounts. Its primary lending products are residential mortgage, commercial lending, and consumer installment loans. Substantially all loans and leases are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Commercial loans and leases are expected to be repaid from cash flow from operations of businesses. Other services include, but are not limited to, cash management services, issuing letters of credit, safe deposit box rental, and providing funds transfer services. Other financial instruments, which potentially represent concentrations of credit risk, include deposit accounts in other financial institutions and federal funds sold.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP 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. Estimates used in the preparation of the financial statements are based on various factors including the current interest rate environment and the general strength of the local economy. Changes in the overall interest rate environment can significantly affect the Company's net interest income and the value of its recorded assets and liabilities. Actual results could differ from those estimates used in the preparation of the financial statements. The allowance for loan losses, carrying value of other real estate owned, actuarial assumptions used to calculate postretirement benefits, and the fair values of financial instruments are estimates that are particularly subject to change.

Reclassifications

Certain amounts in the accompanying consolidated financial statements presented for prior years have been reclassified to conform to the 2014 presentation. These reclassifications do not affect net income or total shareholders' equity as previously reported.

Segment Information

The Company provides a broad range of financial services to individuals, corporations, and others through its 36 banking locations throughout Central and Northern Kentucky. These services primarily include the activities of lending, receiving deposits, providing cash management services, safe deposit box rental, and trust activities. While the chief decision-makers monitor the revenue streams of the various products and services, operations are managed and financial performance is evaluated on a Company-wide basis. Operating segments are aggregated into one as operating results for all segments are similar. Accordingly, all of the financial service operations are considered by management to be aggregated in one reportable segment.

Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include the following: cash on hand, deposits from other financial institutions that have an initial maturity of less than 90 days when acquired by the Company, federal funds sold, and securities purchased under agreements to resell. Generally, federal funds sold and securities purchased under agreements to resell are purchased and sold for one-day periods. Net cash flows are reported for loan, deposit, and short-term borrowing transactions.

Investment Securities

Investments in debt and equity securities are classified into three categories. Securities that management has the positive intent and ability to hold until maturity are classified as held to maturity. Securities that are bought and held specifically for the purpose of selling them in the near term are classified as trading securities. The Company had no securities classified as trading during 2014, 2013, or 2012. All other securities are classified as available for sale. Securities are designated as available for sale if they might be sold before maturity. Securities classified as available for sale are carried at estimated fair value. Unrealized holding gains and losses for available for sale securities are reported net of deferred income taxes in other comprehensive income. Investments classified as held to maturity are carried at amortized cost. Amortized cost basis for investment securities includes adjustments made to the cost for previous other-than-temporary impairment ("OTTI") recognized in earnings, amortization, accretion, and collection of cash.

Interest income includes amortization and accretion of purchase premiums or discounts. Premiums and discounts on securities are amortized using the interest method over the expected life of the securities without anticipating prepayments, except for mortgage backed securities where prepayments are anticipated. Realized gains and losses on the sales of securities are recorded on the trade date and computed on the basis of specific identification of the adjusted cost of each security and are included in noninterest income.

The Company evaluates investment securities for OTTI at least on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. A decline in the market value of investment securities below cost that is deemed other-than-temporary results in a charge to earnings and the establishment of a new cost basis for the security. Substantially all of the Company’s investment securities are debt securities. In estimating OTTI for debt securities, management considers each of the following: (1) the length of time and extent to which fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether market decline was affected by macroeconomic conditions, and (4) whether the Company has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery in fair value. The assessment of whether an OTTI charge exists involves a high degree of subjectivity and judgment and is based on the information available to the Company at a point in time. The Company had no OTTI losses during any year in each of the three years in the period ended December 31, 2014.

Investment securities classified as available for sale or held-to-maturity are generally evaluated for OTTI under Financial Accounting Standard Board (“FASB”) Accounting Standards Codification™ (“ASC”) Topic 320, “*Investments-Debt and Equity Securities.”* In determining OTTI under ASC Topic 320 the Company considers many factors, including those enumerated above. When OTTI occurs, the amount of the OTTI recognized in earnings depends on whether the Company intends to sell the security or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis. If the Company intends to sell or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, OTTI is recognized in earnings equal to the entire difference between the investment’s amortized cost basis and its fair value at the balance sheet date. If the Company does not intend to sell the security and it is not more likely than not that it will be required to sell the security before recovery of its amortized cost basis, OTTI is separated into the amount representing the credit loss and the amount related to all other factors. The amount of the total OTTI related to the credit loss is determined based on the present value of cash flows expected to be collected and is recognized in earnings. The amount of the total OTTI related to other factors is recognized in other comprehensive income, net of applicable taxes. The previous amortized cost basis less OTTI recognized in earnings becomes the new amortized cost basis of the investment.

Federal Home Loan Bank and Federal Reserve Bank Stock

Federal Home Loan Bank (“FHLB”) and Federal Reserve Bank stock is carried at cost on the consolidated balance sheets under the caption “Other assets.” These stocks are classified as restricted securities and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income. The amount outstanding at December 31, 2014 and 2013 was $9.4 million and $9.5 million, respectively.

Loans and Interest Income

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their unpaid principal amount outstanding adjusted for any charge-offs and deferred fees or costs on originated loans. Interest income on loans is recognized using the interest method based on loan principal amounts outstanding during the period. Interest income also includes amortization and accretion of any premiums or discounts over the expected life of acquired loans at the time of purchase or business acquisition. Loan origination fees, net of certain direct origination costs, are deferred and amortized as yield adjustments over the contractual term of the loans.

The Company disaggregates certain disclosure information related to loans, the related allowance for loan losses, and credit quality measures by either portfolio segment or by loan class. The Company segregates its loan portfolio segments based on similar risk characteristics as follows: real estate loans, commercial loans, and consumer loans. Portfolio segments are further disaggregated into classes for certain required disclosures as follows:

Portfolio Segment	Class
Real estate loans	Real estate mortgage - construction and land development
	Real estate mortgage - residential
	Real estate mortgage - farmland and other commercial enterprises
Commercial loans	Commercial and industrial
	Depository institutions
	Agriculture production and other loans to farmers
	States and political subdivisions
	Leases
	Other
Consumer loans	Secured
	Unsecured

Loan disclosures include presenting certain disaggregated information based on recorded investment. The recorded investment in a loan includes its principal amount outstanding adjusted for certain items that include net deferred loan costs or fees, unamortized premiums or discounts, charge offs, and accrued interest. The Company had a total of $506 thousand and $492 thousand of net deferred loan costs at year-end 2014 and 2013, respectively, included in the carrying amount of loans on the balance sheet, which represents .05% of average loans outstanding for 2014 and 2013. The amount of net deferred loans costs are not material and are omitted from the computation of the recorded investment included in Note 4 that follows. Similarly, accrued interest receivable on loans was $3.1 million and $3.4 million at year-end 2014 and 2013, respectively, or .3% of average loans for both years and has also been omitted from certain information presented in Note 4.

The Company has a loan policy in place that is amended and approved from time to time as needed to reflect current economic conditions and product offerings in its markets. The policy establishes written procedures concerning areas such as the lending authorities of loan officers, committee review and approval of certain credit requests, underwriting criteria, policy exceptions, appraisal requirements, and loan review. Credit is extended to borrowers based primarily on their ability to repay as demonstrated by income and cash flow analysis.

Loans secured by real estate make up the largest segment of the Company’s loan portfolio. If a borrower fails to repay a loan secured by real estate, the Company may liquidate the collateral in order to satisfy the amount owed. Determining the value of real estate is a key component to the lending process for real estate backed loans. If the fair value of real estate (less estimated cost to sell) securing a collateral dependent loan declines below the outstanding loan amount, the Company will write down the carrying value of the loan and thereby incur a loss. The Company uses independent third party state certified or licensed appraisers in accordance with its loan policy to mitigate risk when underwriting real estate loans. Cash flow analysis of the borrower, loan to value limits as adopted by loan policy, and other customary underwriting standards are also in place which are designed to maximize credit quality and mitigate risks associated with real estate lending.

Commercial loans are made to businesses and are secured mainly by assets such as inventory, accounts receivable, machinery, fixtures and equipment, or other business assets. Commercial lending involves significant risk, as loan repayments are more dependent on the successful operation or management of the business and its cash flows. Consumer lending includes loans to individuals mainly for personal autos, boats, or a variety of other personal uses and may be secured or unsecured. Loan repayment associated with consumer loans is highly dependent upon the borrower’s continuing financial stability, which is heavily influenced by local unemployment rates. The Company mitigates its risk exposure to each of its loan segments by analyzing the borrower’s repayment capacity, imposing restrictions on the amount it will loan compared to estimated collateral values, limiting the payback periods, and following other customary underwriting practices as adopted in its loan policy.

The accrual of interest on loans is discontinued when it is determined that the collection of interest or principal is doubtful, or when a default of interest or principal has existed for 90 days or more, unless such loan is well secured and in the process of collection. Past due status is based on the contractual terms of the loan. Interest accrued but not received for a loan placed on nonaccrual status is reversed against interest income. Cash payments received on nonaccrual loans generally are applied to principal until qualifying for return to accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. The Company’s policy for placing a loan on nonaccrual status or subsequently returning a loan to accrual status does not differ based on its portfolio class or segment.

Commercial and real estate loans delinquent in excess of 120 days and consumer loans delinquent in excess of 180 days are charged off, unless the collateral securing the debt is of such value that any loss appears to be unlikely. In all cases, loans are charged off at an earlier date if classified as loss under the Company’s loan grading process or as a result of regulatory examination. The Company’s charge-off policy for impaired loans does not differ from the charge-off policy for loans outside the definition of impaired.

Loans Held for Sale

The Company’s operations include a limited amount of mortgage banking. Mortgage banking activities include the origination of fixed-rate residential mortgage loans for sale to various third-party investors. Mortgage loans originated and intended for sale in the secondary market, principally under programs with the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, and other commercial lending institutions are carried at the lower of cost or estimated fair value determined in the aggregate and included in net loans on the balance sheet until sold. These loans are sold with the related servicing rights either retained or released by the Company depending on the economic conditions present at the time of origination. Mortgage loans held for sale included in net loans totaled $380 thousand and $4.1 million at December 31, 2014 and December 31, 2013, respectively. Mortgage banking revenues, including origination fees, servicing fees, net gains on sales of mortgage loans, and other fee income were 1.1%, 1.6%, and 2.4% of the Company’s total revenue for the years ended December 31, 2014, 2013, and 2012, respectively.

Provision and Allowance for Loan Losses

The provision for loan losses represents charges or credits made to earnings to maintain an allowance for loan losses at a level considered adequate to provide for probable incurred credit losses at the balance sheet date. The allowance for loan losses is a valuation allowance increased by the provision for loan losses and decreased by net charge-offs. Loan losses are charged against the allowance when management believes the uncollectibility of a loan is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The Company estimates the adequacy of the allowance using a risk-rated methodology which is based on the Company's past loan loss experience, known and inherent risks in the loan portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral securing loans, composition of the loan portfolio, current economic conditions, and other relevant factors. This evaluation is inherently subjective as it requires significant judgment and the use of estimates that may be susceptible to change.

The allowance for loan losses consists of specific and general components. The specific component relates to loans that are individually classified as impaired. The general component covers non-impaired loans and is based on historical loss experience adjusted for current risk factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off. Actual loan losses could differ significantly from the amounts estimated by management.

The Company's risk-rated methodology includes segregating non-impaired watch list and past due loans from the general portfolio and allocating a loss percentage to these loans depending on their status. For example, watch list loans, which may be identified by the internal loan review risk-rating process or by regulatory examiner classification, are assigned a certain loss percentage while loans past due 30 days or more are assigned a separate loss percentage. Each of these loss rates considers past experience as well as current factors. The remainder of the general loan portfolio is segregated into portfolio segments having similar risk characteristics identified as follows: real estate loans, commercial loans, and consumer loans. Each of these portfolio segments is assigned a loss percentage based on their respective sixteen quarter rolling historical loss rates, adjusted for qualitative risk factors.

The qualitative risk factors used in the methodology are consistent with the guidance in the most recent Interagency Policy Statement on the Allowance for Loan Losses issued. Each factor is supported by a detailed analysis performed at each subsidiary bank and is both measureable and supportable. Some factors include a minimum allocation in some instances where loss levels are extremely low and it is determined to be prudent from a safety and soundness perspective. Qualitative risk factors that are used in the methodology include the following for each loan portfolio segment:

Delinquency trends
Trends in net charge-offs

Trends in loan volume
Lending philosophy risk
Management experience risk
Concentration of credit risk
Economic conditions risk

A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

The Company accounts for impaired loans in accordance with ASC Topic 310, *“Receivables.”* ASC Topic 310 requires that impaired loans be measured at the present value of expected future cash flows, discounted at the loan’s effective interest rate, at the loan’s observable market price, or at the fair value of the collateral if the loan is collateral dependent. Impaired loans may also be classified as nonaccrual. In many circumstances, however, the Company continues to accrue interest on an impaired loan. Cash receipts on accruing impaired loans are applied to the recorded investment in the loan, including any accrued interest receivable. Cash payments received on nonaccrual impaired loans generally are applied to principal until qualifying for return to accrual status. Loans that are part of a large group of smaller-balance homogeneous loans, such as residential mortgage, consumer, and smaller-balance commercial loans, are collectively evaluated for impairment. Troubled debt restructurings are measured at the present value of estimated future cash flows using the loan’s effective interest rate at inception, or at the fair value of collateral. The Company determines the amount of reserve for troubled debt restructurings that subsequently default in accordance with its accounting policy for the allowance for loan losses.

Mortgage Servicing Rights

Mortgage servicing rights are recognized in other assets on the Company’s consolidated balance sheet at their initial fair value on loans sold with servicing retained. Fair value is based on market prices for comparable mortgage servicing contracts when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. Mortgage servicing rights are subsequently measured using the amortization method in which the mortgage servicing right is expensed in proportion to, and over the period of, the estimated future net servicing income of the underlying loans. Impairment is evaluated based on the fair value of the rights, grouping the underlying loans by interest rates. Impairment of a grouping is reported as a valuation allowance. Capitalized mortgage servicing rights were $694 thousand and $785 thousand at December 31, 2014 and 2013, respectively. No impairment of the asset was determined to exist on either of these dates. Mortgage loans serviced for others totaled $206 million and $200 million at December 31, 2014 and 2013, respectively. Mortgage loans serviced for others are not included in the Company’s balance sheets.

Fair Value of Financial Instruments

Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in Note 19. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Loan Commitments and Related Financial Instruments

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

Intangible Assets

Intangible assets consist of core deposit and customer relationship intangible assets arising from business acquisitions. Intangible assets are initially measured at fair value and then amortized on an accelerated method over their estimated useful lives, which range between seven and ten years. Such assets are evaluated for impairment whenever changes in circumstances indicate that such an evaluation is necessary.

Other Real Estate Owned

Other real estate owned (“OREO”) and held for sale in the accompanying consolidated balance sheets includes properties acquired by the Company through, or in lieu of, actual loan foreclosures. OREO is initially carried at fair value less estimated costs to sell. Fair value of assets is generally based on third party appraisals of the property that includes comparable sales data. If the carrying amount exceeds fair value less estimated costs to sell, an impairment loss is recorded through expense. These assets are subsequently accounted for at the lower of carrying amount or fair value less estimated costs to sell. Operating costs after acquisition are expensed.

Income Taxes

Income tax expense is the total of current year income tax due or refundable and the change in deferred tax assets and liabilities, except for the deferred tax assets and liabilities related to business combinations or components of other comprehensive income. Deferred income tax assets and liabilities result from temporary differences between the tax basis of assets and liabilities and their reported amounts in the consolidated financial statements that will result in taxable or deductible amounts in future years. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in years in which those temporary differences are expected to be recovered or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through income tax expense. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

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

The Company files a consolidated federal income tax return with its subsidiaries. Federal income tax expense or benefit has been allocated to subsidiaries on a separate return basis. The Company's policy is to record the accrual of interest and/or penalties relative to income tax matters, if any, in income tax expense.

Premises and Equipment

Premises, equipment, and leasehold improvements are stated at cost less accumulated depreciation and amortization. Depreciation is computed primarily on the straight-line method over the estimated useful lives generally ranging from two to seven years for furniture and equipment and generally ten to 40 years for buildings and related components. Leasehold improvements are amortized over the shorter of the estimated useful lives or terms of the related leases on the straight-line method. Maintenance, repairs, and minor improvements are charged to operating expenses as incurred and major improvements are capitalized. The cost of assets sold or retired and the related accumulated depreciation are removed from the accounts and any resulting gain or loss is included in noninterest income. Land is carried at cost.

Company-owned Life Insurance

The Company has purchased life insurance policies on certain key employees with their knowledge and written consent. Company-owned life insurance is recorded on the consolidated balance sheet at its cash surrender value, which is the amount that can be realized under the insurance contract at the balance sheet date. The related change in cash surrender value and proceeds received under the policies are reported on the consolidated statements of income under the caption "Income from company-owned life insurance."

Related Party Transactions

In the ordinary course of business, the Company offers loan and deposit products to its directors, executive officers, and principal shareholders - including affiliated companies of which they are principal owners ("Related Parties"). These products are offered on substantially the same terms as those prevailing at the time for comparable transactions with unrelated parties, and these receivables and deposits are included in loans and deposits in the Company's consolidated balance sheets. Additional information related to these transactions can be found in Note 4 and Note 7.

The Company makes payments to Related Parties in the normal course of business for various services, primarily related to legal fees. For example, certain directors of the Parent Company and its subsidiary banks are partners in law firms that act as counsel to the Company. The following table represents the amount and type of payments to Related Parties, other than director fees, for the periods indicated:

(In thousands)			
	2014	2013	2012
Years Ended December 31,			
Legal fees	$212	$169	$445
Commissions and fees related to the sale of repossessed commercial real estate and property management	10	9	140
Insurance premiums/commissions	8	8	24
Other	9	6	-
Total	$239	$192	$609

Retirement Plans

The Company maintains a 401(k) salary savings plan and records expense based on the amount of its matching contributions of employee deferrals. The Company also has a nonqualified supplemental retirement plan for certain key employees that it acquired in connection with the Citizens Northern acquisition. Supplemental retirement plan expense allocates the benefits over years of service.

Net Income Per Common Share

Basic net income per common share is determined by dividing net income available to common shareholders by the weighted average total number of common shares issued and outstanding. Net income available to common shareholders represents net income adjusted for preferred stock dividends including dividends declared, accretion of discounts on preferred stock issuances, and cumulative dividends related to the current dividend period that have not been declared as of the end of the period.

Diluted net income per common share is determined by dividing net income available to common shareholders by the total weighted average number of common shares issued and outstanding plus amounts representing the dilutive effect of stock options outstanding and outstanding warrants. The effects of stock options and outstanding warrants are excluded from the computation of diluted earnings per common share in periods in which the effect would be antidilutive. Dilutive potential common shares are calculated using the treasury stock method.

Net income per common share computations were as follows for the years ended December 31, 2014, 2013, and 2012.

(In thousands, except per share data)

Years Ended December 31,	2014	2013	2012
Net income, basic and diluted	$16,459	$13,446	$12,149
Less preferred stock dividends and discount accretion	1,927	1,951	1,922
Net income available to common shareholders, basic and diluted	$14,532	$11,495	$10,227
Average common shares outstanding, basic and diluted	7,483	7,474	7,457
Net income per common share, basic and diluted	$1.94	$1.54	$1.37

Stock options for 22,049 and 24,049 shares of common stock were not included in the determination of diluted net income per common share for 2013 and 2012, respectively, because they were antidilutive. There were no stock options outstanding at year-end 2014.

Comprehensive Income

Comprehensive income is defined as the change in equity (net assets) of a business enterprise during a period from transactions and other events and circumstances from nonowner sources. For the Company this includes net income, the after tax effect of changes in the net unrealized gains and losses on available for sale investment securities, and the after tax changes to the funded status of postretirement benefit plans.

Dividend Restrictions

Banking regulations require maintaining certain capital levels which limit the amount of dividends paid to the Company by its bank subsidiaries. In addition, two of the Company's subsidiary banks must obtain regulatory approval to pay dividends as a result of agreements entered into related to recent examinations. Refer to Note 18 for additional information.

Restrictions on Cash

The Company is required to maintain funds in cash and/or on deposit with the Federal Reserve Bank in accordance with reserve requirements specified by the Federal Reserve Board of Governors. The required reserve was $20.5 million and $19.9 million at December 31, 2014 and 2013, respectively.

Equity

Outstanding common shares purchased by the Company are retired. When common shares are purchased, the Company allocates a portion of the purchase price of the common shares that are retired to each of the following balance sheet line items: common stock, capital surplus, and retained earnings. The Company did not purchase any of its outstanding common shares during 2014 or 2013.

Trust Assets

Assets of the Company's trust departments, other than cash on deposit at subsidiary banks, are not included in the accompanying financial statements because they are not assets of the Company.

Transfers of Financial Assets

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

Long-term Assets

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

Stock-Based Compensation

The Company recognizes compensation cost for its Employee Stock Purchase Plan ("ESPP") and for stock options granted based on the fair value of these awards at the date of grant. A Black-Scholes model is utilized to estimate the fair value of ESPP and stock option awards. Compensation cost is recognized over the required service period, generally defined as the vesting period, on a straight-line basis. There have been no stock options granted by the Company since 2004. All previously outstanding options expired in 2014.

The ESPP was approved by the Company's shareholders in 2004. The purpose of the ESPP is to provide a means by which eligible employees may purchase, at a discount, shares of the Company's common stock through payroll withholding. The purchase price of the shares is equal to 85% of their fair market value on specified dates as defined in the plan. The ESPP was effective beginning July 1, 2004. There were 6,894, 8,893, and 23,368 shares issued under the plan during 2014, 2013, and 2012, respectively. Compensation expense related to the ESPP included in the accompanying statements of income was $32 thousand, $36 thousand, and $36 thousand in 2014, 2013, and 2012, respectively.

Following are the weighted average assumptions used and estimated fair market value for the ESPP, which is considered a compensatory plan under ASC Topic 718, "*Compensation-Stock Compensation.*"

	ESPP		
	2014	2013	2012
Expected volatility	37.4%	45.7%	53.5%
Dividend yield	-	-	-
Risk-free interest rate	.04	.06	.07
Expected life (in years)	.25	.25	.25
Fair value	$4.69	$4.01	$1.54

Recently Issued But Not Yet Effective Accounting Standards

In April 2014, the FASB issued Accounting Standards Update ("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.* This ASU changes the requirements for reporting discontinued operations and seeks to enhance the FASB and International Accounting Standards Board's ("IASB") convergence project regarding such reporting requirements. A discontinued operation may include a component of an entity, a group of components of an entity, a business or a non-profit activity. A disposal of a component of an entity or a group of components of an entity is required to be reported in discontinued operations if the disposal represents a strategic shift that has, or will have, a major effect on an entity's operations and financial results. This ASU, which is intended to reduce the frequency of disposals reported as discontinued operations, requires additional disclosures regarding discontinued operations. Those disclosures include among others, the requirement that an entity present, for each comparative period, the assets and liabilities of a disposal group that includes a discontinued operation separately in the asset and liability sections, respectively, of the statement of financial position.

For the Company, the guidance of ASU 2014-08 is effective prospectively for annual periods beginning on or after December 15, 2014, and interim periods within that year. The Company does not expect there to be a material impact on its consolidated financial position, results of operations, or cash flows upon adoption.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, as part of a joint project with the IASB to clarify revenue-recognition principles and develop a common revenue standard for U.S. GAAP and International Financial Reporting Standards ("IFRS"). ASU No. 2014-09 is expected to remove inconsistencies and weaknesses in revenue requirements and improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets. The scope of the new ASU includes all contracts with customers to provide goods or services in the ordinary course of business, except the following contracts that are specifically excluded from the scope:

Lease contracts within the scope of ASC 840

- Insurance contracts within the scope of ASC 944
- Financial instruments and other contractual rights or obligations (e.g., receivables, debt and equity securities, derivatives)
- Guarantees (other than product or service warranties) within the scope of ASC 460
- Nonmonetary exchanges between entities in the same line of business to facilitate sales to customers other than the parties to the exchange

The primary principle of ASU 2014-09 is that entities 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. To achieve this core principle, the guidance provides that an entity should apply the following steps: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when, or as, the entity satisfies a performance obligation.

The amendments in this ASU are effective for the Company in annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. Entities should apply the amendments either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying this ASU recognized at the date of initial application. If an entity elects the second method, then it should also provide the additional disclosures in reporting periods that include the date of initial application of (1) the amount by which each financial statement line item is affected in the current reporting period, as compared to the guidance that was in effect before the change, and (2) an explanation of the reasons for significant changes. The Company is evaluating the potential impact of ASU 2014-09 on its consolidated financial position, results of operations, and cash flows.

In June 2014, the FASB issued ASU No. 2014-11, *Transfers and Servicing (Topic 860) - Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures*. This ASU amends guidance on the accounting for certain repurchase agreements. The new ASU (1) requires entities to account for repurchase-to-maturity transactions as secured borrowings (rather than as sales with forward repurchase agreements), (2) eliminates accounting guidance on linked repurchase financing transactions, and (3) expands disclosure requirements related to certain transfers of financial assets that are accounted for as sales and certain transfers (specifically, repos, securities lending transactions, and repurchase-to-maturity transactions) accounted for as secured borrowings. The accounting changes in this ASU are effective for the first interim or annual period beginning after December 15, 2014. In addition, the disclosure for certain transactions accounted for as a sale are effective for the first interim or annual period beginning on or after December 15, 2014, and the disclosure for transactions accounted for as secured borrowings is required to be presented for annual periods beginning after December 15, 2014, and interim periods beginning after March 15, 2015. The Company does not expect there to be a material impact on its consolidated financial position, results of operations, or cash flows upon adoption.

In August 2014, the FASB issued ASU 2014-14, *Receivables-Troubled Debt Restructurings by Creditors (Subtopic 310-40) - Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure (a consensus of the FASB Emerging Issues Task Force).* The ASU requires that, upon foreclosure, a guaranteed mortgage loan be derecognized and a separate other receivable be recognized when specific criteria are met. The amendments in this ASU are effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. The Company does not expect there to be a material impact on its consolidated financial position, results of operations, or cash flows upon adoption.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company’s financial position, results of operations or cash flows.

2. Accumulated Other Comprehensive Income

The following table presents changes in accumulated other comprehensive income by component, net of tax, for the periods indicated.

Year Ended December 31,	2014			2013		
(In thousands)	Unrealized Gains and Losses on Available for Sale Investment Securities	Postretirement Benefit Obligation	Total	Unrealized Gains and Losses on Available for Sale Investment Securities	Postretirement Benefit Obligation	Total
Beginning balance	$(3,623)	$ 411	$(3,212)	$9,411	$ (2,542)	$6,869
Other comprehensive income (loss) before reclassifications	8,734	(801)	7,933	(12,992)	2,778	(10,214)
Amounts reclassified from accumulated other comprehensive income	63	91	154	(42)	175	133
Net current-period other comprehensive income (loss)	8,797	(710)	8,087	(13,034)	2,953	(10,081)
Ending balance	$5,174	$ (299)	$4,875	$(3,623)	$ 411	$(3,212)

The following table presents amounts reclassified out of accumulated other comprehensive income by component for the period indicated. Line items in the statement of income affected by the reclassification are also presented.

(In thousands)	Amount Reclassified from Accumulated Other Comprehensive Income		Affected Line Item in the Statement Where Net Income is Presented
Year Ended December 31,	2014	2013	
Unrealized gains and losses on available for sale investment securities	$ (97)	$ 65	Investment securities (losses) gains, net
	34	(23)	Income tax expense
	$ (63)	$ 42	Net of tax
Amortization related to postretirement benefits			
Prior service costs	$ (207)	$ (257)	Salaries and employee benefits
Actuarial gains (losses)	67	(12)	Salaries and employee benefits

		(140	)		(269	)	Total before tax
		49			94		Income tax expense
	$	(91	)	$	(175	)	Net of tax
Total reclassifications for the period	$	(154	)	$	(133	)	Net of tax

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3. Investment Securities

The following tables summarize the amortized cost and estimated fair values of the securities portfolio at December 31, 2014 and 2013 and the corresponding amounts of gross unrealized gains and losses. The summary is divided into available for sale and held to maturity securities.

December 31, 2014 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available For Sale				
Obligations of U.S. government-sponsored entities	$ 110,094	$ 369	$ 1,015	$ 109,448
Obligations of states and political subdivisions	133,563	2,600	397	135,766
Mortgage-backed securities – residential	363,729	7,959	1,199	370,489
Mortgage-backed securities – commercial	2,515	7	10	2,512
Corporate debt securities	6,639	26	358	6,307
Mutual funds and equity securities	1,889	2	25	1,866
Total securities – available for sale	$ 618,429	$ 10,963	$ 3,004	$ 626,388
Held To Maturity				
Obligations of states and political subdivisions	$ 3,728	$ 195	$ -	$ 3,923

December 31, 2013 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available For Sale				
Obligations of U.S. government-sponsored entities	$ 96,750	$ 155	$ 3,155	$ 93,750
Obligations of states and political subdivisions	132,311	2,056	2,397	131,970
Mortgage-backed securities – residential	379,238	5,071	6,232	378,077
Mortgage-backed securities – commercial	748	-	59	689
Corporate debt securities	7,266	40	1,049	6,257
Mutual funds and equity securities	2,082	15	20	2,077
Total securities – available for sale	$ 618,395	$ 7,337	$ 12,912	$ 612,820
Held To Maturity				
Obligations of states and political subdivisions	$ 765	$ 62	$ -	$ 827

At year-end 2014 and 2013, the Company held no investment securities of any single issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of shareholders' equity.

The amortized cost and estimated fair value of the securities portfolio at December 31, 2014, by contractual maturity, are detailed below. The summary is divided into available for sale and held to maturity securities. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. Mutual funds and equity securities in the available for sale portfolio at December 31, 2014 consist of investments by the Company’s captive insurance subsidiary. These securities have no stated maturity and are not included in the maturity schedule that follows.

Mortgage-backed securities are stated separately due to the nature of payment and prepayment characteristics of these securities, as principal is not due at a single date.

	Available For Sale		Held To Maturity	
December 31, 2014 (In thousands)	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$7,951	$7,970	$-	$ -
Due after one year through five years	144,282	144,933	-	-
Due after five years through ten years	82,454	82,996	705	799
Due after ten years	15,609	15,622	3,023	3,124
Mortgage-backed securities	366,244	373,001	-	-
Total	$616,540	$624,522	$3,728	$ 3,923

Gross realized gains and losses on the sale of available for sale investment securities were as follows for the year indicated.

(In thousands)	2014	2013	2012
Gross realized gains	$190	$14	$1,349
Gross realized losses	253	64	140
Net realized (loss) gain	$(63)	$(50)	$1,209
Income tax (benefit) provision related to net realized (loss) gain	$(22)	$(18)	$423

Investment securities with a carrying value of $294 million and $277 million at December 31, 2014 and 2013 were pledged to secure public and trust deposits, repurchase agreements, and for other purposes.

Investment securities with unrealized losses at year-end 2014 and 2013 not recognized in income are presented in the tables below. The tables segregate investment securities that have been in a continuous unrealized loss position for less than twelve months from those that have been in a continuous unrealized loss position for twelve months or more. The table also includes the fair value of the related securities.

	Less than 12 Months		12 Months or More		Total	
December 31, 2014 (In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	$22,696	$ 76	$60,892	$ 939	$83,588	$ 1,015

Obligations of U.S. government-sponsored entities						
Obligations of states and political subdivisions	20,746	81	21,272	316	42,018	397
Mortgage-backed securities – residential	37,451	82	71,311	1,117	108,762	1,199
Mortgage-backed securities – commercial	-	-	723	10	723	10
Corporate debt securities	76	4	5,525	354	5,601	358
Mutual funds and equity securities	305	11	95	14	400	25
Total	$81,274	$ 254	$159,818	$ 2,750	$241,092	$ 3,004

December 31, 2013 (In thousands)	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. government-sponsored entities	$65,094	$ 2,434	$11,830	$ 721	$76,924	$ 3,155
Obligations of states and political subdivisions	48,715	1,594	15,095	803	63,810	2,397
Mortgage-backed securities – residential	219,032	5,199	16,306	1,033	235,338	6,232
Mortgage-backed securities – commercial	689	59	-	-	689	59
Corporate debt securities	80	-	4,816	1,049	4,896	1,049
Mutual funds and equity securities	716	17	22	3	738	20
Total	$334,326	$ 9,303	$48,069	$ 3,609	$382,395	$ 12,912

Unrealized losses included in the tables above have not been recognized in income since they have been identified as temporary. The Company evaluates investment securities for other-than-temporary impairment at least quarterly, and more frequently when economic or market conditions warrant. Many factors are considered, including: (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, (3) whether the market decline was effected by macroeconomic conditions, and (4) whether the Company has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. The assessment of whether an OTTI charge exists involves a high degree of subjectivity and judgment and is based on the information available to the Company at a point in time.

At December 31, 2014, the Company's investment securities portfolio had gross unrealized losses of $3.0 million, a decrease of $9.9 million compared to year-end 2013. Of the total gross unrealized losses at December 31, 2014, $2.8 million or 91.5% relates to investments that have been in a continuous loss position for 12 months or more. Unrealized losses on mortgage-backed securities make up $1.1 million of the total unrealized loss on investment securities in a continuous loss position of 12 months or more.

Corporate debt securities in the Company's investment securities portfolio at December 31, 2014 include single-issuer trust preferred capital securities with an unrealized loss of $354 thousand and a carrying value of $5.5 million. This is an improvement in the unrealized loss of $694 thousand or 66.2% from year end 2013. These securities were issued by a national and global financial services firm and were purchased by the Company during 2007. The securities are currently performing and continue to be rated as investment grade by major rating agencies. The issuer of the securities announced in the first quarter of 2014 an increase in per share common dividend payments and authorization of a common equity purchase plan. The Company does not intend to sell these securities nor does it believe it is likely that it will be required to sell these securities prior to their anticipated recovery. The Company believes these securities are not impaired due to reasons of credit quality or other factors, but rather the unrealized loss is primarily attributed to continuing uncertainties in both international and domestic economies and market volatility. The Company believes that it will collect all amounts due according to the contractual terms of these securities and that the fair values of these securities will recover as they approach their maturity dates.

The Company attributes the unrealized losses in other sectors of its investment securities portfolio to changes in market interest rates and volatility. Investment securities with unrealized losses at December 31, 2014 are performing according to their contractual terms, and the Company does not expect to incur a loss on these securities unless they are sold prior to maturity. The Company does not have the intent to sell these securities nor does it believe it is likely that it will be required to sell these securities prior to their anticipated recovery. The Company does not consider any of the securities to be impaired due to reasons of credit quality or other factors.

4. Loans and Allowance for Loan Losses

Major classifications of loans are summarized in the following table.

December 31, (In thousands)	2014	2013
Real Estate:		
Real estate mortgage – construction and land development	$97,045	$101,352
Real estate mortgage – residential	361,022	371,582
Real estate mortgage – farmland and other commercial enterprises	375,277	418,147
Commercial:		
Commercial and industrial	47,112	47,426
States and political subdivisions	22,369	21,561
Lease financing	159	902
Other	15,547	23,840
Consumer:		
Secured	7,963	8,579
Unsecured	5,450	6,513
Total loans	931,944	999,902
Less unearned income	1	19
Total loans, net of unearned income	$931,943	$999,883

Loans with a carrying value of $441 million and $484 million at December 31, 2014 and December 31, 2013, respectively, were pledged to secure borrowings and lines of credit. Such borrowings primarily include FHLB advances and short-term borrowing arrangements with the Federal Reserve.

Loans to directors, executive officers, and principal shareholders of the Parent Company and its subsidiaries (including loans to affiliated companies of which they are principal owners) and loans to members of the immediate family of such persons were $17.9 million at December 31, 2014. Such loans were made in the normal course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other customers and did not involve more than the normal risk of collectability. An analysis of the activity with respect to these loans is presented in the table below.

(In thousands)	Amount
Balance at December 31, 2013	$18,065
New loans	5,356
Repayments	(5,537)
Loans no longer meeting disclosure requirements, new loans meeting disclosure requirements, and other adjustments, net	40
Balance at December 31, 2014	$17,924

Activity in the allowance for loan losses by portfolio segment was as follows for each of the three years in the period ended December 31, 2014:

(In thousands)	Real Estate	Commercial	Consumer	Total
2014				
Balance at beginning of period	$18,716	$ 1,409	$ 452	$20,577
Provision for loan losses	(4,922)	620	(62)	(4,364)
Recoveries	624	786	97	1,507
Loans charged off	(1,876)	(1,662)	(214)	(3,752)
Balance at end of period	$12,542	$ 1,153	$ 273	$13,968
2013				
Balance at beginning of period	$22,254	$ 1,513	$ 678	$24,445
Provision for loan losses	(2,432)	(2)	(166)	(2,600)
Recoveries	327	155	221	703
Loans charged off	(1,433)	(257)	(281)	(1,971)
Balance at end of period	$18,716	$ 1,409	$ 452	$20,577
2012				
Balance at beginning of period	$23,538	$ 3,508	$ 1,218	$28,264
Provision for loan losses	4,930	(1,825)	(333)	2,772
Recoveries	666	145	234	1,045
Loans charged off	(6,880)	(315)	(441)	(7,636)
Balance at end of period	$22,254	$ 1,513	$ 678	$24,445

The following tables present individually impaired loans by class of loans for the dates indicated.

As of and for the Year Ended December 31, 2014 (In thousands)	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Allowance for Loan Losses Allocated	Average	Interest Income Recognized	Cash Basis Interest Recognized
Real Estate								
Real estate mortgage – construction and land development	$13,656	$ 6,902	$ 3,917	$ 10,819	$ 744	$13,557	$ 424	$ 423
Real estate mortgage – residential	10,256	3,473	6,649	10,122	1,172	11,254	550	535
Real estate mortgage – farmland and other commercial enterprises	23,003	5,247	17,649	22,896	1,359	28,711	1,088	1,070
Commercial								
Commercial and industrial	93	22	71	93	71	255	6	5
Consumer								
Secured	-	-	-	-	-	6	-	-
Unsecured	25	-	25	25	25	54	4	4

Total	$47,033	$ 15,644	$ 28,311	$ 43,955	$ 3,371	$53,837	$ 2,072	$ 2,037

As of and for the Year Ended December 31, 2013 (In thousands)	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Allowance for Loan Losses Allocated	Average	Interest Income Recognized	Cash Basis Interest Recognized
Real Estate								
Real estate mortgage – construction and land development	$ 17,234	$ 9,742	$ 4,699	$ 14,441	$ 930	$ 17,314	$ 509	$ 461
Real estate mortgage – residential	11,595	2,871	8,612	11,483	1,443	12,727	460	445
Real estate mortgage – farmland and other commercial enterprises	32,102	12,262	19,746	32,008	1,443	32,785	1,546	1,519
Commercial								
Commercial and industrial	311	24	293	317	200	994	40	40
Consumer								
Secured	18	-	18	18	15	19	1	1
Unsecured	71	-	72	72	71	147	9	9
Total	$ 61,331	$ 24,899	$ 33,440	$ 58,339	$ 4,102	$ 63,986	$ 2,565	$ 2,475

Year Ended December 31, 2012 (In thousands)	Average	Interest Income Recognized	Cash Basis Interest Recognized
Real Estate			
Real estate mortgage – construction and land development	$ 34,880	$ 871	$ 804
Real estate mortgage – residential	13,754	333	324
Real estate mortgage – farmland and other commercial enterprises	38,077	1,859	1,876
Commercial			
Commercial and industrial	403	17	17
Consumer			
Secured	66	6	6
Unsecured	271	17	16
Total	$ 87,451	$ 3,103	$ 3,043

The following tables present the balance of the allowance for loan losses and the recorded investment in loans by portfolio segment based on impairment method as of December 31, 2014 and 2013.

December 31, 2014 (In thousands)	Real Estate	Commercial	Consumer	Total
Allowance for Loan Losses				

Ending allowance balance attributable to loans:				
Individually evaluated for impairment	$3,275	$ 71	$ 25	$3,371
Collectively evaluated for impairment	9,267	1,082	248	10,597
Total ending allowance balance	$12,542	$ 1,153	$ 273	$13,968
Loans				
Loans individually evaluated for impairment	$43,837	$ 93	$ 25	$43,955
Loans collectively evaluated for impairment	789,507	85,093	13,388	887,988
Total ending loan balance, net of unearned income	$833,344	$ 85,186	$ 13,413	$931,943

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December 31, 2013 (In thousands)	Real Estate	Commercial	Consumer	Total
Allowance for Loan Losses				
Ending allowance balance attributable to loans:				
Individually evaluated for impairment	$3,816	$ 200	$ 86	$4,102
Collectively evaluated for impairment	14,900	1,209	366	16,475
Total ending allowance balance	$18,716	$ 1,409	$ 452	$20,577
Loans				
Loans individually evaluated for impairment	$57,932	$ 317	$ 90	$58,339
Loans collectively evaluated for impairment	833,149	93,393	15,002	941,544
Total ending loan balance, net of unearned income	$891,081	$ 93,710	$ 15,092	$999,883

The following tables present the recorded investment in nonperforming loans by class of loans as of December 31, 2014 and 2013.

December 31, 2014 (In thousands)	Nonaccrual	Restructured Loans	Loans Past Due 90 Days or More and Still Accruing
Real Estate:			
Real estate mortgage – construction and land development	$ 3,744	$ 3,742	$ -
Real estate mortgage – residential	3,474	4,674	-
Real estate mortgage – farmland and other commercial enterprises	4,202	16,004	-
Commercial:			
Commercial and industrial	81	-	-
Other	7	-	-
Consumer:			
Unsecured	-	9	-
Total	$ 11,508	$ 24,429	$ -

December 31, 2013 (In thousands)	Nonaccrual	Restructured Loans	Loans Past Due 90 Days or More and Still Accruing
Real Estate:			
Real estate mortgage – construction and land development	$ 5,821	$ 4,391	$ -
Real estate mortgage – residential	5,154	4,826	10

Real estate mortgage – farmland and other commercial enterprises	12,677	16,987	434
Commercial:			
Commercial and industrial	160	-	-
Lease financing	22	-	-
Consumer:			
Secured	3	-	-
Unsecured	1	51	-
Total	$ 23,838	$ 26,255	$ 444

The Company has allocated $2.2 million and $2.7 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings and that are in compliance with those terms as of December 31, 2014 and 2013, respectively. The Company had no commitments to lend additional amounts to customers with outstanding loans that are classified as troubled debt restructurings at December 31, 2014 and 2013.

The Company had no credits during 2014 that were modified as troubled debt restructurings. The Company had eight credits in 2013 that were modified as troubled debt restructurings. Seven of those credits with an aggregate recorded investment of $338 thousand represent debt by borrowers discharged under Chapter 7 bankruptcy. The borrower in each case did not reaffirm their debt, and the release of personal liability by the court was deemed a concession. However, each borrower continues to make payments under the original terms of the loan agreement. The remaining restructuring consisted of a credit secured by commercial real estate whereby the maturity date was extended 48 months.

The following table presents loans by class modified as troubled debt restructurings that occurred during the year ended December 31, 2013. There were no loans modified as troubled debt restructurings during 2014.

(Dollars in thousands) Troubled Debt Restructurings:	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
2013			
Real Estate:			
Real estate mortgage – residential	3	$ 309	$ 309
Real estate mortgage – farmland and other commercial enterprises	1	598	598
Commercial:			
Commercial and industrial	1	13	13
Consumer:			
Secured	3	16	16
Total	8	$ 936	$ 936

The troubled debt restructurings identified above increased the allowance for loan losses by $37 thousand for 2013. There were no charge-offs related to these loans.

There were no payment defaults during 2014 for credits that were restructured during the previous twelve months. For 2013, the Company had one restructured credit for which there was a payment default within twelve months following the modification. This credit was secured by residential real estate with an outstanding balance of $8 thousand at year-end 2014. No charge-offs have been recorded for this credit.

The tables below present an age analysis of past due loans 30 days or more by class of loans as of the dates indicated. Past due loans that are also classified as nonaccrual are included in their respective past due category.

December 31, 2014 (In thousands)	30-89 Days Past Due	90 Days or More Past Due	Total	Current	Total Loans	Loans Past Due 90 Days or More and Still Accruing	Nonaccrual Loans
Real Estate:							
Real estate mortgage – construction and land development	$-	$272	$272	$96,773	$97,045	$ -	$ 3,744
Real estate mortgage – residential	1,395	1,595	2,990	358,032	361,022	-	3,474
Real estate mortgage – farmland and other commercial enterprises	75	3,484	3,559	371,718	375,277	-	4,202
Commercial:							
Commercial and industrial	-	13	13	47,099	47,112	-	81
States and political subdivisions	-	-	-	22,369	22,369	-	-
Lease financing, net	-	-	-	158	158	-	-
Other	40	7	47	15,500	15,547	-	7
Consumer:							
Secured	58	-	58	7,905	7,963	-	-
Unsecured	16	1	17	5,433	5,450	-	-
Total	$1,584	$5,372	$6,956	$924,987	$931,943	$ -	$ 11,508

December 31, 2013 (In thousands)	30-89 Days Past Due	90 Days or More Past Due	Total	Current	Total Loans	Loans Past Due 90 Days or More and Still Accruing	Nonaccrual Loans
Real Estate:							
Real estate mortgage– construction and land development	$58	$613	$671	$100,681	$101,352	$ -	$ 5,821
Real estate mortgage – residential	1,225	2,502	3,727	367,855	371,582	10	5,154
Real estate mortgage – farmland and other commercial enterprises	3,548	7,978	11,526	406,621	418,147	434	12,677
Commercial:							
Commercial and industrial	71	53	124	47,302	47,426	-	160
States and political subdivisions	-	-	-	21,561	21,561	-	-
Lease financing, net	-	22	22	861	883	-	22
Other	56	-	56	23,784	23,840	-	-
Consumer:							
Secured	41	3	44	8,535	8,579	-	3

Unsecured	58	1	59	6,454	6,513	-	1
Total	$5,057	$11,172	$16,229	$983,654	$999,883	$ 444	$ 23,838

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends and conditions. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis includes large-balance loans and non-homogeneous loans, such as commercial real estate and certain residential real estate loans. Loan rating grades, as described further below, are assigned based on a continuous process. The amount and adequacy of the allowance for loan loss is determined on a quarterly basis. The Company uses the following definitions for its risk ratings:

Special Mention. Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the borrower’s repayment ability, weaken the collateral or inadequately protect the Company’s credit position at some future date. These credits pose elevated risk, but their weaknesses do not yet justify a substandard classification.

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

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

Loans not meeting the criteria above which are analyzed individually as part of the above described process are considered to be pass rated loans, which are considered to have a low risk of loss. Based on the most recent analysis performed, the risk category of loans by class of loans is as follows for the dates indicated. Each of the following tables excludes immaterial amounts attributed to accrued interest receivable.

	Real Estate			Commercial			
December 31, 2014 (In thousands)	Real Estate Mortgage -Construction and Land Development	Real Estate Mortgage -Residential	Real Estate Mortgage -Farmland and Other Commercial Enterprises	Commercial and Industrial	States and Political Subdivisions	Lease Financing	Other
Credit risk profile by internally assigned rating grades:							
Pass	$81,438	$ 326,124	$ 327,019	$45,665	$ 22,369	$ 158	$15,526

Special Mention	2,674	16,429	27,855	946	-	-	14
Substandard	12,933	18,469	19,941	501	-	-	7
Doubtful	-	-	462	-	-	-	-
Total	$97,045	$ 361,022	$ 375,277	$47,112	$ 22,369	$ 158	$15,547

December 31, 2013 (In thousands)	Real Estate Real Estate Mortgage -Construction and Land Development	Real Estate Mortgage-Residential	Real Estate Mortgage-Farmland and Other Commercial Enterprises	Commercial Commercial and Industrial	States and Political Subdivisions	Lease Financing	Other
Credit risk profile by internally assigned rating grades:							
Pass	$77,873	$ 334,104	$ 352,238	$45,652	$ 21,561	$ 861	$23,820
Special Mention	7,755	15,120	29,156	963	-	-	-
Substandard	15,724	22,358	36,753	735	-	22	20
Doubtful	-	-	-	76	-	-	-
Total	$101,352	$ 371,582	$ 418,147	$47,426	$ 21,561	$ 883	$23,840

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

	December 31, 2014		December 31, 2013	
	Consumer		Consumer	
(In thousands)	Secured	Unsecured	Secured	Unsecured
Credit risk profile based on payment activity:				
Performing	$7,963	$ 5,441	$8,576	$ 6,461
Nonperforming	-	9	3	52
Total	$7,963	$ 5,450	$8,579	$ 6,513

5. Other Real Estate Owned

OREO was as follows as of the date indicated:

December 31, (In thousands)	2014	2013
Construction and land development	$17,628	$23,504
Residential real estate	2,219	2,695
Farmland and other commercial enterprises	12,113	11,627
Total	$31,960	$37,826

OREO activity for 2014 and 2013 was as follows:

(In thousands)	2014	2013
Beginning balance	$37,826	$52,562
Transfers from loans and other increases	8,874	6,110
Proceeds from sales, net	(11,336)	(15,169)
Loss on sales, net	(776)	(182)
Write downs and other decreases, net	(2,628)	(5,495)
Ending balance	$31,960	$37,826

6. Premises and Equipment

Premises and equipment consist of the following.

December 31, (In thousands)	2014	2013
Land, buildings, and leasehold improvements	$59,681	$58,770
Furniture and equipment	18,290	18,561
Total premises and equipment	77,971	77,331
Less accumulated depreciation and amortization	43,038	41,058
Premises and equipment, net	$34,933	$36,273

Depreciation and amortization of premises and equipment was $3.5 million, $3.4 million, and $3.4 million for 2014, 2013, and 2012, respectively.

7. Deposit Liabilities

Major classifications of deposits are summarized as follows for the dates indicated:

December 31, (In thousands)	2014	2013
Noninterest Bearing	$292,788	$277,294
Interest Bearing		
Demand	335,657	320,503
Savings	363,185	340,903
Time	395,531	471,515
Total interest bearing	1,094,373	1,132,921
Total Deposits	$1,387,161	$1,410,215

At December 31, 2014, the scheduled maturities of time deposits were as follows:

(In thousands)	Amount
2015	$233,322
2016	88,580
2017	45,424
2018	19,989
2019	4,959
Thereafter	3,257
Total	$395,531

Time deposits that meet or exceed the Federal Deposit Insurance Corporation (“FDIC”) limit of $250 thousand were $28.0 million and $30.4 million at December 31, 2014 and 2013, respectively.

Deposits from directors, executive officers, and principal shareholders of the Parent Company and its subsidiaries (including deposits from affiliated companies of which they are principal owners) and deposits from members of the immediate family of such persons were $19.8 million and $19.0 million at December 31, 2014 and 2013, respectively. Such deposits were accepted in the normal course of business on substantially the same terms as those prevailing at the time for comparable transactions with other customers.

8. Federal Funds Purchased and Other Short-term Borrowings

Federal funds purchased and other short-term borrowings represent borrowings with an original maturity of less than one year. All of the Company's short-term borrowings are made up of federal funds purchased and securities sold under agreements to repurchase, which represent borrowings that generally mature one business day following the date of the transaction. Information on federal funds purchased and other short-term borrowings is as follows:

December 31, (Dollars in thousands)	2014			2013		
Federal funds purchased and securities sold under agreement to repurchase	$	28,590		$	29,123	
Total short-term	$	28,590		$	29,123	
Average balance during the year	$	30,428		$	29,440	
Maximum month-end balance during the year		33,568			32,885	
Average interest rate during the year		.18	%		.25	%
Average interest rate at year-end		.16			.25	

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9. Securities Sold Under Agreements to Repurchase and Other Long-term Borrowings

Long-term securities sold under agreements to repurchase and other borrowings represent borrowings with an original maturity of one year or more. The table below displays a summary of the ending balance and average rate for borrowed funds on the dates indicated.

December 31, (Dollars in thousands)	2014	Average Rate		2013	Average Rate	
Federal Home Loan Bank advances	$18,961	3.99	%	$27,126	4.14	%
Subordinated notes payable	48,970	1.71		48,970	1.71	
Securities sold under agreements to repurchase	100,763	3.92		100,754	3.92	
Total long-term borrowings	$168,694	3.29	%	$176,850	3.34	%

Long-term FHLB advances are made pursuant to several different credit programs, which have their own interest rates and range of maturities. At December 31, 2014, interest rates on all FHLB advances are fixed and range between 2.99% and 5.81%, averaging 3.99%, over a remaining weighted average maturity period of 2.8 years. At December 31, 2013, interest rates on FHLB advances ranged between 2.99% and 6.90%, averaging 4.14%, over a remaining weighted average maturity period of 2.9 years. Long-term FHLB borrowings of $18.0 million and $26.0 million at year-end 2014 and 2013, respectively, were callable quarterly. None of the long-term FHLB advances are convertible to a floating interest rate.

For FHLB advances, the subsidiary banks pledge FHLB stock and fully disbursed, otherwise unencumbered, 1-4 family first mortgage loans as collateral for these advances as required by the FHLB. Based on this collateral and the Company's holdings of FHLB stock, the Company is eligible to borrow up to an additional $108 million from the FHLB at year-end 2014.

During 2005, the Company completed two private offerings of trust preferred securities through two separate Delaware statutory trusts sponsored by the Company. Farmers Capital Bank Trust I ("Trust I") sold $10.0 million of preferred securities and Farmers Capital Bank Trust II ("Trust II") sold $15.0 million of preferred securities. The proceeds from the offerings were used to fund the cash portion of the acquisition of Citizens Bancorp, Inc., the former parent company of Citizens Northern. The trust preferred securities mature September 30, 2035 and are redeemable at any time by the Trust at par.

Farmers Capital Bank Trust III ("Trust III"), a Delaware statutory trust sponsored by the Company, was formed during 2007 for the purpose of financing the cost of acquiring Company shares under a share repurchase program. Trust III sold $22.5 million of trust preferred securities to the public with an initial fixed rate of 6.60% through October 2012, thereafter at a variable rate of interest, reset quarterly, equal to the 3-month LIBOR plus a predetermined spread of

132 basis points. The trust preferred securities mature on November 1, 2037 and are redeemable at any time by the Trust at par. Trust I, Trust II, and Trust III are hereafter collectively referred to as the "Trusts."

The Trusts used the proceeds from the sale of preferred securities, plus capital contributed to establish the trusts, to purchase the Company's subordinated notes in amounts and bearing terms that parallel the amounts and terms of the respective preferred securities. The subordinated notes to Trust I and Trust II mature in 2035 and in 2037 for Trust III, and bear a floating interest rate (current three-month LIBOR plus 150 basis points in the case of the notes held by Trust I, current three-month LIBOR plus 165 basis points in the case of the notes held by Trust II, and current three-month LIBOR plus 132 basis points in the case of the notes held by Trust III). Interest on the notes is payable quarterly. Interest payments to the Trusts and distributions to preferred shareholders by the Trusts may be deferred for 20 consecutive quarterly periods. There have been no deferrals of interest payments during the life of the Trusts.

The subordinated notes are redeemable in whole or in part, without penalty, at the Company's option. The notes are junior in right of payment of all present and future senior indebtedness. At December 31, 2014 and 2013 the balance of the subordinated notes payable to Trust I, Trust II, and Trust III was $10.3 million, $15.5 million, and $23.2 million, respectively. The interest rates in effect as of the last determination date for 2014 were 1.76%, 1.91%, and 1.55% for Trust I, Trust II, and Trust III, respectively. For 2013 these rates were 1.75%, 1.90%, and 1.56% for Trust I Trust II, and Trust III, respectively.

The Company is not considered the primary beneficiary of the Trusts; therefore the Trusts are not consolidated into its financial statements. Accordingly, the Company does not report the securities issued by the Trusts as liabilities, but instead reports as liabilities the subordinated notes issued by the Company and held by the Trusts. The Company, which owns all of the common securities of the Trusts, accounts for its investment in each of the Trusts as other assets. The Company records interest expense on the corresponding notes issued to the Trusts on its statements of income.

The subordinated notes, net of the Company's investment in the Trusts, may be included in Tier 1 capital (with certain limitations applicable) under current regulatory capital guidelines and interpretations. The net amount of subordinated notes in excess of the limit may be included in Tier 2 capital, subject to restrictions. At year-end 2014 and 2013, the Company's Tier 1 capital included $47.5 million, which represents the full amount of the subordinated notes net of the Company's investment in the Trusts.

The Company entered into a balance sheet leverage transaction in 2007 whereby it borrowed $200 million in multiple fixed rate term repurchase agreements with an initial weighted average cost of 3.95% and invested the proceeds in Government National Mortgage Association ("GNMA") bonds, which were pledged as collateral. The Company is required to secure the borrowed funds by GNMA bonds valued at 106% of the outstanding principal balance. The borrowings have an outstanding balance of $100 million at December 31, 2014, are callable on a quarterly basis, and mature in November 2017. The repurchase agreements are held by three of the Company's subsidiary banks and are guaranteed by the Parent Company. The Company has $763 thousand of other long-term repurchase agreements outstanding at December 31, 2014 made in the ordinary course of business with commercial customers. The average interest rate related to these other fixed rate borrowings is 1.17%.

Maturities of long-term borrowings at December 31, 2014 are as follows:

(In thousands)	Amount
2015	$254
2016	509
2017	115,000
2018	3,000
2019	25
Thereafter	49,906
Total	$168,694

10. Income Taxes

The components of income tax expense are as follows:

December 31, (In thousands)	2014	2013	2012
Currently payable	$2,168	$4,908	$3,953
Deferred	3,931	(473)	(1,043)
Total applicable to operations	6,099	4,435	2,910
Deferred tax (credited) charged to components of shareholders' equity:			
Unfunded status of postretirement benefits	(382)	1,589	(92)
Net unrealized securities gains (losses)	4,737	(7,019)	214
Total income taxes	$10,454	$(995)	$3,032

An analysis of the difference between the effective income tax rates and the statutory federal income tax rate follows.

December 31,	2014	2013	2012
Federal statutory rate	35.0%	35.0%	35.0%
Changes from statutory rates resulting from:			
Tax-exempt interest	(5.2)	(6.3)	(7.6)
Nondeductible interest to carry tax-exempt obligations	.2	.3	.4
Nondeductible legal expense	-	-	.5
Tax credits	-	-	(1.8)
Premium income not subject to tax	(1.2)	(1.3)	(2.5)
Company-owned life insurance	(1.9)	(1.8)	(3.5)
Uncertain tax position	(.3)	(.5)	(.9)
Other, net	.4	(.6)	(.3)
Effective tax rate on pretax income	27.0%	24.8%	19.3%

The tax effects of the significant temporary differences that comprise deferred tax assets and liabilities at December 31, 2014 and 2013 are as follows:

December 31, (In thousands)	2014	2013
Assets		
Allowance for loan losses	$4,904	$7,217
Deferred directors' fees	253	285
Postretirement benefit obligations	5,164	4,459
Other real estate owned	2,418	3,568
Partnership investments	372	1,508
Self-funded insurance	214	213
Paid time off	723	701
Depreciation	1,163	798
Intangibles	2,813	3,179
Unrealized losses on available for sale investment securities, net	-	1,951
Other	399	232
Total deferred tax assets	18,423	24,111
Liabilities		
Unrealized gains on available for sale investment securities, net	2,786	-
Prepaid expenses	459	596
Federal Home Loan Bank stock dividends	1,087	1,097
Deferred loan fees	816	772
Lease financing operations	51	136
Total deferred tax liabilities	5,199	2,601
Net deferred tax asset	$13,224	$21,510

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not the Company will realize the benefits of these deductible differences at December 31, 2014.

The Internal Revenue Code grants preferential treatment to the interest income derived from debt issued by states and political subdivisions in that it is not subject to Federal taxation. As a financial institution, the Company is not allowed a tax deduction for a pro rata portion of the interest expense incurred to purchase debt with tax-free attributes. The amount of disallowed interest expense is determined by the total amount of debt issued during the calendar year by the issuer and dependent upon the issuer being considered a qualified small issuer. Debt purchased by a financial institution that meets the requirements to be designated a “qualified tax exempt obligation” has a lower interest expense disallowance than debt that does not meet the “qualified tax exempt obligation” designation. As part of the normal due diligence for a loan with tax-free attributes, the Company relies on the attestation of the borrower, legal counsel for the borrower, and the legal counsel for the Company concerning the representations of the borrower for their debt. During the fourth quarter of 2010, the Company became aware that the qualified status of the debt issued by a customer was being reviewed by the Internal Revenue Service (“IRS”). The customer had previously made representations that their debt was qualified.

During the first quarter of 2011, the Company became aware that this customer had received verbal notification of the IRS's intent to issue an adverse ruling regarding the qualified status of the financing. At that time, the Company had a potential accumulated tax liability of $402 thousand at risk related to the determination for the tax years 2007 through 2010. Under ASC Topic 740, *"Income Taxes,"* the Company is required to recognize a tax position when it is more likely than not that the position would be sustained in a tax examination, with the tax examination being presumed to occur. Additionally, ASC Topic 740 indicates that a subsequent change in facts and circumstances should be recognized in the period in which the change occurs. As such, the Company recorded an accrual of $449 thousand including the $402 thousand accumulated tax liability and interest of $47 thousand in the first quarter of 2011. The amount of this tax liability has been completely reduced since the initial recording of the liability due to the statute of limitations expiring on a portion of the potential tax payment in each of the subsequent three years.

The original loan contract contains provisions that the customer will indemnify the Company for any penalties, taxes or interest thereon for which the Company becomes liable as a result of a determination of taxability. The Company intends to exercise its rights under the contract; however, due to the contingent nature of the indemnification provisions, the Company will not record the effects of the indemnification until it is realized.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

(In thousands)	2014	2013
Balance at beginning of year	$66	$154
Reductions to tax positions of prior years	(66)	(88)
Balance at end of year	$-	$66

At year-end 2014, no unrecognized tax benefits remain that would favorably affect the effective income tax rate in future periods. The Company does not expect any future impact concerning this chain of events.

The Company's policy is to record the accrual of interest or penalties relative to unrecognized tax benefits, if any, in its income tax expense accounts. The total amount of interest recorded in the income tax expense (benefit) line item of the income statement for the year ended December 31, 2011 was $32 thousand. This interest amount was reduced by $12 thousand during 2014, $11 thousand during 2013, and $9 thousand during 2012 due to the statute of limitations expiring on a portion of the potential tax payment. The amount accrued for interest at December 31, 2014 and 2013 was zero and $12 thousand, respectively. No penalties were accrued or recorded during any year in the three years ended December 31, 2014.

The Company files U.S. federal and various state income tax returns. The Company is no longer subject to income tax examinations by taxing authorities for the years before 2011.

11. Retirement Plans

The Company maintains a salary savings plan that covers substantially all of its employees. The Company matches voluntary tax deferred employee contributions at 50% of eligible deferrals up to a maximum of 6% of the participants' compensation. The Company may, at the discretion of its Board, contribute an additional amount based upon a percentage of covered employees' salaries. The Company did not make a discretionary contribution during 2014, 2013, or 2012. Discretionary contributions are allocated among participants in the ratio that each participant's compensation bears to all participants' compensation. Eligible employees are presented with various investment alternatives related to the salary savings plan. Those alternatives include various stock and bond mutual funds ranging from traditional growth funds to more stable income funds as well as an option to invest in bank certificates of deposits. Company shares are not an available investment alternative in the salary savings plan. The total retirement plan expense for 2014, 2013, and 2012 was $483 thousand, $528 thousand, and $485 thousand, respectively.

In connection with its acquisition of Citizens Northern, the Company acquired nonqualified supplemental retirement plans for certain key employees. Benefits provided under these plans are unfunded, and payments to plan participants are made by the Company.

The following schedules set forth a reconciliation of the changes in the supplemental retirement plans' benefit obligation and funded status for the years ended December 31, 2014 and 2013.

(In thousands)	2014	2013
Change in Benefit Obligation		
Obligation at beginning of year	$774	$741
Service cost	12	28
Interest cost	22	29
Actuarial (gain) loss	(189)	3
Benefit payments	(36)	(27)
Obligation at end of year	$583	$774

The following table provides disclosure of the net periodic benefit cost as of December 31 for the years indicated.

(In thousands)	2014	2013
Service cost	$12	$28
Interest cost	22	29
Recognized net actuarial (gain) loss	(4)	12
Net periodic benefit cost	$30	$69
Major assumptions:		
Discount rate used to determine net period benefit cost	4.06%	4.03%
Discount rate used to determine benefit obligation at year end	3.22	4.06

The following table presents estimated future benefit payments in the period indicated.

(In thousands)	Supplemental Retirement Plan
2015	$ 36
2016	36
2017	36
2018	36
2019	36
2020-2024	312

Total	$ 492

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Amounts recognized in accumulated other comprehensive income as of December 31, 2014 and 2013 are as follows:

(In thousands)	2014	2013
Unrecognized net actuarial (gain) loss	$(37)	$148
Total	$(37)	$148

The estimated cost that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year for the supplemental retirement plan is zero.

12. Common Stock Options

During 1997, the Company's Board of Directors approved a nonqualified stock option plan (the "Plan"), subsequently approved by the Company's shareholders, that provides for the granting of stock options to key employees and officers of the Company. The Plan provides for the granting of options to purchase up to 450,000 shares of the Company's common stock at a price equal to the fair value of the Company's common stock on the date the option is granted. The options expire after ten years from the grant date and must be held for a minimum of one year before they can be exercised. Forfeited options are available for the granting of additional stock options under the Plan. Options forfeited from the initial grant in 1997 were used to grant options during 2000 and 2004. Total options granted were 450,000, 54,000, and 40,049 in the years 1997, 2000, and 2004, respectively. All unexercised options granted under the Plan expired during 2014.

A summary of the activity in the Company's Plan for 2014 is presented below.

	2014	
	Shares	Weighted Average Exercise Price
Options outstanding at beginning of year	22,049	$ 34.80
Forfeited	(4,000)	34.80
Expired	(18,049)	34.80
Options outstanding at year-end	-	$ -
Options exercisable at year-end	-	$ -

At December 31, 2014, there were 76,221 options available for future grants under the Plan. There were no options exercised or granted in any year in the three-year periods ending December 31, 2014, nor were there any modifications or cash paid to settle stock option awards during those periods.

13. Postretirement Medical Benefits

The Company provides lifetime medical and dental benefits upon retirement for certain employees meeting the eligibility requirements as of December 31, 1989 (“Plan 1”). Additional participants are not eligible to be included in Plan 1 unless they met the requirements on this date. There were 38 of such participants in Plan 1 at year-end 2014. During 2003, the Company implemented an additional postretirement health insurance program (“Plan 2”). Under Plan 2, any employee meeting the service requirement of 20 years of full time service to the Company and is at least age 55 years of age upon retirement is eligible to continue their health insurance coverage. Under both plans, retirees not yet eligible for Medicare have coverage identical to the coverage offered to active employees. Under both plans, Medicare-eligible retirees are provided with a Medicare Advantage plan. The Company pays 100% of the cost of Plan 1. The Company and the retirees each pay 50% of the cost under Plan 2. Both plans are unfunded.

The following schedules set forth a reconciliation of the changes to the benefit obligation and funded status of the plans for the years ended December 31, 2014 and 2013.

(In thousands)	2014	2013
Change in Benefit Obligation		
Obligation at beginning of year	$12,588	$15,935
Service cost	482	630
Interest cost	569	551
Actuarial loss (gain)	1,422	(4,277)
Participant contributions	115	97
Benefit payments	(384)	(348)
Obligation at end of year	$14,792	$12,588

The following table provides disclosure of the net periodic benefit cost as of December 31 for the years indicated.

(In thousands)	2014	2013
Service cost	$482	$630
Interest cost	569	551
Recognized prior service cost	207	257
Amortization of net actuarial gain	(63)	-
Net periodic benefit cost	$1,195	$1,438
Major assumptions:		
Discount rate used to determine net periodic benefit cost	4.93 %	4.03 %
Discount rate used to determine benefit obligation as of year end	3.92	4.93
Retiree participation rate (Plan 1)	100.00	100.00
Retiree participation rate (Plan 2)	72.00	72.00

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. For measurement purposes, the rate of increase in pre-Medicare medical care claims costs was 6.5%, 6.0%, and 5.5% for 2015, 2016, and 2017, respectively, then grading down by .25% annually to 4.75% for 2020 and thereafter. For dental claims cost, it was 5% for 2015 and thereafter. A 1% change in the assumed health care cost trend rates would have the following incremental effects:

(In thousands)	1% Increase	1% Decrease
Effect on total of service and interest cost components of net periodic postretirement health care benefit cost	$ 299	$ (225)
Effect on accumulated postretirement benefit obligation	3,058	(2,391)

The following table presents estimated future benefit payments in the period indicated.

(In thousands)	Postretirement Medical Benefits
2015	$ 355
2016	373
2017	414
2018	448
2019	466
2020-2024	2,965
Total	$ 5,021

Amounts recognized in accumulated other comprehensive income as of December 31, 2014 and 2013 are as follows:

(In thousands)	2014	2013
Unrecognized net actuarial loss (gain)	$295	$(1,190)
Unrecognized prior service cost	175	383
Total	$470	$(807)

The estimated costs that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are as follows:

(In thousands)	Postretirement Medical Benefits
Unrecognized prior service cost	$ 51
Unrecognized net actuarial loss	42
Total	$ 93

14. Leases

The Company leases certain branch sites and banking equipment under various operating leases. Branch site leases have renewal options of varying lengths and terms. The following table presents estimated future minimum rental commitments under these leases for the period indicated.

(In thousands)	Operating Leases
2015	$ 343
2016	272
2017	136
2018	114
2019	83
Thereafter	427
Total	$ 1,375

Rent expense was $407 thousand, $399 thousand, and $424 thousand for 2014, 2013, and 2012, respectively.

15. Financial Instruments With Off-Balance Sheet Risk

The Company 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. The financial instruments include commitments to extend credit in the form of unused lines of credit and standby letters of credit.

These financial instruments involve to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The contract amounts of these instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require the payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements. Total commitments to extend credit were $161 million and $140 million at December 31, 2014 and 2013, respectively. The Company evaluates each customer’s creditworthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit, if deemed necessary by the Company, is based on management’s credit evaluation of the counter-party. Collateral held varies, but may include accounts receivable, marketable securities, inventory, premises and equipment, residential real estate, and income producing commercial properties.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Since many of the commitments are expected to expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements. The credit risk involved in issuing letters of credit is essentially the same as that received when extending credit to customers. The fair value of these instruments is not considered material for disclosure. The Company had $13.3 million and $23.4 million in irrevocable letters of credit outstanding at December 31, 2014 and 2013, respectively.

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

December 31,	2014		2013	
(In thousands)	Fixed Rate	Variable Rate	Fixed Rate	Variable Rate
Commitments to extend credit, including unused lines of credit	$60,731	$100,612	$56,884	$82,934
Standby letters of credit	2,809	10,535	2,578	20,816
Total	$63,540	$111,147	$59,462	$103,750

16. Concentration of Credit Risk

The Company's bank subsidiaries actively engage in lending, primarily in their home counties around Central and Northern Kentucky and adjacent areas. Collateral is received to support these loans as deemed necessary. The more significant categories of collateral include cash on deposit with the Company's banks, marketable securities, income producing properties, commercial real estate, home mortgages, and consumer durables. Loans outstanding, commitments to make loans, and letters of credit range across a large number of industries and individuals. The obligations are significantly diverse and reflect no material concentration in one or more areas, other than most of the Company's loans are in Kentucky and secured by real estate and thus significantly affected by changes in the Kentucky economy.

17. Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. As of December 31, 2014, there were various pending legal actions and proceedings against the Company arising from the normal course of business and in which claims for damages are asserted. It is the opinion of management, after discussion with legal counsel, that the disposition or ultimate resolution of such claims and legal actions will not have a material effect upon the consolidated financial statements of the Company.

18. Regulatory Matters

The Company and its subsidiary banks are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements will initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the banks must meet specific capital guidelines that involve quantitative measures of the banks' assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Company and its subsidiary banks' capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and its subsidiary banks to maintain minimum amounts and ratios (set forth in the tables below) of Tier 1 and total capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital to average assets (as defined). As of December 31, 2014, the most recent notification from the FDIC categorized the banks as well-capitalized under the regulatory framework for prompt corrective action. To be categorized as well-capitalized, the banks must maintain minimum Tier 1 Risk-based, Total Risk-based, and Tier 1 Leverage ratios as set forth in the tables. There are no conditions or events since that notification that management believes have changed the institutions' category. As noted below under the caption "*Summary of Regulatory Agreements,*" two of the Company's subsidiary banks are required to maintain certain capital ratios that exceed the regulatory established well-capitalized status.

In July 2013, U.S. banking regulators adopted final rules related to standards on bank capital adequacy and liquidity (commonly referred to "Basel III"). The new rules are effective for the Company beginning on January 1, 2015, subject to a phase-in period for certain provisions extending through January 1, 2019. The new rules include a new common equity Tier 1 capital ratio, an increase to the minimum Tier 1 capital ratio, an increase to risk-weightings of certain assets, implementation of a new capital conservation buffer in excess of the required minimum, and changes to how regulatory capital is defined. The Company has completed a pro forma analysis which indicates that it meets the minimum capital ratios and a fully phased-in capital conservation buffer under the new rules.

The regulatory capital amounts and ratios of the consolidated Company and its subsidiary banks are presented in the following tables for the dates indicated.

(Dollars in thousands)	Actual		For Capital Adequacy Purposes		To Be Well-Capitalized Under Prompt Corrective Action Provisions	
December 31, 2014	Amount	Ratio	Amount	Ratio	Amount	Ratio
Tier 1 Risk-based Capital[1]						
Consolidated	$215,090	19.75%	$43,569	4.00%	N/A	N/A
Farmers Bank	65,744	17.71	14,852	4.00	$22,278	6.00%
United Bank[2]	57,691	18.00	12,820	4.00	19,230	6.00
First Citizens	29,703	13.66	8,700	4.00	13,049	6.00
Citizens Northern[2]	24,575	14.46	6,798	4.00	10,197	6.00
Total Risk-based Capital [1]						
Consolidated	$228,710	21.00%	$87,137	8.00%	N/A	N/A
Farmers Bank	69,418	18.70	29,704	8.00	$37,130	10.00%
United Bank[2]	61,728	19.26	25,640	8.00	32,050	10.00
First Citizens	31,094	14.30	17,399	8.00	21,749	10.00
Citizens Northern[2]	26,703	15.71	13,596	8.00	16,995	10.00
Tier 1 Leverage Capital [3]						
Consolidated	$215,090	12.04%	$71,461	4.00%	N/A	N/A
Farmers Bank	65,744	9.40	27,965	4.00	$34,956	5.00%
United Bank[2]	57,691	11.08	20,829	4.00	26,037	5.00
First Citizens	29,703	9.44	12,587	4.00	15,734	5.00
Citizens Northern[2]	24,575	10.11	9,723	4.00	12,153	5.00

(Dollars in thousands)	Actual		For Capital Adequacy Purposes		To Be Well-Capitalized Under Prompt Corrective Action Provisions	
December 31, 2013	Amount	Ratio	Amount	Ratio	Amount	Ratio
Tier 1 Risk-based Capital[1]						
Consolidated	$216,162	18.95 %	$45,623	4.00 %	N/A	N/A
Farmers Bank	67,409	17.56	15,351	4.00	$23,026	6.00 %
United Bank[2]	51,336	15.06	13,634	4.00	20,450	6.00
First Citizens	28,814	12.92	8,917	4.00	13,376	6.00
Citizens Northern[2]	24,455	13.57	7,208	4.00	10,812	6.00
Total Risk-based Capital [1]						
Consolidated	$230,497	20.21 %	$91,245	8.00 %	N/A	N/A
Farmers Bank	72,231	18.82	30,702	8.00	$38,377	10.00 %
United Bank[2]	55,664	16.33	27,267	8.00	34,084	10.00
First Citizens	30,485	13.67	17,835	8.00	22,294	10.00
Citizens Northern[2]	26,708	14.82	14,415	8.00	18,019	10.00
Tier 1 Leverage Capital [3]						
Consolidated	$216,162	11.90 %	$72,677	4.00 %	N/A	N/A
Farmers Bank	67,409	9.60	28,077	4.00	$35,096	5.00 %
United Bank[2]	51,336	9.67	21,233	4.00	26,542	5.00
First Citizens	28,814	9.03	12,768	4.00	15,960	5.00
Citizens Northern[2]	24,455	9.67	10,113	4.00	12,641	5.00

[1]Tier 1 Risk-based and Total Risk-based Capital ratios are computed by dividing a bank's Tier 1 or Total Capital, as defined by regulation, by a risk-weighted sum of the bank's assets, with the risk weighting determined by general standards established by regulation. The safest assets (e.g., government obligations) are assigned a weighting of 0% with riskier assets receiving higher ratings (e.g., ordinary commercial loans are assigned a weighting of 100%).

[2]See discussion below under the caption *"Summary of Regulatory Agreements"* for minimum capital ratios required as part of the bank's regulatory agreement.

[3]Tier 1 Leverage ratio is computed by dividing a bank's Tier 1 Capital by its total quarterly average assets, as defined by regulation.

Payment of dividends by the Company's subsidiary banks is subject to certain regulatory restrictions as set forth in national and state banking laws and regulations. Generally, capital distributions are limited to undistributed net income for the current and prior two years, subject to the capital requirements as summarized above. Furthermore, at December 31, 2014, two of the Company's subsidiary banks are required to obtain regulatory approval before declaring or paying a dividend to the Parent Company as a result of agreements entered into with their primary regulator.

Summary of Regulatory Agreements

Below is a summary of the regulatory agreements that two of the Company's subsidiary banks have entered into with their primary regulators. The agreement entered into during 2009 between the Parent Company and its primary regulator was terminated in March 2014 as a result of satisfactory compliance, most notably from the progress made in lowering nonperforming assets and increasing capital levels.

United Bank

In November of 2009, the FDIC and the Kentucky Department of Financial Institutions ("KDFI") entered into a Cease and Desist Order ("C&D") with United Bank primarily as a result of its level of nonperforming assets. The C&D was terminated in December 2011 coincident with the issuance of a Consent Order ("Consent Order") entered into between the parties. The Consent Order is substantially the same as the C&D, with the primary exception being that United Bank must achieve and maintain a Tier 1 Leverage ratio of 9.0% and a Total Risk-based Capital ratio of 13.0%.

During January 2014, the formal Consent Order entered into during 2011 with United Bank was terminated and replaced with a stepped-down enforcement action in the form of an informal Memorandum of Understanding ("Memorandum"). The informal Memorandum includes many of the same provisions covered by the Consent Order.

Other components in the regulatory order include oversight and reporting obligations to its regulators in terms of complying with the Memorandum. It also includes requirements in the level of reporting by management to its board of directors of its financial results, budgeting, and liquidity analysis, as well as restricting the bank from extending additional credit to borrowers with credits classified as substandard, doubtful or special mention in the report of examination. There is also a requirement to obtain written consent prior to declaring or paying a dividend and to develop a written contingency plan if the bank is unable to meet the capital levels established in the Memorandum.

The Company received written notification in March 2015 that the FDIC and KDFI, as a result of their recent examination, terminated the Memorandum that was entered into with United Bank effective immediately. In connection with the termination of the Memorandum, the Board of Directors of United Bank agreed to adopt a resolution which includes many of the same provisions as the Memorandum, including the requirement to seek approval from the FDIC and KDFI prior to the payment of dividends. However, the requirement for maintaining a minimum Tier 1 Leverage ratio of 9.0% and a Total Risk-based Capital ratio of 13.0% no longer applies.

Citizens Northern

The FDIC and KDFI entered into a Memorandum with Citizens Northern on September 8, 2010. The Memorandum was terminated July 7, 2013 and replaced with an updated Memorandum. The updated Memorandum contains many of the same provisions included in the terminated Memorandum, with a new requirement that Citizens Northern maintain a Tier 1 leverage ratio at or above 9.0%. In addition, the updated Memorandum requires having and retaining qualified management in the areas of loan administration and collection. It also requires Citizens Northern to address credit underwriting and administration weaknesses identified in the most recent examination of the bank by the FDIC and KDFI.

Other parts of the regulatory order include the development and documentation of plans for reducing problem loans, providing progress reports on compliance with the Memorandum, and for the development and implementation of a written profit plan and strategic plans. It also restricts the bank from extending additional credit to borrowers with credits classified as substandard, doubtful or special mention in the report of examination.

Regulators continue to monitor the Company's progress and compliance with the regulatory agreements through periodic on-site examinations, regular communications, and quarterly data analysis. The Company believes it is adequately addressing all issues of the regulatory agreements to which it is subject. However, only the respective regulatory agencies can determine if compliance with the applicable regulatory agreements has been met. The Company believes that each of its subsidiary banks are in compliance with the requirements identified in their regulatory agreements as of December 31, 2014.

The Parent Company maintains cash available to fund a certain amount of additional injections of capital to its bank subsidiaries as determined by management or if required by its regulators. If needed, further amounts in excess of available cash may be funded by future public or private sales of securities, although the Parent Company is currently under no directive by its regulators to raise any additional capital.

19. Fair Value Measurements

ASC Topic 820, *"Fair Value Measurements and Disclosures,"* defines fair value, establishes a framework for measuring fair value, and sets forth disclosures about fair value measurements. ASC Topic 825, *"Financial Instruments,"* allows entities to choose to measure certain financial assets and liabilities at fair value. The Company has not elected the fair value option for any of its financial assets or liabilities.

ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. It also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. This Topic describes three levels of inputs that may be used to measure fair value:

Level 1:	Quoted prices for identical assets or liabilities in active markets that the entity has the ability to access at the measurement date.
Level 2:	Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
Level 3:	Significant unobservable inputs that reflect a reporting entity's own assumptions supported by little or no market activity, about the assumptions that market participants would use in pricing the asset or liability.

Following is a description of the valuation method used for instruments measured at fair value on a recurring basis. For this disclosure, the Company only has available for sale investment securities that meet the requirement.

Available for sale investment securities

Valued primarily by independent third party pricing services under the market valuation approach that include, but are not limited to, the following inputs:

Mutual funds and equity securities are priced utilizing real-time data feeds from active market exchanges for identical securities and are considered Level 1 inputs.

Government-sponsored agency debt securities, obligations of states and political subdivisions, mortgage-backed securities, corporate bonds, and other similar investment securities are priced with available market information through processes using benchmark yields, matrix pricing, prepayment speeds, cash flows, live trading data, and market spreads sourced from new issues, dealer quotes, and trade prices, among others sources and are considered Level 2 inputs.

Available for sale investment securities are the Company's only balance sheet item that meets the disclosure requirements for instruments measured at fair value on a recurring basis. Disclosures as of December 31, 2014 and 2013 are as follows:

(In thousands) Available For Sale Investment Securities	Fair Value	Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2014				
Obligations of U.S. government-sponsored entities	$109,448	$-	$ 109,448	$ -
Obligations of states and political subdivisions	135,766	-	135,766	-
Mortgage-backed securities – residential	370,489	-	370,489	-
Mortgage-backed securities – commercial	2,512	-	2,512	-
Corporate debt securities	6,307	-	6,307	-
Mutual funds and equity securities	1,866	1,866	-	-
Total	$626,388	$1,866	$ 624,522	$ -
December 31, 2013				
Obligations of U.S. government-sponsored entities	$93,750	$-	$ 93,750	$ -
Obligations of states and political subdivisions	131,970	-	131,970	-
Mortgage-backed securities – residential	378,077	-	378,077	-
Mortgage-backed securities – commercial	689	-	689	-
Corporate debt securities	6,257	-	6,257	-
Mutual funds and equity securities	2,077	2,077	-	-
Total	$612,820	$2,077	$ 610,743	$ -

The Company is required to measure and disclose certain other assets and liabilities at fair value on a nonrecurring basis in periods following their initial recognition. The Company's disclosure about assets and liabilities measured at fair value on a nonrecurring basis consists of impaired loans and OREO. The carrying value of these assets are adjusted to fair value on a nonrecurring basis through impairment charges as described more fully below.

Impairment charges on collateral-dependent loans are recorded by either an increase to the provision for loan losses and related allowance or by direct loan charge-offs. The fair value of collateral-dependent impaired loans with specific allocations of the allowance for loan losses is measured based on recent appraisals of the underlying collateral. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Appraisers take absorption rates into consideration and adjustments are routinely made in the appraisal process to identify differences between the comparable sales and income data available. Such adjustments consist mainly of estimated costs to sell that are not included in certain appraisals or to update appraised collateral values as a result of market declines of similar properties for which a newer appraisal is available. These adjustments can be significant and typically result in a Level 3 classification of the inputs for determining fair value.

OREO includes properties acquired by the Company through, or in lieu of, actual loan foreclosures and is carried at fair value less estimated costs to sell. Fair value of OREO at acquisition is generally based on third party appraisals of the property that includes comparable sales data and is considered as Level 3 inputs. The carrying value of each OREO property is updated at least annually and more frequently when market conditions significantly impact the value of the property. If the carrying amount of the OREO exceeds fair value less estimated costs to sell, an impairment loss is recorded through noninterest expense.

The following table represents the carrying amount of assets measured at fair value on a nonrecurring basis and still held by the Company as of the dates indicated. The amounts in the table only represent assets whose carrying amount has been adjusted by impairment charges during the period in a manner as described above; therefore, these amounts will differ from the total amounts outstanding. Collateral-dependent impaired loan amounts in the tables below exclude restructured loans since they are measured based on present value techniques, which are outside the scope of the fair value reporting framework.

		Fair Value Measurements Using		
(In thousands)	Fair Value	Quoted Prices in	Significant Other	Significant Unobservable Inputs
Description		Active Markets for Identical	Observable Inputs (Level 2)	(Level 3)

		Assets (Level 1)		
December 31, 2014				
Collateral-dependent Impaired Loans				
Real estate mortgage - construction and land development	$284	$-	$ -	$ 284
Real estate mortgage - residential	946	-	-	946
Real estate mortgage - farmland and other commercial enterprises	340	-	-	340
Total	$1,570	$-	$ -	$ 1,570
OREO				
Construction and land development	$8,123	$-	$ -	$ 8,123
Residential real estate	863	-	-	863
Farmland and other commercial enterprises	5,459	-	-	5,459
Total	$14,445	$-	$ -	$ 14,445

(In thousands) Description	Fair Value	Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2013				
Collateral-dependent Impaired Loans				
Real estate mortgage - construction and land development	$334	$-	$ -	$ 334
Real estate mortgage - residential	2,085	-	-	2,085
Real estate mortgage - farmland and other commercial enterprises	3,152	-	-	3,152
Commercial and industrial	88	-	-	88
Total	$5,659	$-	$ -	$ 5,659
OREO				
Construction and land development	$14,465	$-	$ -	$ 14,465
Residential real estate	1,116	-	-	1,116
Farmland and other commercial enterprises	9,152	-	-	9,152
Total	$24,733	$-	$ -	$ 24,733

The following table presents impairment charges recorded in earnings on assets measured at fair value on a nonrecurring basis.

(In thousands) Years Ended December 31,	2014	2013
Impairment charges:		
Collateral-dependent impaired loans	$575	$787
OREO	1,595	4,689
Total	$2,170	$5,476

The following table presents quantitative information about unobservable inputs for assets measured on a nonrecurring basis using Level 3 measurements. As previously discussed, the fair value of real estate securing collateral-dependent impaired loans and OREO are based on current third party appraisals. It is often necessary, however, for the Company to discount the appraisal amounts supporting its impaired loans and OREO. These discounts relate primarily to marketing and other holding costs that are not included in certain appraisals or to update values as a result of market declines of similar properties for which newer appraisals are available. Discounts also result from contracts to sell properties entered into during the period. The range of discounts is presented in the table below for 2014. The upper end of the range identified in the table below related to OREO is the result of a single transaction of a relatively small-dollar property.

(In thousands)	Fair Value at December 31, 2014	Valuation Technique	Unobservable Inputs	Range		Weighted Average	
Collateral-dependent impaired loans	$ 1,570	Discounted appraisals	Marketability discount	0% - 6.0	%	1.0	%
OREO	$ 14,445	Discounted appraisals	Marketability discount	1.3% - 19.9	%	6.2	%

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Fair Value of Financial Instruments

The table that follows represents the estimated fair values of the Company's financial instruments made in accordance with the requirements of ASC Topic 825, *"Financial Instruments."* ASC Topic 825 requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet for which it is practicable to estimate that value. The estimated fair value amounts have been determined by the Company using available market information and present value or other valuation techniques. These derived fair values are subjective in nature, involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. ASC Topic 825 excludes certain financial instruments and all nonfinancial instruments from the disclosure requirements. Accordingly, the aggregate fair value amounts presented are not intended to represent the underlying value of the Company.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments not presented elsewhere for which it is practicable to estimate that value.

Cash and Cash Equivalents, Accrued Interest Receivable, and Accrued Interest Payable

The carrying amount is a reasonable estimate of fair value due to the relatively short time between the origination of the instrument and its expected realization or settlement.

Investment Securities Held to Maturity

Fair value is based on quoted market price, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities or with available market information through processes using benchmark yields, matrix pricing, prepayment speeds, cash flows, live trading data, and market spreads sourced from new issues, dealer quotes, and trade prices, among others sources.

Loans

The fair value of loans is estimated by discounting expected future cash flows using current discount rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. Expected future cash flows are projected based on contractual cash flows adjusted for estimated prepayments.

Federal Home Loan Bank and Federal Reserve Bank Stock

It is not practical to determine the fair value of Federal Home Loan Bank and Federal Reserve Bank stock due to restrictions placed on its transferability.

Deposit Liabilities

The fair value of demand deposits, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date and fair value approximates carrying value. The fair value of fixed maturity certificates of deposit is estimated by discounting the expected future cash flows using the rates currently offered for certificates of deposit with similar remaining maturities.

Federal Funds Purchased and Other Short-term Borrowings

The carrying amount is the estimated fair value for these borrowings which reprice frequently in the near term.

Securities Sold Under Agreements to Repurchase, Subordinated Notes Payable, and Other Long-term Borrowings

The fair value of these borrowings is estimated by discounting the expected future cash flows using rates currently available for debt with similar terms and remaining maturities. For subordinated notes payable, the Company uses its best estimate to determine an appropriate discount rate since active markets for similar debt transactions are very limited.

Commitments to Extend Credit and Standby Letters of Credit

Pricing of these financial instruments is based on the credit quality and relationship, fees, interest rates, probability of funding, compensating balance, and other covenants or requirements. Loan commitments generally have fixed expiration dates, variable interest rates and contain termination and other clauses that provide for relief from funding in the event there is a significant deterioration in the credit quality of the customer. Many loan commitments are expected to, and typically do, expire without being drawn upon. The rates and terms of the Company’s commitments to lend and standby letters of credit are competitive with others in the various markets in which the Company operates. There are no unamortized fees relating to these financial instruments, as such the carrying value and fair value are both zero.

The following table presents the estimated fair values of the Company's financial instruments and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2014 and 2013. Information for available for sale investment securities is presented within this footnote in greater detail above.

(In thousands)	Carrying Amount	Fair Value	Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2014					
Assets					
Cash and cash equivalents	$100,914	$100,914	$100,914	$ -	$ -
Held to maturity investment securities	3,728	3,923	-	3,923	-
Loans, net	917,975	918,697	-	-	918,697
Accrued interest receivable	5,625	5,625	-	5,625	-
Federal Home Loan Bank and Federal Reserve Bank Stock	9,368	N/A	-	-	-
Liabilities					
Deposits	1,387,161	1,388,614	991,630	-	396,984
Federal funds purchased and other short-term borrowings	28,590	28,590	-	28,590	-
Securities sold under agreements to repurchase and other long-term borrowings	119,724	129,244	-	129,244	-
Subordinated notes payable to unconsolidated trusts	48,970	22,594	-	-	22,594
Accrued interest payable	944	944	-	944	-
December 31, 2013					
Assets					
Cash and cash equivalents	$68,253	$68,253	$68,253	$ -	$ -
Held to maturity investment securities	765	827	-	827	-
Loans, net	979,306	977,846	-	-	977,846
Accrued interest receivable	5,901	5,901	-	5,901	-
Federal Home Loan Bank and Federal Reserve Bank Stock	9,516	N/A	-	-	-
Liabilities					
Deposits	1,410,215	1,412,572	938,700	-	473,872
	29,123	29,123	-	29,123	-

Federal funds purchased and other short-term borrowings					
Securities sold under agreements to repurchase and other long-term borrowings	127,880	139,375	-	139,375	-
Subordinated notes payable to unconsolidated trusts	48,970	26,070	-	-	26,070
Accrued interest payable	1,137	1,137	-	1,137	-

20. Parent Company Financial Statements

Condensed Balance Sheets

December 31, (In thousands)	2014	2013
Assets		
Cash and cash equivalents	$32,086	$36,471
Investment in subsidiaries	193,390	185,668
Other assets	1,074	851
Total assets	$226,550	$222,990
Liabilities		
Dividends payable	$113	$188
Subordinated notes payable to unconsolidated trusts	48,970	48,970
Other liabilities	4,538	3,777
Total liabilities	53,621	52,935
Shareholders' Equity		
Preferred stock	10,000	29,988
Common stock	936	935
Capital surplus	51,344	51,102
Retained earnings	105,774	91,242
Accumulated other comprehensive income (loss)	4,875	(3,212)
Total shareholders' equity	172,929	170,055
Total liabilities and shareholders' equity	$226,550	$222,990

Condensed Statements of Income and Comprehensive Income

Years Ended December 31, (In thousands)	2014	2013	2012
Income			
Dividends from subsidiaries	$16,525	$14,566	$12,012
Interest	28	29	19
Other noninterest income	3,132	3,740	3,476
Total income	19,685	18,335	15,507
Expense			
Interest expense - subordinated notes payable to unconsolidated trusts	844	864	1,879
Noninterest expense	3,977	3,980	3,875
Total expense	4,821	4,844	5,754
Income before income tax benefit and equity in undistributed income of subsidiaries	14,864	13,491	9,753
Income tax benefit	(555)	(428)	(759)
Income before equity in undistributed income of subsidiaries	15,419	13,919	10,512
Equity in undistributed income (loss) of subsidiaries	1,040	(473)	1,637
Net income	16,459	13,446	12,149

Other comprehensive income (loss)	8,087	(10,081)	226
Comprehensive income	$24,546	$3,365	$12,375

Condensed Statements of Cash Flows

Years Ended December 31, (In thousands)	2014			2013			2012		
Cash Flows From Operating Activities									
Net income	$	16,459		$	13,446		$	12,149	
Adjustments to reconcile net income to net cash provided by operating activities:									
Equity in undistributed (income) loss of subsidiaries		(1,040	)		473			(1,637	)
Noncash employee stock purchase plan expense and director fee compensation		4			4			3	
Noncash director fee compensation		82			-			-	
Change in other assets and liabilities, net		454			(799	)		(590	)
Deferred income tax expense (benefit)		17			(62	)		(64	)
Net cash provided by operating activities		15,976			13,062			9,861	
Cash Flows From Investing Activities									
Return of equity from nonbank subsidiary		1,500			-			500	
Investment in bank subsidiaries		-			-			(2,500	)
Net cash provided by (used in) investing activities		1,500			-			(2,000	)

Cash Flows From Financing Activities								
Redemption of preferred stock		(20,000	)		-			-
Dividends paid, preferred stock		(1,990	)		(1,500	)		(1,500	)
Repurchase of common stock warrant		-			-			(75	)
Shares issued under employee stock purchase plan		129			133			128
Net cash used in financing activities		(21,861	)		(1,367	)		(1,447	)
Net (decrease) increase in cash and cash equivalents		(4,385	)		11,695			6,414
Cash and cash equivalents at beginning of year		36,471			24,776			18,362
Cash and cash equivalents at end of year	$	32,086		$	36,471		$	24,776

21. Quarterly Financial Data (Unaudited)

(In thousands, except per share data)

Quarters Ended 2014	March 31	June 30	Sept. 30	Dec. 31
Interest income	$16,374	$16,331	$15,976	$15,671
Interest expense	2,695	2,604	2,513	2,341
Net interest income	13,679	13,727	13,463	13,330
Provision for loan losses	132	(1,388)	(1,536)	(1,572)
Net interest income after provision for loan losses	13,547	15,115	14,999	14,902
Noninterest income	5,373	5,991	6,142	5,767
Noninterest expense	14,430	14,323	15,751	14,774
Income before income taxes	4,490	6,783	5,390	5,895
Income tax expense	1,120	1,959	1,283	1,737
Net income	3,370	4,824	4,107	4,158
Less preferred stock dividends and discount accretion	537	563	450	377
Net income available to common shareholders	$2,833	$4,261	$3,657	$3,781
Net income per common share, basic and diluted	$.38	$.57	$.49	$.51
Weighted average common shares outstanding, basic and diluted	7,479	7,482	7,485	7,487

(In thousands, except per share data)

Quarters Ended 2013	March 31	June 30	Sept. 30	Dec. 31
Interest income	$16,742	$16,631	$16,563	$16,797
Interest expense	3,166	3,038	2,953	2,838
Net interest income	13,576	13,593	13,610	13,959
Provision for loan losses	(632)	(362)	(586)	(1,020)
Net interest income after provision for loan losses	14,208	13,955	14,196	14,979
Noninterest income	5,411	5,441	5,678	5,586
Noninterest expense	14,509	14,722	15,984	16,358
Income before income taxes	5,110	4,674	3,890	4,207
Income tax expense	1,318	1,127	855	1,135
Net income	3,792	3,547	3,035	3,072
Less preferred stock dividends and discount accretion	485	487	489	490
Net income available to common shareholders	$3,307	$3,060	$2,546	$2,582
Net income per common share, basic and diluted	$.44	$.41	$.34	$.35
Weighted average common shares outstanding, basic and diluted	7,470	7,473	7,475	7,477

22. Intangible Assets

Acquired core deposit and customer relationship intangible assets were as follows as of December 31 for the years indicated.

	2014			2013		
Amortized Intangible Assets (In thousands)	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Core deposit intangibles	$4,524	$ 4,075	$449	$4,524	$ 3,910	$614
Customer relationship intangibles	-	-	-	2,414	2,174	240
Total	$4,524	$ 4,075	$449	$6,938	$ 6,084	$854

Aggregate amortization expense of core deposit and customer relationship intangible assets was $405 thousand, $540 thousand, and $1.0 million for 2014, 2013, and 2012, respectively. Customer relationship intangibles in the amount of $2.4 million recorded in connection with a prior business acquisition during 2004 have been removed from the gross carrying amount and accumulated amortization for 2014 due to being fully amortized. Core deposit intangible assets are scheduled to be fully amortized during 2015 as follows:

(In thousands)	Amount
2015	$ 449

23. Preferred Stock

On January 9, 2009, as part of the U.S. Department of Treasury's ("Treasury") Capital Purchase Program ("CPP"), the Company issued 30,000 shares of Series A, no par value cumulative perpetual preferred stock to the Treasury for $30.0 million. The Company also issued a warrant to the Treasury as part of the CPP. In June 2012, the Treasury conducted an auction in which it sold all of its investment in the Company's Series A preferred stock to private investors. The Company received no proceeds as part of the transaction. In July 2012, the Company repurchased the warrant it issued to the Treasury. Upon settlement of the warrant repurchase, the Treasury has no remaining equity stake in the Company.

The Company accounted for the allocation of the proceeds received from the issuance of the preferred shares, net of transaction costs, on a pro rata basis between the Series A preferred stock and the warrant based on their relative fair values. The Company assigned $2.0 million and $28.0 million to the warrant and the Series A preferred stock, respectively. The resulting discount on the Series A preferred stock was accreted up to the $30.0 million liquidation amount over the initial five year expected life of the Series A preferred stock. The discount accretion was recorded as additional preferred stock dividends, resulting in an effective dividend rate of 6.56%.

The Series A preferred shares have a liquidation preference of $1 thousand per share (plus any accrued and unpaid dividends) and, since the initial five year period of paying dividends at 5% has expired, currently pay a cumulative cash dividend quarterly of 9% per annum. So long as the preferred shares are outstanding, the Company may not declare or pay a dividend or other distribution on its common stock, and generally may not purchase, redeem or otherwise acquire any shares of its common stock, unless all accrued and unpaid dividends on the preferred shares for all past dividend periods are paid in full.

Holders of the preferred shares generally have no voting rights. However, if the Company defers dividend payments on its Series A preferred shares for an aggregate of six quarterly dividend periods, the authorized number of directors of the Company will increase by two and the holders of the Series A preferred shares will have the right to elect directors to fill such director positions at the Company’s next annual meeting of stockholders or special meeting called for that purpose. The Company has made all dividend payments timely on its outstanding preferred shares quarterly and has not made any payment deferrals. The Company may redeem the preferred shares for 100% of the liquidation preference amount at any time, in whole or in part, subject to obtaining prior approval of its banking regulators.

The Company redeemed 20,000 shares of its outstanding preferred stock during 2014 at its stated liquidation value of $1 thousand per share, plus accrued dividends. The shares were approved and redeemed in two separate partial redemptions of 10,000 shares each, as requested, one of which occurred in second quarter and the other in the fourth quarter. There was no additional debt or equity issued in connection with the shares redeemed. There are 10,000 Series A preferred shares outstanding at year-end 2014.

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

None.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, an evaluation was carried out under the supervision and with the participation of our management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on their evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures and internal control over financial reporting are, to the best of their knowledge, effective to ensure that information required to be disclosed by the Company in reports that the Company files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

The Company's Chief Executive Officer and Chief Financial Officer have also concluded that there were no changes in the Company's internal control over financial reporting or in other factors that occurred during the Company's most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting or any corrective actions with regard to significant deficiencies and material weaknesses in internal control over financial reporting.

Management's Report on Internal Control Over Financial Reporting

Management Responsibility. Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. The Company's internal control system is designed to provide reasonable assurance to the Company's management and Board of Directors regarding the reliability of financial reporting and the presentation of published financial statements. However, all internal control systems, no matter how well designed, have inherent limitations.

General Description of Internal Control over Financial Reporting. Internal control over financial reporting refers to a process designed by, or under the supervision of, the Company's Chief Executive Officer and Chief Financial Officer and effected by the Company's Board of Directors, management and other personnel, 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 and includes those policies and procedures that:

Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of Company assets;

Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that the Company's receipts and expenditures are being made only in accordance with the authorization of the Company's management and members of the Company's Board of Directors; and

Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisitions, uses or dispositions of Company assets that could have a material effect on the Company's financial statements.

Inherent Limitations in Internal Control over Financial Reporting. Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented or overridden by collusion or other improper activities. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. However, these inherent limitations are known features of the financial reporting process, and it is possible to design into the process safeguards to reduce, though not eliminate, this risk.

Management's Assessment of the Company's Internal Control over Financial Reporting. Management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2014. In making this assessment, the Company's management used the criteria for effective internal control over financial reporting set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control-Integrated Framework (2013)*.

As a result of our assessment of the Company's internal control over financial reporting, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2014 to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

BKD, LLP, the independent registered public accounting firm that audited the Company's consolidated financial statements included in this Annual Report on Form 10-K, has also audited the effectiveness of the Company's internal control over financial reporting as of December 31, 2014. The audit report on the effectiveness of the Company's internal control over financial reporting is included in this Annual Report on page 77.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

Executive Officer[1]	Age	Positions and Offices With the Registrant	Years of Service With the Registrant
Lloyd C. Hillard, Jr.	68	President and Chief Executive Officer, Director[2]	22[3]

[1]R. Terry Bennett, Chairman of the Company's board of directors, and J. Barry Banker, Vice Chairman, are considered executive officers in name only for purposes of Regulation O.

[2]Also a director of Farmers Bank, United Bank, First Citizens, Citizens Northern, FCB Services, Farmers Insurance (Chairman), FFKT Insurance, EGT Properties, and an administrative trustee of Farmers Capital Bank Trust I, Farmers Capital Bank Trust II, and Farmers Capital Bank Trust III.

[3]Includes years of service with the Parent Company and its subsidiaries.

The Company has adopted a Code of Ethics that applies to the Company's directors, officers, and employees, including the Company's chief executive officer and chief financial officer. The Company makes available its Code of Ethics on its Internet website at www.farmerscapital.com.

Additional information required by Item 10 is hereby incorporated by reference from the Company's definitive proxy statement in connection with its annual meeting of shareholders scheduled for May 12, 2015, which will be filed with the Commission on or about April 1, 2015, pursuant to Regulation 14A.

Item 11. Executive Compensation

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

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

Item 14. Principal Accounting Fees and Services

The information required by Items 11 through 14 is hereby incorporated by reference from the Company's definitive proxy statement in connection with its annual meeting of shareholders scheduled for May 12, 2015, which will be filed with the Commission on or about April 1, 2015, pursuant to Regulation 14A.

PART IV

Item 15. Exhibits, Financial Statement Schedules

(a)1. Financial Statements

The following consolidated financial statements and report of independent registered public accounting firm of the Company is included in Part II, Item 8 on pages 76 through 128:

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets

Consolidated Statements of Income

Consolidated Statements of Comprehensive Income

Consolidated Statements of Changes in Shareholders' Equity

Consolidated Statements of Cash Flows

Notes to Consolidated Financial Statements

(a)2. Financial Statement Schedules

All schedules are omitted for the reason they are not required, or are not applicable, or the required information is disclosed elsewhere in the financial statements and related notes thereto.

(a)3. Exhibits:

3.1	Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation (incorporated by reference to the Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006 (File No. 000-14412)).

3.2	Articles of Amendment to Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation dated January 6, 2009 (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).
3.3	Articles of Amendment to Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation dated November 16, 2009 (incorporated by reference to the Current Report on Form 8-K dated November 17, 2009 (File No. 000-14412)).
3.4	Amended and Restated Bylaws of Farmers Capital Bank Corporation (incorporated by reference to the Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2009 (File No. 000-14412)).
4.1*	Junior Subordinated Indenture, dated as of July 21, 2005, between Farmers Capital Bank Corporation and Wilmington Trust Company, as Trustee, relating to unsecured junior subordinated deferrable interest notes that mature in 2035.
4.2*	Amended and Restated Trust Agreement, dated as of July 21, 2005, among Farmers Capital Bank Corporation, as Depositor, Wilmington Trust Company, as Property and Delaware Trustee, the Administrative Trustees (as named therein), and the Holders (as defined therein).
4.3*	Guarantee Agreement, dated as of July 21, 2005, between Farmers Capital Bank Corporation, as Guarantor, and Wilmington Trust Company, as Guarantee Trustee.
4.4*	Junior Subordinated Indenture, dated as of July 26, 2005, between Farmers Capital Bank Corporation and Wilmington Trust Company, as Trustee, relating to unsecured junior subordinated deferrable interest notes that mature in 2035.
4.5*	Amended and Restated Trust Agreement, dated as of July 26, 2005, among Farmers Capital Bank Corporation, as Depositor, Wilmington Trust Company, as Property and Delaware Trustee, the Administrative Trustees (as named therein), and the Holders (as defined therein).

4.6*	Guarantee Agreement, dated as of July 26, 2005, between Farmers Capital Bank Corporation, as Guarantor, and Wilmington Trust Company, as Guarantee Trustee.
4.7*	Indenture, dated as of August 14, 2007 between Farmers Capital Bank Corporation, as Issuer, and Wilmington Trust Company, as Trustee, relating to fixed/floating rate junior subordinated debt due 2037.
4.8*	Amended and Restated Declaration of Trust, dated as of August 14, 2007, by Farmers Capital Bank Corporation, as Sponsor, Wilmington Trust Company, as Delaware and Institutional Trustee, the Administrative Trustees (as named therein), and the Holders (as defined therein).
4.9*	Guarantee Agreement, dated as of August 14, 2007, between Farmers Capital Bank Corporation, as Guarantor, and Wilmington Trust Company, as Guarantee Trustee.
4.10	Form of Certificate for Fixed Rate Cumulative Perpetual Preferred Stock, Series A (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).
4.11	Letter Agreement, dated January 9, 2009, between Farmers Capital Bank Corporation and the United States Treasury, with respect to the issuance and sale of the Series A preferred stock and the Warrant, and Securities Purchase Agreement-Standard Terms attached thereto as Exhibit A (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).
10.1	Employee Stock Purchase Plan of Farmers Capital Bank Corporation (incorporated by reference to Form S-8 effective June 24, 2004 (File No. 333-116801)).
10.2	Nonqualified Stock Option Plan of Farmers Capital Bank Corporation (incorporated by reference to Form S-8 effective September 8, 1998 (File No. 333-63037)).
10.3	Employment agreement dated December 10, 2012 between Farmers Capital Bank Corporation and Lloyd C. Hillard, Jr. (incorporated by reference to Exhibit 10.1 to Form 8-K/A filed December 26, 2012).
10.4	Amendment No. 1 to Employment agreement dated December 10, 2012 between Farmers Capital Bank Corporation and Lloyd C. Hillard, Jr. (incorporated by reference to Exhibit 10.1 to Form 8-K filed December 30, 2013).
10.5	Amendment No. 2 to Employment agreement dated December 10, 2012 between Farmers Capital Bank Corporation and Lloyd C. Hillard, Jr. (incorporated by reference to Exhibit 10.1 to Form 8-K filed December 8, 2014).
10.6	Employment agreement dated December 17, 2013 between Farmers Capital Bank Corporation and Rickey D. Harp (incorporated by reference to Exhibit 10.1 to Form 8-K filed December 30, 2013).
10.7	Employment agreement dated October 28, 2014 between Farmers Capital Bank Corporation and Mark A. Hampton (incorporated by reference to Exhibit 10.1 to Form 8-K filed October 28, 2014).
21**	Subsidiaries of the Registrant
23.1**	Consent of Independent Registered Public Accounting Firm

31.1**	CEO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2**	CFO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32**	CEO and CFO Certifications Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	Interactive Data Files

* Exhibit not included pursuant to Item 601(b)(4)(iii) and (v) of Regulation S-K. The Company will provide a copy of such exhibit to the Securities and Exchange Commission upon request.

** Filed with this Annual Report on Form 10-K.

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.

FARMERS CAPITAL BANK CORPORATION

By:	*/s/ Lloyd C. Hillard, Jr.* Lloyd C. Hillard, Jr. President and Chief Executive Officer
Date:	March 11, 2015

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/ Lloyd C. Hillard, Jr. Lloyd C. Hillard, Jr.	President, Chief Executive Officer and Director (principal executive officer of the Registrant)	March 11, 2015
/s/ R. Terry Bennett R. Terry Bennett	Chairman	February 25, 2015
/s/ J. Barry Banker J. Barry Banker	Vice Chairman	February 24, 2015
/s/ Michael J. Crawford Michael J. Crawford	Director	February 25, 2015
/s/ John R. Farris John R. Farris	Director	February 25, 2015
/s/ William C. Nash Dr. William C. Nash	Director	February 27, 2015
/s/ David R. O’Bryan David R. O’Bryan	Director	February 26, 2015
/s/ Fred N. Parker Fred N. Parker	Director	February 24, 2015

/s/ David Y. Phelps David Y. Phelps	Director	March 2, 2015
/s/ Marvin E. Strong, Jr. Marvin E. Strong, Jr.	Director	February 27, 2015
/s/ Fred Sutterlin Fred Sutterlin	Director	February 28, 2015
/s/ Judy Worth Judy Worth	Director	February 28, 2015
/s/ Mark A. Hampton Mark A. Hampton	Executive Vice President, Chief Financial Officer, and Secretary (principal financial and accounting officer)	March 11, 2015

INDEX OF EXHIBITS