

LCNB CORP  
Form 10-Q  
May 07, 2012

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2012

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 000-26121

LCNB Corp.  
(Exact name of registrant as specified in its charter)

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

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

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

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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer,

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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 <input type="radio"/>	Accelerated filer <input checked="" type="checkbox"/>
Non-accelerated filer <input type="radio"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="radio"/>

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

The number of shares outstanding of the issuer's common stock, without par value, as of May 7, 2012 was 6,711,928 shares.

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LCNB CORP. AND SUBSIDIARIES  
FOR THE THREE MONTHS ENDED MARCH 31, 2012

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## PART I – FINANCIAL INFORMATION

Item 1. Financial Statements  
 LCNB CORP. AND SUBSIDIARIES  
 CONSOLIDATED BALANCE SHEETS  
 (Dollars in thousands)

	March 31, 2012 (Unaudited)	December 31, 2011
<b>ASSETS:</b>		
Cash and due from banks	\$ 17,429	12,449
Interest-bearing demand deposits	7,849	7,086
Total cash and cash equivalents	25,278	19,535
Investment securities:		
Available-for-sale, at fair value	252,338	254,006
Held-to-maturity, at cost	10,451	10,734
Federal Reserve Bank stock, at cost	949	940
Federal Home Loan Bank stock, at cost	2,091	2,091
Loans, net	454,091	458,331
Premises and equipment, net	17,094	17,346
Goodwill	5,915	5,915
Bank owned life insurance	14,985	14,837
Other assets	8,713	7,835
<b>TOTAL ASSETS</b>	<b>\$ 791,905</b>	<b>791,570</b>
<b>LIABILITIES:</b>		
Deposits:		
Noninterest-bearing	\$ 112,872	106,793
Interest-bearing	562,694	556,769
Total deposits	675,566	663,562
Short-term borrowings	10,590	21,596
Long-term debt	20,731	21,373
Accrued interest and other liabilities	6,505	7,079
<b>TOTAL LIABILITIES</b>	<b>713,392</b>	<b>713,610</b>
<b>SHAREHOLDERS' EQUITY:</b>		
Preferred shares - no par value, authorized 1,000,000 shares, none outstanding	-	-
Common shares - no par value, authorized 12,000,000 shares, issued 7,467,462 and 7,460,494 shares at March 31, 2012 and December 31, 2011, respectively	26,851	26,753
Retained earnings	59,081	57,877
Treasury shares at cost, 755,771 shares at March 31, 2012 and December 31, 2011	(11,698 )	(11,698 )
Accumulated other comprehensive income, net of taxes	4,279	5,028
<b>TOTAL SHAREHOLDERS' EQUITY</b>	<b>78,513</b>	<b>77,960</b>
<b>TOTAL LIABILITES AND SHAREHOLDERS' EQUITY</b>	<b>\$ 791,905</b>	<b>791,570</b>

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



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## LCNB CORP. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands, except per share data)

(Unaudited)

	Three Months Ended March 31,	
	2012	2011
<b>INTEREST INCOME:</b>		
Interest and fees on loans	\$ 6,208	6,518
Interest on investment securities:		
Taxable	887	876
Non-taxable	606	707
Other investments	30	29
<b>TOTAL INTEREST INCOME</b>	<b>7,731</b>	<b>8,130</b>
<b>INTEREST EXPENSE:</b>		
Interest on deposits	1,165	1,584
Interest on short-term borrowings	3	10
Interest on long-term debt	154	178
<b>TOTAL INTEREST EXPENSE</b>	<b>1,322</b>	<b>1,772</b>
<b>NET INTEREST INCOME</b>	<b>6,409</b>	<b>6,358</b>
<b>PROVISION FOR LOAN LOSSES</b>	<b>215</b>	<b>664</b>
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>	<b>6,194</b>	<b>5,694</b>
<b>NON-INTEREST INCOME:</b>		
Trust income	766	483
Service charges and fees on deposit accounts	878	901
Net gain on sales of securities	380	295
Bank owned life insurance income	148	146
Gains from sales of mortgage loans	107	33
Other operating income	57	57
<b>TOTAL NON-INTEREST INCOME</b>	<b>2,336</b>	<b>1,915</b>
<b>NON-INTEREST EXPENSE:</b>		
Salaries and employee benefits	2,982	3,052
Equipment expenses	262	217
Occupancy expense, net	407	455
State franchise tax	206	196
Marketing	111	115
FDIC premiums	111	280
Other non-interest expense	1,369	1,470
<b>TOTAL NON-INTEREST EXPENSE</b>	<b>5,448</b>	<b>5,785</b>
<b>INCOME BEFORE INCOME TAXES</b>	<b>3,082</b>	<b>1,824</b>
<b>PROVISION FOR INCOME TAXES</b>	<b>805</b>	<b>346</b>
<b>NET INCOME FROM CONTINUING OPERATIONS</b>	<b>2,277</b>	<b>1,478</b>
<b>INCOME FROM DISCONTINUED OPERATIONS, NET OF TAX</b>	<b>-</b>	<b>824</b>

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NET INCOME	\$	2,277	2,302
Dividends declared per common share	\$	0.16	0.16
Basic and diluted earnings per common share:			
Continuing operations	\$	0.34	0.22
Discontinued operations		-	0.12
Weighted average common shares outstanding:			
Basic		6,706,295	6,689,743
Diluted		6,773,451	6,741,767

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

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LCNB CORP. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(In thousands)  
(Unaudited)

	Three Months Ended March 31,	
	2012	2011
Net Income	\$ 2,277	2,302
Other comprehensive income:		
Net unrealized gain (loss) on available-for-sale securities (net of taxes of \$259 and \$230 for the three months ended March 31, 2012 and 2011, respectively)	(505)	(447)
Reclassification adjustment for net realized gain on sale of available-for-sale securities included in net income (net of taxes of \$129 and \$100 for the three months ended March 31, 2012 and 2011, respectively)	(251)	(194)
Change in nonqualified pension plan unrecognized net gain (loss) and unrecognized prior service cost (net of taxes of \$5 and \$2 for the three months ended March 31, 2012 and 2011, respectively)	7	5
Nonqualified pension plan curtailment (net of taxes of \$80)	-	155
Total comprehensive income	\$ 1,528	1,821

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

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## LCNB CORP. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Dollars in thousands, except per share amounts)

(Unaudited)

	Common Shares Outstanding	Common Stock	Retained Earnings	Treasury Shares	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance December 31, 2010	6,689,743	\$26,515	54,045	(11,698 )	1,845	70,707
Net income			2,302			2,302
Net unrealized gain (loss) on available-for-sale securities, net of taxes					(447 )	(447 )
Reclassification adjustment for net realized gain on sale of available-for-sale securities included in net income, net of taxes					(194 )	(194 )
Change in nonqualified pension plan unrecognized net gain, net of taxes					8	8
Reclassification adjustment for recognition of nonqualified pension plan net gain, net of taxes					(3 )	(3 )
Nonqualified pension plan curtailment entry, net of taxes					155	155
Compensation expense relating to stock options		10				10
Common stock dividends, \$0.16 per share			(1,070 )			(1,070 )
Balance March 31, 2011	6,689,743	26,525	55,277	(11,698 )	1,364	71,468
Balance December 31, 2011	6,704,723	\$26,753	57,877	(11,698 )	5,028	77,960
Net income			2,277			2,277
Net unrealized gain (loss) on available-for-sale securities, net of tax					(505 )	(505 )
Reclassification adjustment for net realized gain on sale of available-for-sale securities included in net income, net of taxes					(251 )	(251 )
Change in nonqualified pension plan unrecognized net gain, net of taxes					4	4
					3	3

Reclassification adjustment for recognition of nonqualified pension plan net gain, net of taxes						
Dividend Reinvestment and Stock Purchase Plan	6,968	89				89
Compensation expense relating to stock options		9				9
Common stock dividends, \$0.16 per share			(1,073	)		(1,073
Balance March 31, 2012	6,711,691	26,851	59,081	(11,698	)	4,279
						78,513

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

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LCNB CORP. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(In thousands)  
(Unaudited)

	Three Months Ended March 31,	
	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$2,277	2,302
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation, amortization and accretion	775	685
Provision for loan losses	215	664
Curtailment charge for nonqualified defined benefit retirement plan	-	191
Increase in cash surrender value of bank owned life insurance	(148 )	(146 )
Realized gain from sales of securities available-for-sale	(380 )	(295 )
Realized gain from sale of insurance agency	-	(1,503 )
Realized (gain) loss from sales and write-downs of other real estate owned and repossessed assets	81	(16 )
Origination of mortgage loans for sale	(5,866 )	(1,722 )
Realized gains from sales of mortgage loans	(107 )	(33 )
Proceeds from sales of mortgage loans	5,914	1,737
Compensation expense related to stock options	9	10
(Increase) decrease due to changes in assets and liabilities:		
Accrued income receivable	(578 )	(604 )
Other assets	144	(6 )
Other liabilities	(178 )	(261 )
<b>TOTAL ADJUSTMENTS</b>	<b>(119 )</b>	<b>(1,299 )</b>
<b>NET CASH FLOWS FROM OPERATING ACTIVITIES</b>	<b>2,158</b>	<b>1,003</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Proceeds from sales of investment securities available-for-sale	29,944	14,518
Proceeds from maturities and calls of investment securities:		
Available-for-sale	5,514	8,520
Held-to-maturity	413	1,259
Purchases of investment securities:		
Available-for-sale	(34,944 )	(9 )
Held-to-maturity	(131 )	(615 )
Purchase of Federal Reserve Bank stock	(8 )	-
Net (increase) decrease in loans	3,458	(9,102 )
Proceeds from sale of other real estate owned and repossessed assets	14	35
Purchases of premises and equipment	(47 )	(718 )
Proceeds from sale of insurance agency, net of cash disposed	-	1,523
<b>NET CASH FLOWS FROM INVESTING ACTIVITIES</b>	<b>4,213</b>	<b>15,411</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net increase in deposits	12,004	16,552
Net decrease in short-term borrowings	(11,006 )	(10,289 )
Proceeds from long-term debt	-	5,000

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Principal payments on long-term debt	(642 )	(5,718 )
Proceeds from issuance of common stock	15	-
Cash dividends paid on common stock	(999 )	(1,070 )
<b>NET CASH FLOWS FROM FINANCING ACTIVITIES</b>	<b>(628 )</b>	<b>4,475</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>5,743</b>	<b>20,889</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b>	<b>19,535</b>	<b>10,999</b>
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<b>\$25,278</b>	<b>31,888</b>
<b>SUPPLEMENTAL CASH FLOW INFORMATION:</b>		
<b>CASH PAID DURING THE YEAR FOR:</b>		
Interest	\$1,361	1,831
Income taxes	-	620
<b>SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING ACTIVITIES:</b>		
Transfer from loans to other real estate owned and repossessed assets	543	225

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

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LCNB CORP. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

Note 1 - Basis of Presentation

Substantially all of the assets, liabilities and operations of LCNB Corp. ("LCNB") are attributable to its wholly-owned subsidiary, LCNB National Bank (the "Bank"). The accompanying unaudited consolidated financial statements include the accounts of LCNB and the Bank. LCNB completed the sale of its subsidiary, Dakin Insurance Agency, Inc. ("Dakin") on March 23, 2011. The financial results of Dakin are included as income from discontinued operations, net of tax, in the accompanying unaudited consolidated financial statements through the date of sale.

The unaudited interim consolidated financial statements, which have been reviewed by J.D. Cloud & Co. L.L.P., LCNB's independent registered public accounting firm, in accordance with standards established by the Public Company Accounting Oversight Board, as indicated by their report included herein and which does not express an opinion on those statements, have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, the unaudited interim consolidated financial statements include all adjustments (consisting of normal, recurring accruals) considered necessary for a fair presentation of financial position, results of operations, and cash flows for the interim periods, as required by Regulation S-X, Rule 10-01.

Certain prior period data presented in the financial statements have been reclassified to conform with the current year presentation.

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

Results of operations for the three months ended March 31, 2012 are not necessarily indicative of the results to be expected for the full year ending December 31, 2012. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements, accounting policies, and financial notes thereto included in LCNB's 2011 Annual Report on Form 10-K filed with the SEC.

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LCNB CORP. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)  
(Continued)

## Note 2 - Investment Securities

The amortized cost and fair value of available-for-sale investment securities at March 31, 2012 and December 31, 2011 are summarized as follows (in thousands):

	March 31, 2012			Fair Value
	Amortized Cost	Unrealized Gains	Unrealized Losses	
U.S. Treasury notes	\$20,909	-	277	20,632
U.S. Agency notes	75,613	1,329	144	76,798
U.S. Agency mortgage-backed securities	52,346	1,409	80	53,675
Corporate securities	6,307	58	-	6,365
<b>Municipal securities:</b>				
Non-taxable	65,802	3,355	54	69,103
Taxable	21,023	988	4	22,007
Mutual funds	2,111	20	-	2,131
Trust preferred securities	548	36	7	577
Equity securities	977	88	15	1,050
	<b>\$245,636</b>	<b>7,283</b>	<b>581</b>	<b>252,338</b>

	December 31, 2011			Fair Value
	Amortized Cost	Unrealized Gains	Unrealized Losses	
U.S. Treasury notes	\$17,385	165	-	17,550
U.S. Agency notes	81,415	1,517	5	82,927
U.S. Agency mortgage-backed securities	50,923	1,475	111	52,287
Corporate securities	6,334	47	16	6,365
<b>Municipal securities:</b>				
Non-taxable	65,896	3,827	20	69,703
Taxable	21,027	894	14	21,907
Mutual fund	2,103	22	-	2,125
Trust preferred securities	549	37	22	564
Equity securities	526	57	5	578
	<b>\$246,158</b>	<b>8,041</b>	<b>193</b>	<b>254,006</b>

The fair value of held-to-maturity investment securities, consisting of taxable and non-taxable municipal securities, approximates amortized cost at March 31, 2012 and December 31, 2011.

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LCNB CORP. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)  
(Continued)

## Note 2 - Investment Securities (continued)

Substantially all securities in unrealized loss positions at March 31, 2012 have been in a loss position less than twelve months. Management has determined that the unrealized losses at March 31, 2012 are primarily due to fluctuations in market interest rates and do not reflect credit quality deterioration of the securities. Because the Company does not have the intent to sell the investments and it is more likely than not that the Company will not be required to sell the investments before recovery of their amortized cost bases, which may be at maturity, the Company does not consider these investments to be other-than-temporarily impaired.

## Note 3 - Loans

Major classifications of loans at March 31, 2012 and December 31, 2011 are as follows (in thousands):

	March 31, 2012	December 31, 2011
Commercial and industrial	\$ 30,675	30,990
Commercial, secured by real estate	218,638	219,188
Residential real estate	186,765	186,904
Consumer	13,273	14,562
Agricultural	2,357	2,835
Other loans, including deposit overdrafts	5,074	6,554
	456,782	461,033
Deferred net origination costs	199	229
	456,981	461,262
Less allowance for loan losses	2,890	2,931
Loans, net	\$ 454,091	458,331

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LCNB CORP. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)  
(Continued)

## Note 3 – Loans (continued)

Non-accrual, past-due, and accruing restructured loans as of March 31, 2012 and December 31, 2011 are as follows (in thousands):

	March 31, 2012	December 31, 2011
Non-accrual loans:		
Commercial and industrial	\$ 322	495
Commercial, secured by real estate	1,152	1,950
Residential real estate	1,665	1,223
Total non-accrual loans	3,139	3,668
Past-due 90 days or more and still accruing	35	39
Total non-accrual and past-due 90 days or more and still accruing	3,174	3,707
Accruing restructured loans	14,572	14,739
Total	\$ 17,746	18,446
Percentage of total non-accrual and past-due 90 days or more and still accruing to total loans	0.69%	0.80%
Percentage of total non-accrual, past-due 90 days or more and still accruing, and accruing restructured loans to total loans	3.88%	4.00%

Loans sold to and serviced for the Federal Home Loan Mortgage Corporation and other investors are not included in the accompanying consolidated balance sheets. The unpaid principal balances of those loans at March 31, 2012 and December 31, 2011 were \$68,250,000 and \$67,410,000, respectively. Loans sold to the Federal Home Loan Mortgage Corporation during the three months ended March 31, 2012 and 2011 totaled \$5,866,000 and \$1,722,000, respectively.

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## LCNB CORP. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(Continued)

## Note 3 – Loans (continued)

The allowance for loan losses and recorded investment in loans for the three months ended March 31 are as follows (000's):

	Commercial & Industrial	Commercial Real Estate	Residential Real Estate	Consumer	Agricultural	Other	Total
<b>2012</b>							
Allowance for loan losses:							
Balance, beginning of year	\$ 162	1,941	656	166	-	6	2,931
Provision charged to expenses	7	61	155	(6 )	-	(2 )	215
Losses charged off	-	(205 )	(117 )	(46 )	-	(20 )	(388 )
Recoveries	-	70	7	38	-	17	132
Balance, end of period	\$ 169	1,867	701	152	-	1	2,890
<b>Ending balance:</b>							
Individually evaluated for impairment	\$ -	263	150	-	-	-	413
Collectively evaluated for impairment	169	1,604	551	152	-	1	2,477
<b>Loans:</b>							
<b>Ending balance:</b>							
Individually evaluated for impairment	\$ 2,922	13,900	629	9	-	-	17,460
Collectively evaluated for impairment	27,735	204,602	186,378	13,375	2,357	5,074	439,521
Totals	\$ 30,657	218,502	187,007	13,384	2,357	5,074	456,981
<b>2011</b>							
Allowance for loan losses:							
Balance, beginning of year	\$ 305	1,625	459	246	-	6	2,641
Provision charged to expenses	284	200	141	34	-	5	664

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Losses charged off	(251 )	-	(100 )	(91 )	-	(30 )	(472 )
Recoveries	-	30	1	42	-	25	98
Balance, end of period	\$ 338	1,855	501	231	-	6	2,931

Ending balance:

Individually evaluated for impairment	\$ 100	336	-	-	-	-	436
Collectively evaluated for impairment	238	1,519	501	231	-	6	2,495

Loans:

Ending balance:

Individually evaluated for impairment	\$ 833	12,022	533	-	-	-	13,388
Collectively evaluated for impairment	34,533	197,837	187,613	18,420	2,260	9,402	450,065
Totals	35,366	209,859	188,146	18,420	2,260	9,402	463,453

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LCNB CORP. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)  
(Continued)

Note 3 – Loans (continued)

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

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

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LCNB CORP. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)  
(Continued)

## Note 3 – Loans (continued)

An analysis of the Company's loan portfolio by credit quality indicators at March 31, 2012 and December 31, 2011 is as follows (000's):

	Pass	OAEM	Substandard	Doubtful	Total
March 31, 2012					
Commercial & industrial	\$ 25,777	1,676	3,204	-	30,657
Commercial, secured by real estate	207,101	2,115	9,248	38	218,502
Residential real estate	181,376	1,767	3,838	26	187,007
Consumer	13,336	-	48	-	13,384
Agricultural	952	-	1,405	-	2,357
Other	5,074	-	-	-	5,074
Total	\$ 433,616	5,558	17,743	64	456,981
December 31, 2011					
Commercial & industrial	\$ 26,099	1,700	2,804	370	30,973
Commercial, secured by real estate	206,728	2,133	9,633	568	219,062
Residential real estate	182,409	1,681	2,682	376	187,148
Consumer	14,601	-	50	39	14,690
Agricultural	1,430	-	1,405	-	2,835
Other	6,554	-	-	-	6,554
Total	\$ 437,821	5,514	16,574	1,353	461,262

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Note 3 – Loans (continued)

A loan portfolio aging analysis at March 31, 2012 and December 31, 2011 is as follows (000's):

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total Loans Receivable	Total Loans Greater Than 90 Days and Accruing
<b>March 31, 2012</b>							
Commercial & industrial	\$ 1	-	322	323	30,334	30,657	-
Commercial, secured by real estate	-	301	933	1,234	217,268	218,502	-
Residential real estate	813	1,029	1,489	3,331	183,676	187,007	35
Consumer	68	23	-	91	13,293	13,384	-
Agricultural	-	-	-	-	2,357	2,357	-
Other	35	-	-	35	5,039	5,074	-
<b>Total</b>	<b>\$917</b>	<b>1,353</b>	<b>2,744</b>	<b>5,014</b>	<b>451,967</b>	<b>456,981</b>	<b>35</b>
<b>December 31, 2011</b>							
Commercial & industrial	\$ 2	-	495	497	30,476	30,973	-
Commercial, secured by real estate	-	83	1,769	1,852	217,210	219,062	-
Residential real estate	1,132	22	1,202	2,356	184,792	187,148	-
Consumer	82	37	39	158	14,532	14,690	39
Agricultural	-	-	-	-	2,835	2,835	-
Other	59	-	-	59	6,495	6,554	-
<b>Total</b>	<b>\$ 1,275</b>	<b>142</b>	<b>3,505</b>	<b>4,922</b>	<b>456,340</b>	<b>461,262</b>	<b>39</b>

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Note 3 – Loans (continued)

Impaired loans at March 31, 2012 and December 31, 2011 are as follows (000's):

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
<b>March 31, 2012</b>					
With no related allowance recorded:					
Commercial & industrial	\$2,922	3,252	-	2,958	33
Commercial real estate	12,085	12,597	-	12,268	111
Residential real estate	332	332	-	332	-
Consumer	8	8	-	8	-
<b>Total</b>	<b>\$15,347</b>	<b>16,189</b>	<b>-</b>	<b>15,566</b>	<b>144</b>
With an allowance recorded:					
Commercial & industrial	-	-	-	-	-
Commercial real estate	\$1,815	1,835	263	2,311	21
Residential real estate	297	297	150	272	-
Consumer	1	1	-	1	-
<b>Total</b>	<b>\$2,113</b>	<b>2,133</b>	<b>413</b>	<b>2,584</b>	<b>21</b>
<b>Total:</b>					
Commercial & industrial	\$2,922	3,252	-	2,958	33
Commercial real estate	13,900	14,432	263	14,579	132
Residential real estate	629	629	150	604	-
Consumer	9	9	-	9	-
<b>Total</b>	<b>\$17,460</b>	<b>18,322</b>	<b>413</b>	<b>18,150</b>	<b>165</b>
<b>December 31, 2011</b>					
With no related allowance recorded:					
Commercial & industrial	\$2,881	3,211	-	3,015	139
Commercial real estate	12,373	12,587	-	12,686	529
Residential real estate	332	332	-	332	-
Consumer	8	8	-	5	1
<b>Total</b>	<b>\$15,594</b>	<b>16,138</b>	<b>-</b>	<b>16,038</b>	<b>669</b>
With an allowance recorded:					
Commercial & industrial	\$177	177	-	330	14
Commercial real estate	2,120	3,136	257	2,514	67
Residential real estate	264	264	142	257	-
Consumer	2	2	-	1	-
<b>Total</b>	<b>\$2,563</b>	<b>3,579</b>	<b>399</b>	<b>3,102</b>	<b>81</b>
<b>Total:</b>					

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Commercial & industrial	\$3,058	3,388	-	3,345	153
Commercial real estate	14,493	15,723	257	15,200	596
Residential real estate	596	596	142	589	-
Consumer	10	10	-	6	1
Total	\$18,157	19,717	399	19,140	750

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## Note 3 – Loans (continued)

Loan modifications that were classified as troubled debt restructurings during the three months ended March 31, 2012 and 2011 are as follows (dollars in thousands):

	Three Months Ended March 31,			
	2012	Balance at Modification	2011	Balance at Modification
	Number of Loans		Number of Loans	
Commercial and industrial	-	\$ -	1	\$ 204
Commercial, secured by real estate	-	-	2	625
Residential real estate	1	30	-	-
Consumer	-	-	1	2
	1	\$ 30	4	\$ 831

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

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

There were no troubled debt restructurings that subsequently defaulted within twelve months of the restructuring date for the three months ended March 31, 2012 and 2011.

## Note 4 – Other Real Estate Owned

Other real estate owned includes property acquired through foreclosure or deed-in-lieu of foreclosure and also includes property deemed to be in-substance foreclosed and are included in "other assets" in the consolidated balance sheets. Changes in other real estate owned are as follows (000's):

	Three Months Ended March 31,	
	2012	2011
Balance, beginning of year	\$ 1,619	2,088
Additions	543	-
Reductions due to valuation write-downs	(76 )	-
Balance, end of period	\$ 2,086	2,088

Other real estate owned at March 31, 2012 consisted of two commercial properties and one single-family residential home. Other real estate owned at March 31, 2011 consisted of two commercial properties and one single-family residential home. Additions for the 2012 period consisted of one commercial property.



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## Note 5 – Borrowings

Funds borrowed from the Federal Home Loan Bank of Cincinnati at March 31, 2012 and December 31, 2011 are as follows (dollars in thousands):

	Current Interest Rate		March 31, 2012	December 31, 2011
<b>Fixed Rate Advances, due at maturity:</b>				
Advance due August 2012	1.99	%	\$ 6,000	6,000
Advance due January 2015	2.00	%	5,000	5,000
Advance due March 2017	5.25	%	5,000	5,000
<b>Fixed Rate Advances, with monthly principal and interest payments:</b>				
Advance due March 2014	2.45	%	2,074	2,326
Advance due March 2019	2.82	%	2,657	3,047
			\$ 20,731	21,373

All advances from the Federal Home Loan Bank of Cincinnati are secured by a blanket pledge of LCNB's 1-4 family first lien mortgage loans in the amount of approximately \$146 million and \$147 million at March 31, 2012 and December 31, 2011, respectively. Additionally, LCNB is required to hold minimum levels of FHLB stock, based on the outstanding borrowings.

Short-term borrowings at March 31, 2012 and December 31, 2011 are as follows (dollars in thousands):

	March 31, 2012		December 31, 2011	
	Amount	Rate	Amount	Rate
FHLB short-term advance	\$ -	-	12,000	0.04
Repurchase agreements	10,590	0.10	9,596	0.10
	\$ 10,590	0.10	21,596	0.07

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## Note 6 – Income Taxes

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

	For the three months ended			
	March 31,			
	2012		2011	
Statutory tax rate	34.0	%	34.0	%
Increase (decrease) resulting from -				
Tax exempt interest	(6.4	)%	(12.5	)%
Tax exempt income on bank owned life insurance	(1.6	)%	(2.7	)%
Other, net	0.1	%	0.2	%
Effective tax rate	26.1	%	19.0	%

## Note 7 - Commitments and Contingent Liabilities

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

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

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## Note 7 - Commitments and Contingent Liabilities (continued)

LCNB uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. Financial instruments whose contract amounts represent off-balance-sheet credit risk at March 31, 2012 and December 31, 2011 are as follows (in thousands):

	March 31, 2012	December 31, 2011
Commitments to extend credit:		
Commercial loans	\$ 3,953	3,227
Other loans:		
Fixed rate	2,736	1,391
Adjustable rate	721	2,099
Unused lines of credit:		
Fixed rate	4,052	3,883
Adjustable rate	53,069	55,274
Unused overdraft protection amounts on demand and NOW accounts	9,796	9,810
Standby letters of credit	5,575	5,575
	\$ 79,902	81,259

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. Unused lines of credit include amounts not drawn in line of credit loans. Commitments to extend credit and unused lines of credit generally have fixed expiration dates or other termination clauses.

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. At March 31, 2012 and December 31, 2011, outstanding guarantees of approximately \$546,000 were issued to developers and contractors. These guarantees generally are fully secured and have varying maturities. In addition, LCNB has a participation in four letters of credit securing payment of principal and interest on a bond issue. The participation amounts at March 31, 2012 and December 31, 2011 totaled approximately \$5.0 million. The letters of credit have a final maturity date of July 15, 2014, as extended.

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

Management believes that LCNB has sufficient liquidity to fund its lending and capital expenditure commitments.

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LCNB CORP. AND SUBSIDIARIES  
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Note 7 - Commitments and Contingent Liabilities (continued)

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

Note 8 – Regulatory Capital

The Bank and LCNB are required by regulators to meet certain minimum levels of capital adequacy. These are expressed in the form of certain ratios. Capital is separated into Tier 1 capital (essentially shareholders' equity less goodwill and other intangibles) and Tier 2 capital (essentially the allowance for loan losses limited to 1.25% of risk-weighted assets). The first two ratios, which are based on the degree of credit risk in LCNB's assets, provide for weighting assets based on assigned risk factors and include off-balance sheet items such as loan commitments and stand-by letters of credit. The ratio of Tier 1 capital to risk-weighted assets must be at least 4.0% and the ratio of Total capital (Tier 1 capital plus Tier 2 capital) to risk-weighted assets must be at least 8.0%. The capital leverage ratio supplements the risk-based capital guidelines. Banks are required to maintain a minimum ratio of Tier 1 capital to adjusted quarterly average total assets of 3.0%.

For various regulatory purposes, financial institutions are classified into categories based upon capital adequacy. The highest "well-capitalized" category requires capital ratios of at least 10% for total risk-based, 6% for Tier 1 risk-based, and 5% for leverage. As of the most recent notification from their regulators, the Bank and LCNB were categorized as "well-capitalized" under the regulatory framework for prompt corrective action. Management believes that no conditions or events have occurred since the last notification that would change the Bank's or LCNB's category.

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## LCNB CORP. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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## Note 8 – Regulatory Capital (continued)

A summary of the regulatory capital and capital ratios of LCNB follows (dollars in thousands):

	At March 31, 2012	At December 31, 2011
Regulatory Capital:		
Shareholders' equity	\$ 78,513	77,960
Goodwill and other intangibles	(6,057)	(6,071)
Accumulated other comprehensive income	(4,279)	(5,028)
Tier 1 risk-based capital	68,177	66,861
Eligible allowance for loan losses	2,890	2,931
Total risk-based capital	\$ 71,067	69,792
Capital ratios:		
Total risk-based (8% required)	14.93%	14.54%
Tier 1 risk-based (4% required)	14.33%	13.93%
Leverage (3% required)	8.72%	8.51%

## Note 9 – Employee Benefits

LCNB participates in a noncontributory defined benefit retirement multi-employer plan that covers substantially all regular full-time employees hired before January 1, 2009.

Employees of LCNB also participate in a defined contribution retirement plan. Employees hired on or after January 1, 2009 receive a 50% employer match on their contributions into the 401(k) plan, up to a maximum LCNB contribution of 3% of each individual employee's annual compensation. Employees hired before January 1, 2009 who received a benefit reduction under certain amendments to the defined benefit retirement plan receive an automatic contribution of 5% or 7% of annual compensation, depending on the sum of an employee's age and vesting service, into the 401(k) plan, regardless of the contributions made by the employees. This contribution is made annually and these employees do not receive any employer matches to their 401(k) contributions.

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## Note 9 – Employee Benefits (continued)

Funding and administrative costs of the qualified noncontributory defined benefit retirement plan and 401(k) plan charged to pension and other employee benefits in the consolidated statements of income for the three-month periods ended March 31, 2012 and 2011 are as follows (in thousands):

	Three Months Ended March 31,	
	2012	2011
Qualified noncontributory defined benefit retirement plan	\$ 142	124
401(k) plan	36	75

Certain highly compensated employees participate in a nonqualified defined benefit retirement plan. The nonqualified plan ensures that participants receive the full amount of benefits to which they would have been entitled under the noncontributory defined benefit retirement plan in the absence of limits on benefit levels imposed by certain sections of the Internal Revenue Code.

The components of net periodic pension cost of the nonqualified defined benefit retirement plan for the three months ended March 31, 2012 and 2011 are summarized as follows (in thousands):

	Three Months Ended March 31,	
	2012	2011
Service cost	\$ 22	44
Interest cost	11	9
Amortization of unrecognized net (gain)/loss	5	(4 )
Amortization of unrecognized prior service cost	7	11
Net periodic pension cost	\$ 45	60

Amounts recognized in accumulated other comprehensive income, net of deferred federal income taxes, at March 31, 2012 and December 31, 2011 for the nonqualified defined benefit retirement plan consists of (in thousands):

	March 31, 2012	December 31, 2011
Net actuarial loss	\$ 151	156
Past service cost	66	74
	\$ 217	230

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## LCNB CORP. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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## Note 10 - Stock Based Compensation

LCNB established an Ownership Incentive Plan (the "Plan") during 2002 that allows for stock-based awards to eligible employees, as determined by the Board of Directors. The awards may be in the form of stock options, share awards, and/or appreciation rights. The Plan provides for the issuance of up to 200,000 shares.

Options granted to date vest ratably over a five year period and expire ten years after the date of grant. Stock options outstanding at March 31, 2012 are as follows:

Outstanding Stock Options				Exercisable Stock Options		
Exercise Price Range	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Number	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)
9.00 - \$ \$10.99	29,110	\$ 9.00	6.0	18,964	\$ 9.00	5.6
11.00 - \$ \$12.99	74,290	12.03	7.4	29,159	12.01	5.3
13.00 - \$ \$14.99	11,056	13.09	0.8	11,056	13.09	0.8
17.00 - \$ \$18.99	24,158	18.16	2.9	24,158	18.16	2.9
	138,614	12.55	5.8	83,337	13.25	4.1

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

	2012		2011	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding, January 1	124,123	\$ 12.54	99,040	\$ 12.71
Granted	14,491	12.60	25,083	11.85
Exercised	-	-	-	-
Outstanding, March 31	138,614	12.55	124,123	12.54
Exercisable, March 31	83,337	13.25	57,746	14.06

The aggregate intrinsic value (the amount by which the current market value of the underlying stock exceeds the exercise price of the option) for options outstanding at March 31, 2012 that were "in the money" (market price greater than exercise price) was \$216,000. The aggregate intrinsic value at that date for only the options that were exercisable was \$119,000. The aggregate intrinsic value for options outstanding at March 31, 2011 that were in the money was \$83,000 and the aggregate intrinsic value at that date for only the options that were exercisable was \$32,000. The

intrinsic value changes based on changes in the market value of the Company's stock.

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## LCNB CORP. AND SUBSIDIARIES

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## Note 10 - Stock Based Compensation (continued)

The fair value of options granted is estimated at the date of grant using the Black-Scholes option-pricing model. The following table shows the estimated weighted-average fair value of options granted and the assumptions used in calculating that value for the years indicated:

	2012		2011	
Estimated weighted-average fair value of options granted	\$	2.80	\$	2.09
Risk-free interest rate		0.84 %		2.84 %
Average dividend	\$	0.64	\$	0.64
Volatility factor of the expected market price of the Company's common stock		39.56 %		27.37 %
Average life in years		6.5		6.5

Total expense related to options included in salaries and wages in the consolidated statements of income for the three months ended March 31, 2012 and 2011 was \$9,000 and \$10,000, respectively.

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## Note 11 - Earnings Per Common Share

Basic earnings per common share is calculated by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per common share is adjusted for the dilutive effects of stock options, warrant, and restricted stock. The diluted average number of common shares outstanding has been increased for the assumed exercise of stock options, warrant, and restricted stock with proceeds used to purchase treasury shares at the average market price for the period. The computations are as follows for the three months ended March 31, 2012 and 2011 (dollars in thousands, except share and per share data):

	For the Three Months Ended March 31,	
	2012	2011
Net income from continuing operations	\$ 2,277	1,478
Income from discontinued operations, net of taxes	-	824
Net income	\$ 2,277	2,302
Weighted average number of shares outstanding used in the calculation of basic earnings per common share	6,706,295	6,689,743
Add dilutive effect of:		
Stock options	7,103	3,880
Stock warrants	60,053	48,144
	67,156	52,024
Adjusted weighted average number of shares outstanding used in the calculation of diluted earnings per common share	6,773,451	6,741,767
Basic earnings per common share:		
Continuing operations	\$ 0.34	0.22
Discontinued operations	-	0.12
Diluted earnings per common share		
Continuing operations	0.34	0.22
Discontinued operations	-	0.12

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Note 12 - Fair Value of Financial Instruments

LCNB measures certain assets at fair value using various valuation techniques and assumptions, depending on the nature of the asset. Fair value is defined as the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date.

The inputs to valuation techniques used to measure fair value are assigned to one of three broad levels:

- Level 1 – quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the reporting date.
- Level 2 – inputs other than quoted prices included within level 1 that are observable for the asset or liability either directly or indirectly. Level 2 inputs may include quoted prices for similar assets in active markets, quoted prices for identical assets or liabilities in markets that are not active, inputs other than quoted prices (such as interest rates or yield curves) that are observable for the asset or liability, and inputs that are derived from or corroborated by observable market data.
- Level 3 - inputs that are unobservable for the asset or liability.

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

LCNB utilizes a pricing service for determining the fair values of most of its investment securities. Fair value for U.S. Treasury Notes and corporate securities are determined based on market quotations (level 1). Fair value for most of the other investment securities is calculated using the discounted cash flow method for each security. The discount rates for these cash flows are estimated by the pricing service using rates observed in the market (level 2). Cash flow streams are dependent on estimated prepayment speeds and the overall structure of the securities given existing market conditions. In addition, the Company has invested in two mutual funds that invest in debt securities or loans that qualify for credit under the Community Reinvestment Act. The investment in one of the mutual funds is considered to have level 2 inputs because, among other factors, the fund invests primarily in U.S. Government and Agency Obligations, which are considered to be level 2 investments. The investment in the other mutual fund is considered to have level 3 inputs because its shares are not traded in an active market, it does not publish a daily net asset value, and it is primarily a loan fund. Additionally, LCNB owns trust preferred securities in various financial institutions and equity securities in non-financial companies. Market quotations (level 1) are used to determine fair value for these investments.

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Note 12 - Fair Value of Financial Instruments (continued)

Assets that may be recorded at fair value on a nonrecurring basis include impaired loans, other real estate owned, and other repossessed assets. A loan is considered impaired when management believes it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement. Impaired loans are carried at the present value of estimated future cash flows using the loan's existing rate or the fair value of collateral if the loan is collateral dependent, if this value is less than the loan balance. When the fair value of the collateral is based on an observable market price or current appraised value, the inputs are considered to be level 2. When an appraised value is not available and there is not an observable market price, the inputs are considered to be level 3.

Other real estate owned is adjusted to fair value upon transfer of the loan to foreclosed assets, usually based on an appraisal of the property. Subsequently, foreclosed assets are carried at the lower of carrying value or fair value. The inputs for a valuation based on current appraised value are considered to be level 2.

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## Note 12 - Fair Value of Financial Instruments (continued)

The following table summarizes the valuation of LCNB's assets recorded at fair value by input levels as of March 31, 2012 and December 31, 2011 (in thousands):

	Fair Value Measurements	Fair Value Measurements at the End of the Reporting Period Using			Total Gains (Losses)
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
March 31, 2012					
Recurring fair value measurements:					
Investment securities available-for-sale:					
U.S. Treasury notes	\$ 20,632	20,632	-	-	
U.S. Agency notes	76,798	-	76,798	-	
U.S. Agency mortgage-backed securities	53,675	-	53,675	-	
Corporate securities	6,365	6,365	-	-	
Municipal securities:					
Non-taxable	69,103	-	69,103	-	
Taxable	22,007	-	22,007	-	
Mutual funds	2,131	-	1,131	1,000	
Trust preferred securities	577	577	-	-	
Equity securities	1,050	1,050	-	-	
Total recurring fair value measurements	\$ 252,338	28,624	222,714	1,000	
Nonrecurring fair value measurements:					
Impaired loans	\$ 1,700	-	709	991	-
Other real estate owned (a)	2,086	-	1,543	543	(76 )
Repossessed assets (b)	5	-	-	5	(5 )
Total nonrecurring fair value measurements	\$ 3,791	-	2,252	1,539	(81 )
December 31, 2011					
Recurring fair value measurement:					
Investment securities available-for-sale:					
U.S. Treasury notes	\$ 17,550	17,550	-	-	
U.S. Agency notes	82,927	-	82,927	-	
U.S. Agency mortgage-backed securities	52,287	-	52,287	-	
Corporate securities	6,365	4,152	2,213	-	
Municipal securities:					
Non-taxable	69,703	-	69,703	-	

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Taxable	21,907	-	21,907	-
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