

PENNS WOODS BANCORP INC  
Form 10-Q  
May 09, 2012  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-Q**

**x Quarterly Report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934**

**for the Quarterly Period Ended March 31, 2012.**

**o Transition report pursuant to Section 13 or 15 (d) of the Exchange Act**

**for the Transition Period from                      to                      .**

**No. 0-17077**

**(Commission File Number)**

**PENNS WOODS BANCORP, INC.**

**(Exact name of Registrant as specified in its charter)**

**PENNSYLVANIA**

**23-2226454**

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer  
Identification No.)

**300 Market Street, P.O. Box 967 Williamsport, Pennsylvania**  
(Address of principal executive offices)

**17703-0967**  
(Zip Code)

**(570) 322-1111**

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, or a smaller reporting company. See the definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Small reporting company

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

On May 2, 2012 there were 3,837,576 shares of the Registrant's common stock outstanding.

Table of Contents

**PENNS WOODS BANCORP, INC.**

**INDEX TO QUARTERLY REPORT ON FORM 10-Q**

	<b>Page Number</b>
<b><u>Part I</u></b>	
<b><u>Financial Information</u></b>	
<b><u>Item 1.</u></b>	
<b><u>Financial Statements</u></b>	
<u>Consolidated Balance Sheet (Unaudited) as of March 31, 2012 and December 31, 2011</u>	3
<u>Consolidated Statement of Income (Unaudited) for the Three Months Ended March 31, 2012 and 2011</u>	4
<u>Consolidated Statement of Comprehensive Income (Unaudited) for the Three Months Ended March 31, 2012 and 2011</u>	5
<u>Consolidated Statement of Changes in Shareholders' Equity (Unaudited) for the Three Months Ended March 31, 2012 and 2011</u>	5
<u>Consolidated Statement of Cash Flows (Unaudited) for the Three Months Ended March 31, 2012 and 2011</u>	6
<u>Notes to Consolidated Financial Statements (Unaudited)</u>	7
<b><u>Item 2.</u></b>	
<b><u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></b>	23
<b><u>Item 3.</u></b>	
<b><u>Quantitative and Qualitative Disclosures About Market Risk</u></b>	32
<b><u>Item 4.</u></b>	
<b><u>Controls and Procedures</u></b>	32
<b><u>Part II</u></b>	
<b><u>Other Information</u></b>	
<b><u>Item 1.</u></b>	
<b><u>Legal Proceedings</u></b>	33
<b><u>Item 1A.</u></b>	
<b><u>Risk Factors</u></b>	33
<b><u>Item 2.</u></b>	
<b><u>Unregistered Sales of Equity Securities and Use of Proceeds</u></b>	33
<b><u>Item 3.</u></b>	
<b><u>Defaults Upon Senior Securities</u></b>	33
<b><u>Item 4.</u></b>	
<b><u>Mine Safety Disclosures</u></b>	33
<b><u>Item 5.</u></b>	
<b><u>Other Information</u></b>	33
<b><u>Item 6.</u></b>	
<b><u>Exhibits</u></b>	33
<b><u>Signatures</u></b>	34
<b><u>Exhibit Index and Exhibits</u></b>	35



Table of Contents**Part I. FINANCIAL INFORMATION****Item 1. Financial Statements**

**PENNS WOODS BANCORP, INC.**  
**CONSOLIDATED BALANCE SHEET**  
**(UNAUDITED)**

(In Thousands, Except Share Data)	March 31, 2012	December 31, 2011
<b>ASSETS:</b>		
Noninterest-bearing balances	\$ 16,272	\$ 13,829
Interest-bearing deposits in other financial institutions	7,159	56
Total cash and cash equivalents	23,431	13,885
Investment securities, available for sale, at fair value	284,778	270,097
Investment securities, held to maturity, (fair value of \$55)	55	54
Loans held for sale	2,065	3,787
Loans	443,577	435,959
Less: Allowance for loan losses	7,745	7,154
Loans, net	435,832	428,805
Premises and equipment, net	8,283	7,707
Accrued interest receivable	4,100	3,905
Bank-owned life insurance	15,973	16,065
Investment in limited partnerships	3,379	3,544
Goodwill	3,032	3,032
Deferred tax asset	6,416	7,991
Other assets	5,770	5,081
<b>TOTAL ASSETS</b>	<b>\$ 793,114</b>	<b>\$ 763,953</b>
<b>LIABILITIES:</b>		
Interest-bearing deposits	\$ 505,271	\$ 470,310
Noninterest-bearing deposits	116,271	111,354
Total deposits	621,542	581,664
Short-term borrowings	14,768	29,598
Long-term borrowings, Federal Home Loan Bank (FHLB)	61,278	61,278
Accrued interest payable	506	536
Other liabilities	9,741	10,417
<b>TOTAL LIABILITIES</b>	<b>707,835</b>	<b>683,493</b>
<b>SHAREHOLDERS EQUITY:</b>		
Common stock, par value \$8.33, 10,000,000 shares authorized; 4,018,068 and 4,017,677 shares issued	33,484	33,480
Additional paid-in capital	18,127	18,115
Retained earnings	38,279	36,394
Accumulated other comprehensive gain (loss):		

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Net unrealized gain on available for sale securities	5,832	2,914
Defined benefit plan	(4,133)	(4,133)
Less: Treasury stock at cost, 180,596 shares	(6,310)	(6,310)
<b>TOTAL SHAREHOLDERS EQUITY</b>	<b>85,279</b>	<b>80,460</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS EQUITY</b>	<b>\$ 793,114</b>	<b>\$ 763,953</b>

See accompanying notes to the unaudited consolidated financial statements.

Table of Contents

**PENNS WOODS BANCORP, INC.**  
**CONSOLIDATED STATEMENT OF INCOME**  
**(UNAUDITED)**

(In Thousands, Except Per Share Data)	2012	Three Months Ended March 31,	2011
<b>INTEREST AND DIVIDEND INCOME:</b>			
Loans, including fees	\$	6,314	\$ 6,288
Investment securities:			
Taxable		1,474	1,375
Tax-exempt		1,405	1,267
Dividend and other interest income		92	52
<b>TOTAL INTEREST AND DIVIDEND INCOME</b>		<b>9,285</b>	<b>8,982</b>
<b>INTEREST EXPENSE:</b>			
Deposits		961	1,194
Short-term borrowings		34	57
Long-term borrowings, FHLB		620	734
<b>TOTAL INTEREST EXPENSE</b>		<b>1,615</b>	<b>1,985</b>
<b>NET INTEREST INCOME</b>		<b>7,670</b>	<b>6,997</b>
<b>PROVISION FOR LOAN LOSSES</b>		<b>600</b>	<b>600</b>
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>		<b>7,070</b>	<b>6,397</b>
<b>NON-INTEREST INCOME:</b>			
Service charges		447	503
Securities gains, net		589	125
Bank-owned life insurance		268	174
Gain on sale of loans		183	249
Insurance commissions		442	209
Brokerage commissions		212	274
Other		622	411
<b>TOTAL NON-INTEREST INCOME</b>		<b>2,763</b>	<b>1,945</b>
<b>NON-INTEREST EXPENSE:</b>			
Salaries and employee benefits		3,017	2,632
Occupancy, net		328	348
Furniture and equipment		346	308
Pennsylvania shares tax		169	172
Amortization of investment in limited partnerships		165	166
FDIC deposit insurance		123	187
Other		1,316	1,175
<b>TOTAL NON-INTEREST EXPENSE</b>		<b>5,464</b>	<b>4,988</b>
<b>INCOME BEFORE INCOME TAX PROVISION</b>		<b>4,369</b>	<b>3,354</b>
<b>INCOME TAX PROVISION</b>		<b>680</b>	<b>501</b>
<b>NET INCOME</b>	\$	<b>3,689</b>	\$ <b>2,853</b>

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

<b>EARNINGS PER SHARE - BASIC</b>	\$	0.96	\$	0.74
<b>EARNINGS PER SHARE - DILUTED</b>	\$	0.96	\$	0.74
<b>WEIGHTED AVERAGE SHARES OUTSTANDING - BASIC</b>		3,837,204		3,835,295
<b>WEIGHTED AVERAGE SHARES OUTSTANDING - DILUTED</b>		3,837,204		3,835,295
<b>DIVIDENDS PER SHARE</b>	\$	0.47	\$	0.46

See accompanying notes to the unaudited consolidated financial statements.



Table of Contents

## PENNS WOODS BANCORP, INC.

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(UNAUDITED)

(In Thousands)	Three Months Ended March 31,	
	2012	2011
Net Income	\$ 3,689	\$ 2,853
Other comprehensive income:		
Change in unrealized gain on available for sale securities	5,010	2,051
Tax Effect	(1,703)	(697)
Net realized gain included in net income	589	125
Tax Effect	(200)	(42)
Total other comprehensive income	2,918	1,271
Comprehensive income	\$ 6,607	\$ 4,124

See accompanying notes to the unaudited consolidated financial statements.

## PENNS WOODS BANCORP, INC.

## CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS EQUITY

(UNAUDITED)

(In Thousands, Except Per Share Data)	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)		TREASURY STOCK	TOTAL SHAREHOLDERS EQUITY
	SHARES	AMOUNT			INCOME	(LOSS)		
Balance, December 31, 2010	4,015,753	\$ 33,464	\$ 18,064	\$ 31,091	\$ (9,689)	\$ (6,310)	\$ 66,620	
Comprehensive income:								
Net income				2,853			2,853	
Other comprehensive income					1,271		1,271	
Dividends declared, (\$0.46 per share)				(1,764)			(1,764)	
Common shares issued for employee stock purchase plan	480	4	14				18	
Balance, March 31, 2011	4,016,233	\$ 33,468	\$ 18,078	\$ 32,180	\$ (8,418)	\$ (6,310)	\$ 68,998	
(In Thousands, Except Per Share Data)	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)		TREASURY STOCK	TOTAL SHAREHOLDERS EQUITY
	SHARES	AMOUNT			INCOME	(LOSS)		
Balance, December 31, 2011	4,017,677	\$ 33,480	\$ 18,115	\$ 36,394	\$ (1,219)	\$ (6,310)	\$ 80,460	
Comprehensive income:								
Net income				3,689			3,689	

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Other comprehensive income						2,918		2,918
Dividends declared, (\$0.47 per share)						(1,804)		(1,804)
Common shares issued for employee stock purchase plan	391		4		12			16
Balance, March 31, 2012	4,018,068	\$	33,484	\$	18,127	\$	38,279	\$
						1,699	\$	(6,310)
								85,279

See accompanying notes to the unaudited consolidated financial statements.

Table of Contents

**PENNS WOODS BANCORP, INC.**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**  
**(UNAUDITED)**

(In Thousands)	Three Months Ended March 31,	
	2012	2011
<b>OPERATING ACTIVITIES:</b>		
Net Income	\$ 3,689	\$ 2,853
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	191	175
Provision for loan losses	600	600
Accretion and amortization of investment security discounts and premiums	(377)	(459)
Securities gains, net	(589)	(125)
Originations of loans held for sale	(4,301)	(8,686)
Proceeds of loans held for sale	6,206	10,775
Gain on sale of loans	(183)	(249)
Earnings on bank-owned life insurance	(268)	(174)
Decrease in prepaid federal deposit insurance	112	165
Other, net	(1,590)	(693)
Net cash provided by operating activities	3,490	4,182
<b>INVESTING ACTIVITIES:</b>		
Investment securities available for sale:		
Proceeds from sales	9,765	2,728
Proceeds from calls and maturities	3,400	2,001
Purchases	(22,741)	(7,876)
Investment securities held to maturity:		
Proceeds from sales		5
Proceeds from calls and maturities		25
Net (increase) decrease in loans	(7,627)	2,892
Acquisition of bank premises and equipment	(767)	(151)
Proceeds from the sale of foreclosed assets	131	92
Purchase of bank-owned life insurance	(29)	(32)
Proceeds from bank-owned life insurance death benefit	383	
Proceeds from redemption of regulatory stock	281	345
Net cash (used for) provided by investing activities	(17,204)	29
<b>FINANCING ACTIVITIES:</b>		
Net increase in interest-bearing deposits	34,961	5,278
Net increase in noninterest-bearing deposits	4,917	5,931
Net decrease in short-term borrowings	(14,830)	(11,663)
Dividends paid	(1,804)	(1,764)
Issuance of common stock	16	18
Net cash provided by (used for) financing activities	23,260	(2,200)
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>9,546</b>	<b>2,011</b>
<b>CASH AND CASH EQUIVALENTS, BEGINNING</b>	<b>13,885</b>	<b>9,493</b>
<b>CASH AND CASH EQUIVALENTS, ENDING</b>	<b>\$ 23,431</b>	<b>\$ 11,504</b>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>		
Interest paid	\$ 1,645	\$ 2,041
Income taxes paid	925	750

Transfer of loans to foreclosed real estate

577

See accompanying notes to the unaudited consolidated financial statements.

Table of Contents

**PENNS WOODS BANCORP, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**Note 1 Basis of Presentation**

The consolidated financial statements include the accounts of Penns Woods Bancorp, Inc. (the Company) and its wholly-owned subsidiaries: Woods Investment Company, Inc., Woods Real Estate Development Company, Inc., and Jersey Shore State Bank (the Bank) and its wholly-owned subsidiary, The M Group, Inc. D/B/A The Comprehensive Financial Group (The M Group). All significant inter-company balances and transactions have been eliminated in the consolidation.

The interim financial statements are unaudited but, in the opinion of management, reflect all adjustments necessary for the fair presentation of results for such periods. The results of operations for any interim period are not necessarily indicative of results for the full year. These financial statements should be read in conjunction with the financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

The accounting policies followed in the presentation of interim financial results are the same as those followed on an annual basis. These policies are presented on pages 37 through 43 of the Annual Report on Form 10-K for the year ended December 31, 2011.

In reference to the attached financial statements, all adjustments are of a normal recurring nature pursuant to Rule 10-01(b) (8) of Regulation S-X.

**Note 2 Recent Accounting Pronouncements**

In April 2011, the Financial Accounting Standards Board (FASB) issued ASU 2011-03, *Transfers and Services (Topic 860): Reconsideration of Effective Control for Repurchase Agreements*. The main objective in developing this update is to improve the accounting for repurchase agreements (repos) and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. The amendments in this update remove from the assessment of effective control (1) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and (2) the collateral maintenance implementation guidance related to that criterion. The amendments in this update apply to all entities, both public and nonpublic. The amendments affect all entities that enter into agreements to transfer financial assets that both entitle and obligate the transferor to repurchase or redeem the financial assets before their maturity. The guidance in this update is effective for the first interim or annual period beginning on or after December 15, 2011 and should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted. This ASU did not have a significant impact on the Company's financial statements.

## Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

In May 2011, the FASB issued ASU 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. The amendments in this update result in common fair value measurement and disclosure requirements in U.S. GAAP and IFRSs. Consequently, the amendments change the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. The amendments in this update are to be applied prospectively. For public entities, the amendments are effective during interim and annual periods beginning after December 15, 2011. Early application by public entities is not permitted. The Company has provided the necessary disclosures in Note 10 Fair Value Measurements.

In June 2011, the FASB issued ASU 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income*. The amendments in this update improve the comparability, clarity, consistency, and transparency of financial reporting and increase the prominence of items reported in other comprehensive income. To increase the prominence of items reported in other comprehensive income and to facilitate convergence of U.S. GAAP and IFRS, the option to present components of other comprehensive income as part of the statement of changes in stockholders' equity was eliminated. The amendments require that all non-owner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In the two-statement approach, the first statement should present total net income and its components followed consecutively by a second statement that should present total other comprehensive income, the components of other comprehensive income, and the total of comprehensive income. All entities that report items of comprehensive income, in any period presented, will be affected by the changes in this update. For public entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The amendments in this update should be applied retrospectively, and early adoption is permitted. The Company has provided the necessary disclosure in the Consolidated Statement of Comprehensive Income.

In September 2011, the FASB issued ASU 2011-08, *Intangibles - Goodwill and Other Topics (Topic 350), Testing Goodwill for Impairment*. The objective of this update is to simplify how entities test goodwill for impairment. The amendments in the update permit an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350. The more-likely-than-not threshold is defined as having a likelihood of more than 50 percent. Under the amendments in this update, an entity is not required to calculate the fair value of a reporting unit unless the entity determines that it is more likely than not that its fair value is less than its carrying amount. The amendments in this update apply to all entities, both public

Table of Contents

and nonpublic, that have goodwill reported in their financial statements and are effective for interim and annual goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued or have not yet been made available for issuance. This ASU did not have a significant impact on the Company's financial statements.

In December 2011, the FASB issued ASU 2011-10, *Property, Plant, and Equipment (Topic 360): Derecognition of in Substance Real Estate - a Scope Clarification*. The amendments in this update affect entities that cease to have a controlling financial interest in a subsidiary that is in substance real estate as a result of default on the subsidiary's nonrecourse debt. Under the amendments in this update, when a parent (reporting entity) ceases to have a controlling financial interest in a subsidiary that is in substance real estate as a result of default on the subsidiary's nonrecourse debt, the reporting entity should apply the guidance in Subtopic 360-20 to determine whether it should derecognize the in substance real estate. Generally, a reporting entity would not satisfy the requirements to derecognize the in substance real estate before the legal transfer of the real estate to the lender and the extinguishment of the related nonrecourse indebtedness. That is, even if the reporting entity ceases to have a controlling financial interest under Subtopic 810-10, the reporting entity would continue to include the real estate, debt, and the results of the subsidiary's operations in its consolidated financial statements until legal title to the real estate is transferred to legally satisfy the debt. The amendments in this update should be applied on a prospective basis to deconsolidation events occurring after the effective date. Prior periods should not be adjusted even if the reporting entity has continuing involvement with previously derecognized in substance real estate entities. For public entities, the amendments in this update are effective for fiscal years, and interim periods within those years, beginning on or after June 15, 2012. Early adoption is permitted. This ASU is not expected to have a significant impact on the Company's financial statements.

In December 2011, the FASB issued ASU 2011-11, *Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities*. The amendments in this update affect all entities that have financial instruments and derivative instruments that are either (1) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement. The requirements amend the disclosure requirements on offsetting in Section 210-20-50. This information will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments in the scope of this update. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. The Company is currently evaluating the impact the adoption of this ASU will have on the Company's financial statements.

In December 2011, the FASB issued ASU 2011-12, *Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05*. In order to defer only those changes in update 2011-05 that relate to the presentation of reclassification adjustments, the paragraphs in this update supersede certain pending paragraphs in update 2011-05. Entities should continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before update 2011-05. All other requirements in update 2011-05 are not affected by this update, including the requirement to report comprehensive income either in a single continuous financial statement or in two separate but consecutive financial statements. Public entities should apply these requirements for fiscal years, and interim periods within those years, beginning after December 15, 2011. This ASU did not have a significant impact on the Company's financial statements.

**Note 3 Per Share Data**

There are no convertible securities which would affect the denominator in calculating basic and dilutive earnings per share. Net income as presented on the consolidated statement of income will be used as the numerator. The following table sets forth the composition of the weighted average common shares (denominator) used in the basic and dilutive earnings per share computation.

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2011</b>
Weighted average common shares issued	4,017,800	4,015,891
Average treasury stock shares	(180,596)	(180,596)
Weighted average common shares and common stock equivalents used to calculate basic earnings per share	3,837,204	3,835,295
Additional common stock equivalents (stock options) used to calculate diluted earnings per share		
Weighted average common shares and common stock equivalents used to calculate diluted earnings per share	3,837,204	3,835,295



Table of Contents

There were no options outstanding during the three months ended March 31, 2011 and 2012.

**Note 4 Investment Securities**

The amortized cost and fair values of investment securities at March 31, 2012 and December 31, 2011 are as follows:

(In Thousands)	March 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<b>Available for sale (AFS)</b>				
U.S. Government and agency securities	\$ 21,801	\$ 1,698	\$	\$ 23,499
State and political securities	175,921	9,570	(3,320)	182,171
Other debt securities	66,170	284	(788)	65,666
Total debt securities	263,892	11,552	(4,108)	271,336
Financial institution equity securities	8,866	1,313	(22)	10,157
Other equity securities	3,184	145	(44)	3,285
Total equity securities	12,050	1,458	(66)	13,442
Total investment securities AFS	\$ 275,942	\$ 13,010	\$ (4,174)	\$ 284,778
<b>Held to maturity (HTM)</b>				
Other debt securities	\$ 55	\$	\$	\$ 55
Total investment securities HTM	\$ 55	\$	\$	\$ 55

(In Thousands)	December 31, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<b>Available for sale (AFS)</b>				
U.S. Government and agency securities	\$ 26,755	\$ 1,916	\$	\$ 28,671
State and political securities	174,790	8,398	(4,887)	178,301
Other debt securities	51,447	133	(2,066)	49,514
Total debt securities	252,992	10,447	(6,953)	256,486
Financial institution equity securities	9,939	1,095	(232)	10,802
Other equity securities	2,751	133	(75)	2,809
Total equity securities	12,690	1,228	(307)	13,611
Total investment securities AFS	\$ 265,682	\$ 11,675	\$ (7,260)	\$ 270,097
<b>Held to maturity (HTM)</b>				
Other debt securities	\$ 54	\$ 1	\$	\$ 55
Total investment securities HTM	\$ 54	\$ 1	\$	\$ 55

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

The following tables show the Company's gross unrealized losses and fair value, aggregated by investment category and length of time, that the individual securities have been in a continuous unrealized loss position, at March 31, 2012 and December 31, 2011.

Table of Contents

(In Thousands)	Less than Twelve Months		March 31, 2012 Twelve Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
State and political securities	\$ 9,513	\$ (382)	\$ 17,392	\$ (2,938)	\$ 26,905	\$ (3,320)
Other debt securities	41,084	(786)	98	(2)	41,182	(788)
Total debt securities	50,597	(1,168)	17,490	(2,940)	68,087	(4,108)
Financial institution equity securities	193	(7)	142	(15)	335	(22)
Other equity securities	462	(7)	125	(37)	587	(44)
Total equity securities	655	(14)	267	(52)	922	(66)
Total	\$ 51,252	\$ (1,182)	\$ 17,757	\$ (2,992)	\$ 69,009	\$ (4,174)

(In Thousands)	Less than Twelve Months		December 31, 2011 Twelve Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
State and political securities	\$ 1,142	\$ (6)	\$ 28,260	\$ (4,881)	\$ 29,402	\$ (4,887)
Other debt securities	35,858	(2,048)	82	(18)	35,940	(2,066)
Total debt securities	37,000	(2,054)	28,342	(4,899)	65,342	(6,953)
Financial institution equity securities	1,140	(116)	273	(116)	1,413	(232)
Other equity securities	263	(65)	130	(10)	393	(75)
Total equity securities	1,403	(181)	403	(126)	1,806	(307)
Total	\$ 38,403	\$ (2,235)	\$ 28,745	\$ (5,025)	\$ 67,148	\$ (7,260)

At March 31, 2012 there were a total of 54 and 51 individual securities that were in a continuous unrealized loss position for less than twelve months and twelve months or greater, respectively.

The Company reviews its position quarterly and has determined that, at March 31, 2012, the declines outlined in the above table represent temporary declines and the Company does not intend to sell and does not believe it will be required to sell these securities before recovery of their cost basis, which may be at maturity. There were 105 positions that were temporarily impaired at March 31, 2012. The Company has concluded that the unrealized losses disclosed above are not other than temporary but are the result of interest rate changes, sector credit ratings changes, or company-specific ratings changes that are not expected to result in the non-collection of principal and interest during the period.

The amortized cost and fair value of debt securities at March 31, 2012, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities since borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(In Thousands)	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$ 10,315	\$ 10,332	\$ 55	\$ 55
Due after one year to five years	41,905	41,709		

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Due after five years to ten years	21,569	21,560				
Due after ten years	190,103	197,735				
Total	\$ 263,892	\$ 271,336	\$ 55	\$ 55		

Total gross proceeds from sales of securities available for sale were \$9,765,000 and \$2,728,000, for the three months ended March 31, 2012 and 2011, respectively. The following table represents gross realized gains and losses on those transactions:

Table of Contents

(In Thousands)	Three Months Ended March 31,	
	2012	2011
<b>Gross realized gains:</b>		
U.S. Government and agency securities	\$ 138	\$ 4
State and political securities	6	5
Other debt securities	55	6
Financial institutions equity securities	355	
Other equity securities	126	121
<b>Total gross realized gains</b>	<b>\$ 680</b>	<b>\$ 136</b>
<b>Gross realized losses:</b>		
U.S. Government and agency securities	\$	\$
State and political securities		
Other debt securities		11
Financial institutions equity securities	66	
Other equity securities	25	
<b>Total gross realized losses</b>	<b>\$ 91</b>	<b>\$ 11</b>

There were no impairment charges included in gross realized losses for the three months ended March 31, 2012 and 2011, respectively.

**Note 5 Federal Home Loan Bank Stock**

The Bank is a member of the Federal Home Loan Bank ( FHLB ) of Pittsburgh and as such, is required to maintain a minimum investment in stock of the FHLB that varies with the level of advances outstanding with the FHLB. The stock is bought from and sold to the FHLB based upon its \$100 par value. The stock does not have a readily determinable fair value and as such is classified as restricted stock, carried at cost and evaluated for impairment as necessary. The stock's value is determined by the ultimate recoverability of the par value rather than by recognizing temporary declines. The determination of whether the par value will ultimately be recovered is influenced by criteria such as the following: (a) the significance of the decline in net assets of the FHLB as compared to the capital stock amount and the length of time this situation has persisted (b) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance (c) the impact of legislative and regulatory changes on the customer base of the FHLB and (d) the liquidity position of the FHLB.

The FHLB had incurred losses in 2009 and for parts of 2010 due primarily to other-than-temporary impairment credit losses on its private-label mortgage-backed securities portfolio. These securities were the most effected by the extreme economic conditions in place during the previous several years. As a result, the FHLB had suspended the payment of dividends and limited the amount of excess capital stock repurchases. The FHLB has reported net income for both the fourth quarter and the year ended December 31, 2011 and declared a 0.10 percent annualized dividend to its shareholders that was paid during the first quarter of 2012. While the FHLB has not committed to regular dividend payments or future limited repurchases of excess capital stock, it will continue to monitor the overall financial performance of the FHLB in order to determine the status of limited repurchases of excess capital stock or dividends in the future. Management evaluated the stock and concluded that the stock was not impaired for the periods presented herein. More consideration was given to the long-term prospects for the FHLB as opposed to the recent stress caused by the extreme economic conditions the world is facing. Management also considered that the FHLB maintains regulatory capital ratios in excess of all regulatory capital requirements, liquidity appears adequate, new shares of FHLB stock continue to change hands at the \$100 par value, and the resumption of dividends.

**Note 6 Credit Quality and Related Allowance for Loan Losses**

Management segments the Bank's loan portfolio to a level that enables risk and performance monitoring according to similar risk characteristics. Loans are segmented based on the underlying collateral characteristics. Categories include commercial and agricultural, real estate, and installment loans to individuals. Real estate loans are further segmented into three categories: residential, commercial and construction.

The following table presents the related aging categories of loans, by segment, as of March 31, 2012 and December 31, 2011:

Table of Contents

(In Thousands)	Current	Past Due 30 To 89 Days	March 31, 2012 Past Due 90 Days Or More & Still Accruing	Non- Accrual	Total
Commercial and agricultural	\$ 53,479	\$ 71	\$	\$	\$ 53,550
Real estate mortgage:					
Residential	184,662	1,190		517	186,369
Commercial	162,350	739		1,115	164,204
Construction	20,391	114		9,675	30,180
Installment loans to individuals	10,784	49	1		10,834
	431,666	\$ 2,163	\$ 1	\$ 11,307	445,137
Less: Net deferred loan fees and discounts	(1,560)				(1,560)
Allowance for loan losses	7,745				7,745
Loans, net	\$ 425,481				\$ 438,952

(In Thousands)	Current	Past Due 30 To 89 Days	December 31, 2011 Past Due 90 Days Or More & Still Accruing	Non- Accrual	Total
Commercial and agricultural	\$ 53,124	\$ 5	\$	\$	\$ 53,129
Real estate mortgage:					
Residential	176,875	1,438	378	692	179,383
Commercial	162,977	135		1,176	164,288
Construction	19,605	95		9,757	29,457
Installment loans to individuals	11,180	111	6		11,297
	423,761	\$ 1,784	\$ 384	\$ 11,625	437,554
Less: Net deferred loan fees and discounts	1,595				1,595
Allowance for loan losses	7,154				7,154
Loans, net	\$ 415,012				\$ 428,805

The following table presents the interest income if interest had been recorded based on the original loan agreement terms and rate of interest for non-accrual loans and interest income recognized on a cash basis for non-accrual loans as of March 31, 2012 and March 31, 2011:

(In Thousands)	Three Months Ended March 31,	
	2012	2011
Interest income if interest had been recorded based on the original loan agreement terms and rate of interest for non-accrual loans	145	210
Interest income recognized on a cash basis for non-accrual loans	40	6

**Impaired Loans**

Impaired loans are loans for which it is probable the Bank will not be able to collect all amounts due according to the contractual terms of the loan agreement. The Bank evaluates such loans for impairment individually and does not aggregate loans by major risk classifications. The definition of impaired loans is not the same as the definition of non-accrual loans, although the two categories overlap. The Bank may choose to place a loan on non-accrual status due to payment delinquency or uncertain collectability, while not classifying the loan as impaired. Factors considered by management in determining impairment include payment status and collateral value. The amount of impairment for these types of loans is determined by the difference between the present value of the expected cash flows related to the loan, using the original interest rate, and

## Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

its recorded value, or as a practical expedient in the case of collateralized loans, the difference between the fair value of the collateral and the recorded amount of the loan. When foreclosure is probable, impairment is measured based on the fair value of the collateral.

Management evaluates individual loans in all of the commercial segments for possible impairment if the loan is greater than \$100,000 and if the loan is either on non-accrual status or has a risk rating of substandard. Management may also elect to measure an individual loan for impairment if less than \$100,000 on a case by case basis.

Mortgage loans on one-to-four family properties and all consumer loans are large groups of smaller-balance homogeneous loans and are measured for impairment collectively. Loans that experience insignificant payment delays, which are defined as 90 days or less,



Table of Contents

generally are not classified as impaired. Management determines the significance of payment delays on a case-by-case basis taking into consideration all circumstances surrounding the loan and the borrower including the length of the delay, the borrower's prior payment record, and the amount of shortfall in relation to the principal and interest owed. Interest income for impaired loans is recorded consistent with the Bank's policy on nonaccrual loans.

The following table presents the recorded investment, unpaid principal balance, and related allowance of impaired loans by segment as of March 31, 2012 and December 31, 2011:

(In Thousands)	Recorded Investment	March 31, 2012 Unpaid Principal Balance	Related Allowance
With no related allowance recorded:			
Commercial and agricultural	\$	\$	\$
Real estate mortgages - residential	587	596	
Real estate mortgages - commercial	342	342	
Real estate mortgages - construction	797	1,095	
Installment loans to individuals			
	1,726	2,033	
With an allowance recorded:			
Commercial and agricultural			
Real estate mortgages - residential	833	858	98
Real estate mortgages - commercial	6,140	6,140	1,518
Real estate mortgages - construction	8,879	10,379	2,102
Installment loans to individuals			
	15,852	17,377	3,718
Total:			
Commercial and agricultural			
Real estate mortgages - residential	1,420	1,454	98
Real estate mortgages - commercial	6,482	6,482	1,518
Real estate mortgages - construction	9,676	11,474	2,102
Installment loans to individuals			
	\$ 17,578	\$ 19,410	\$ 3,718

Table of Contents

(In Thousands)	Recorded Investment	December 31, 2011 Unpaid Principal Balance	Related Allowance
With no related allowance recorded:			
Commercial and agricultural	\$	\$	\$
Real estate mortgages - residential	742	751	
Real estate mortgages - commercial	382	382	
Real estate mortgages - construction	815	1,113	
Installment loans to individuals			
	1,939	2,246	
With an allowance recorded:			
Commercial and agricultural			
Real estate mortgages - residential	861	888	101
Real estate mortgages - commercial	6,150	6,150	1,481
Real estate mortgages - construction	8,929	10,429	2,155
Installment loans to individuals			
	15,940	17,467	3,737
Total:			
Commercial and agricultural			
Real estate mortgages - residential	1,603	1,639	101
Real estate mortgages - commercial	6,532	6,532	1,481
Real estate mortgages - construction	9,744	11,542	2,155
Installment loans to individuals			
	\$ 17,879	\$ 19,713	\$ 3,737

The following table presents the average recorded investment in impaired loans and related interest income recognized for the three months ended for March 31, 2012 and 2011:

(In Thousands)	Three Months Ended March 31,	
	2012	2011
Average investment in impaired loans	\$ 17,728	\$ 10,005
Interest income recognized on an accrual basis on impaired loans	81	79
Interest income recognized on a cash basis on impaired loans	56	6

There is approximately \$317,000 committed to be advanced in connection with impaired loans.

**Modifications**

The loan portfolio also includes certain loans that have been modified in a Troubled Debt Restructuring (TDR), where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Certain TDRs are classified as nonperforming at the time of restructure and may only be returned to performing status after considering the borrower's sustained repayment performance for a reasonable period, generally six months.

Loan modifications that are considered TDRs completed during the three months ended March 31, 2012 and 2011 were as follows:



Table of Contents

(In Thousands, Except Number of Contracts)	Number of Contracts	Three Months Ended March 31,		
		2012 Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	2011 Pre-Modification Outstanding Recorded Investment
Commercial and agricultural		\$	\$	\$
Real estate mortgages - residential	1	104	104	123
Real estate mortgages - commercial	1	37	37	880
Real estate mortgages - construction	2	26	26	610
Installment loans to individuals				2
Total	4	\$ 167	\$ 167	\$ 1,615

Loan modifications considered troubled debt restructurings made during the twelve months previous to March 31, 2012, that have defaulted during the three months ended March 31, 2012 were as follows:

(In Thousands, Except Number of Contracts)	Three Months Ended March 31, 2012	
	Number of Contracts	Recorded Investment
Commercial and agricultural		\$
Real estate mortgages - residential	1	104
Real estate mortgages - commercial		
Real estate mortgages - construction	1	236
Installment loans to individuals		
Total	2	\$ 340

Troubled debt restructurings amounted to approximately \$17,361,000 and \$5,362,000 as of March 31, 2012 and 2011.

**Internal Risk Ratings**

Management uses a ten point internal risk rating system to monitor the credit quality of the overall loan portfolio. The first six categories are considered not criticized, and are aggregated as Pass rated. The criticized rating categories utilized by management generally follow bank regulatory definitions. The special mention category includes assets that are currently protected but are potentially weak, resulting in an undue and unwarranted credit risk, but not to the point of justifying a substandard classification. Loans in the substandard category have well-defined weaknesses that jeopardize the liquidation of the debt, and have a distinct possibility that some loss will be sustained if the weaknesses are not corrected. All loans greater than 90 days past due are considered Substandard. Loans in the doubtful category exhibit the same weaknesses found in the substandard loans, however, the weaknesses are more pronounced. Such loans are static and collection in full is improbable. However, these loans are not yet rated as loss because certain events may occur which would salvage the debt. Loans classified loss are considered uncollectible and charge-off is imminent.

To help ensure that risk ratings are accurate and reflect the present and future capacity of borrowers to repay a loan as agreed, the Bank has a structured loan rating process with several layers of internal and external oversight. Generally, consumer and residential mortgage loans are included in the pass category unless a specific action, such as bankruptcy, repossession, or death occurs to raise awareness of a possible credit event. An external annual loan review of all commercial relationships \$800,000 or greater is performed, as well as a sample of smaller transactions. Confirmation of the appropriate risk category is included in the review. Detailed reviews, including plans for resolution, are

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

performed on loans classified as Substandard, Doubtful, or Loss on a quarterly basis.

The following table presents the credit quality categories identified above as of March 31, 2012 and December 31, 2011:

(In Thousands)	March 31, 2012						Totals
	Commercial and Agricultural	Residential	Real Estate Mortgages		Construction	Installment Loans to Individuals	
Pass	\$ 52,236	\$ 185,459	\$ 153,037	\$ 20,457	\$ 10,834	\$ 422,023	
Special Mention	1,150		1,775			2,925	
Substandard	164	910	9,392	9,723		20,189	
Doubtful							
Total	\$ 53,550	\$ 186,369	\$ 164,204	\$ 30,180	\$ 10,834	\$ 445,137	

Table of Contents

(In Thousands)	December 31, 2011							Totals
	Commercial and Agricultural	Residential	Real Estate Mortgages		Construction	Installment Loans to Individuals		
Pass	\$ 51,663	\$ 177,916	\$ 152,994	\$ 19,652	\$ 11,291	\$ 413,516		
Special Mention	1,198	89	5,804			7,091		
Substandard	268	1,378	5,490	9,805	6	16,947		
Doubtful								
Total	\$ 53,129	\$ 179,383	\$ 164,288	\$ 29,457	\$ 11,297	\$ 437,554		

**Allowance for Loan Losses**

An allowance for loan losses ( ALL ) is maintained to absorb losses from the loan portfolio. The ALL is based on management's continuing evaluation of the risk characteristics and credit quality of the loan portfolio, assessment of current economic conditions, diversification and size of the portfolio, adequacy of collateral, past and anticipated future loss experience, and the amount of non-performing loans.

The Bank's methodology for determining the ALL is based on the requirements of ASC Section 310-10-35 for loans individually evaluated for impairment (previously discussed) and ASC Subtopic 450-20 for loans collectively evaluated for impairment, as well as the Interagency Policy Statements on the Allowance for Loan and Lease Losses and other bank regulatory guidance. The total of the two components represents the Bank's ALL.

Loans that are collectively evaluated for impairment are analyzed with general allowances being made as appropriate. Allowances are segmented based on collateral characteristics previously disclosed, and consistent with credit quality monitoring. Loans that are collectively evaluated for impairment are grouped into two classes for evaluation. A general allowance is determined for Pass rated credits, while a separate pool allowance is provided for Criticized rated credits that are not individually evaluated for impairment.

For the general allowances, historical loss trends are used in the estimation of losses in the current portfolio. These historical loss amounts are modified by other qualitative factors. A historical charge-off factor is calculated utilizing a twelve quarter moving average. Management has identified a number of additional qualitative factors which it uses to supplement the historical charge-off factor because these factors are likely to cause estimated credit losses associated with the existing loan pools to differ from historical loss experience. The additional factors that are evaluated quarterly and updated using information obtained from internal, regulatory, and governmental sources are: national and local economic trends and conditions; levels of and trends in delinquency rates and non-accrual loans; trends in volumes and terms of loans; effects of changes in lending policies; experience, ability, and depth of lending staff; value of underlying collateral; and concentrations of credit from a loan type, industry and/or geographic standpoint.

Loans in the criticized pools, which possess certain qualities or characteristics that may lead to collection and loss issues, are closely monitored by management and subject to additional qualitative factors. Management also monitors industry loss factors by loan segment for applicable adjustments to actual loss experience.

Management reviews the loan portfolio on a quarterly basis in order to make appropriate and timely adjustments to the ALL. When information confirms all or part of specific loans to be uncollectible, these amounts are promptly charged off against the ALL.

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Activity in the allowance is presented for the three months ended March 31, 2012 and 2011:

(In Thousands)	March 31, 2012						Totals
	Commercial and Agricultural	Residential	Real Estate Mortgages		Construction	Installment Loans to Individuals	
			Commercial				
Beginning Balance	\$ 430	\$ 964	\$ 2,719		\$ 2,846	\$ 195	\$ 7,154
Charge-offs						(32)	(32)
Recoveries	1	2	1		3	16	23
Provision	(19)	(48)	686		(22)	3	600
Ending Balance	\$ 412	\$ 918	\$ 3,406		\$ 2,827	\$ 182	\$ 7,745

(In Thousands)	March 31, 2011						Totals
	Commercial and Agricultural	Residential	Real Estate Mortgages		Construction	Installment Loans to Individuals	
			Commercial				
Beginning Balance	\$ 466	\$ 980	\$ 1,508		\$ 2,893	\$ 188	\$ 6,035
Charge-offs		(25)				(19)	(44)
Recoveries	6	2	20		2	19	49
Provision	184	(66)	56		445	(19)	600
Ending Balance	\$ 656	\$ 891	\$ 1,584		\$ 3,340	\$ 169	\$ 6,640

Table of Contents

The Company grants commercial, industrial, residential, and installment loans to customers throughout north-central Pennsylvania. Although the Company has a diversified loan portfolio at March 31, 2012, a substantial portion of its debtors' ability to honor their contracts is dependent on the economic conditions within this region.

The Company has a concentration of loans at March 31, 2012 and 2011 as follows:

	2012	March 31, 2011
Owners of residential rental properties	13.99%	13.91%
Owners of commercial rental properties	16.51%	16.77%

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of March 31, 2012 and December 31, 2011:

(In Thousands)	March 31, 2012						Totals					
	Commercial and Agricultural	Residential	Real Estate Mortgages		Construction	Installment Loans to Individuals						
Allowance for Loan Losses:												
Ending allowance balance attributable to loans:												
Individually evaluated for impairment	\$	\$	98	\$	1,518	\$	\$	3,718				
Collectively evaluated for impairment		412	820		1,888	725	182	4,027				
Total ending allowance balance	\$	412	\$	918	\$	3,406	\$	2,827	\$	182	\$	7,745
Loans:												
Individually evaluated for impairment	\$	\$	1,420	\$	6,482	\$	9,676	\$	\$	17,578		
Collectively evaluated for impairment		53,550	184,949		157,722	20,504	10,834	427,559				
Total ending loans balance	\$	53,550	\$	186,369	\$	164,204	\$	30,180	\$	10,834	\$	445,137

(In Thousands)	December 31, 2011						Totals					
	Commercial and Agricultural	Residential	Real Estate Mortgages		Construction	Installment Loans to Individuals						
Allowance for Loan Losses:												
Ending allowance balance attributable to loans:												
Individually evaluated for impairment	\$	\$	101	\$	1,481	\$	2,155	\$	\$	3,737		
Collectively evaluated for impairment		430	863		1,238	691	195	3,417				
Total ending allowance balance	\$	430	\$	964	\$	2,719	\$	2,846	\$	195	\$	7,154



## Loans:

Individually evaluated for impairment	\$		\$	1,603	\$	6,532	\$	9,744	\$		\$	17,879
Collectively evaluated for impairment		53,129		177,780		157,756		19,713		11,297		419,675
Total ending loans balance	\$	53,129	\$	179,383	\$	164,288	\$	29,457	\$	11,297	\$	437,554

**Note 7 Net Periodic Benefit Cost-Defined Benefit Plans**

For a detailed disclosure on the Company's pension and employee benefits plans, please refer to Note 12 of the Company's Consolidated Financial Statements included in the Annual Report on Form 10-K for the year ended December 31, 2011.

The following sets forth the components of the net periodic benefit cost of the domestic non-contributory defined benefit plan for the three months ended March 31, 2012 and 2011, respectively:

(In Thousands)	Three Months Ended March 31,	
	2012	2011
Service cost	\$ 157	\$ 106
Interest cost	186	178
Expected return on plan assets	(196)	(184)
Amortization of transition obligation	(1)	(1)
Amortization of prior service cost	7	6
Amortization of net loss	109	41
Net periodic cost	\$ 262	\$ 146

Table of Contents**Employer Contributions**

The Company previously disclosed in its consolidated financial statements, included in the Annual Report on Form 10-K for the year ended December 31, 2011, that it expected to contribute a minimum of \$750,000 to its defined benefit plan in 2012. As of March 31, 2012, there were contributions of \$250,000 made to the plan.

**Note 8 Employee Stock Purchase Plan**

The Company maintains the Penns Woods Bancorp, Inc. 2006 Employee Stock Purchase Plan ( Plan ). The Plan is intended to encourage employee participation in the ownership and economic progress of the Company. The Plan allows for up to 1,000,000 shares to be purchased by employees. The purchase price of the shares is 95% of market value with an employee eligible to purchase up to the lesser of 15% of base compensation or \$12,000 in market value annually. During the three months ended March 31, 2012 and 2011, there were 391 and 480 shares issued under the plan, respectively.

**Note 9 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. These financial instruments are primarily comprised of commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit, interest rate, or liquidity risk in excess of the amount recognized in the consolidated balance sheet. The contract amounts of these instruments express the extent of involvement the Company has in particular classes of financial instruments.

The Company's exposure to credit loss from nonperformance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual amount of these instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The Company may require collateral or other security to support financial instruments with off-balance sheet credit risk.

Financial instruments whose contract amounts represent credit risk are as follows at March 31, 2012 and December 31, 2011:

(In Thousands)	March 31, 2012	December 31, 2011
Commitments to extend credit	\$ 92,116	\$ 80,320
Standby letters of credit	1,164	1,180

Commitments to extend credit are legally binding agreements to lend to customers. Commitments generally have fixed expiration dates or other termination clauses and may require payment of fees. Since many of the commitments are expected to expire without being drawn upon, the

total commitment amounts do not necessarily represent future liquidity requirements. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company, on an extension of credit is based on management's credit assessment of the counterparty.

Standby letters of credit represent conditional commitments issued by the Company to guarantee the performance of a customer to a third party. These instruments are issued primarily to support bid or performance related contracts. The coverage period for these instruments is typically a one year period with an annual renewal option subject to prior approval by management. Fees earned from the issuance of these letters are recognized upon expiration of the coverage period. For secured letters of credit, the collateral is typically Bank deposit instruments or customer business assets.

**Note 10 Fair Value Measurements**

The following disclosures show the hierarchal disclosure framework associated with the level of pricing observations utilized in measuring assets and liabilities at fair value.

- Level I: Quoted prices are available in active markets for identical assets or liabilities as of the reported date.
- Level II: Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these assets and liabilities include items for which quoted prices are available but traded less frequently, and items that are fair valued using other financial instruments, the parameters of which can be directly observed.
- Level III: Assets and liabilities that have little to no pricing observability as of the reported date. These items do not have two-way markets and are measured using management's best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation.

This hierarchy requires the use of observable market data when available.

Table of Contents

The following table presents the assets reported on the balance sheet at their fair value on a recurring basis as of March 31, 2012 and December 31, 2011, by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

(In Thousands)	March 31, 2012			Total
	Level I	Level II	Level III	
Assets measured on a recurring basis:				
Investment securities, available for sale:				
U.S. Government and agency securities	\$	\$ 23,499	\$	\$ 23,499
State and political securities		182,171		182,171
Other debt securities		65,666		65,666
Financial institution equity securities	10,157			10,157
Other equity securities	3,285			3,285
Total assets measured on a recurring basis	\$ 13,442	\$ 271,336	\$	\$ 284,778

(In Thousands)	December 31, 2011			Total
	Level I	Level II	Level III	
Assets measured on a recurring basis:				
Investment securities, available for sale:				
U.S. Government and agency securities	\$	\$ 28,671	\$	\$ 28,671
State and political securities		178,301		178,301
Other debt securities		49,514		49,514
Financial institution equity securities	10,802			10,802
Other equity securities	2,809			2,809
Total assets measured on a recurring basis	\$ 13,611	\$ 256,486	\$	\$ 270,097

The following table presents the assets reported on the consolidated balance sheet at their fair value on a non-recurring basis as of March 31, 2012 and December 31, 2011, by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

(In Thousands)	March 31, 2012			Total
	Level I	Level II	Level III	
Assets measured on a non-recurring basis:				
Impaired loans	\$	\$	\$ 13,859	\$ 13,859
Other real estate owned			2,034	2,034
Total assets measured on a non-recurring basis	\$	\$	\$ 15,893	\$ 15,893

(In Thousands)	December 31, 2011			Total
	Level I	Level II	Level III	
Assets measured on a non-recurring basis:				

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Impaired loans	\$	\$	\$	14,142	\$	14,142
Other real estate owned				2,144		2,144
Total assets measured on a non-recurring basis	\$	\$	\$	16,286	\$	16,286

The following table provides a listing of significant unobservable inputs used in the fair value measurement process for items valued utilizing level III techniques as of March 31, 2012.

Table of Contents

(In Thousands)	Fair Value	Quantitative Information About Level III Fair Value Measurements		Range
		Valuation Technique(s)	Unobservable Inputs	
Impaired loans	13,859	Discounted cash flow	Temporary change in payment amount	0 to -30%
			Probability of default	0%
		Appraisal of collateral	Appraisal adjustments (1)	0 to -20%
Other real estate owned	2,034	Appraisal of collateral	Appraisal adjustments (1)	0%

(1) Appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated liquidation expenses. The range of appraisal adjustments are presented as a percent of the appraisal.

The significant unobservable inputs used in the fair value measurement of the Company's impaired loans using the discounted cash flow valuation technique include temporary changes in payment amounts and the probability of default. Significant increases (decreases) in payment amounts would result in significantly higher (lower) fair value measurements. The probability of default is 0% for impaired loans using the discounted cash flow valuation technique because all defaulted impaired loans are valued using the appraisal of collateral valuation technique.

The significant unobservable input used in the fair value measurement of the Company's impaired loans using the appraisal of collateral valuation technique include appraisal adjustments, which are adjustments to appraisals by management for qualitative factors such as economic conditions and estimated liquidation expenses. The significant unobservable input used in the fair value measurement of the Company's other real estate owned are the same inputs used to value impaired loans using the appraisal of collateral valuation technique.

**Note 11 Fair Value of Financial Instruments**

The Company is required to disclose fair values for its financial instruments. Fair values are made at a specific point in time, based on relevant market information and information about the financial instrument. These fair values do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Also, it is the Company's general practice and intention to hold most of its financial instruments to maturity and not to engage in trading or sales activities. Because no market exists for a significant portion of the Company's financial instruments, fair values are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These fair values are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions can significantly affect the fair values.

Fair values have been determined by the Company using historical data and an estimation methodology suitable for each category of financial instruments. The Company's fair value, methods, and assumptions are set forth below for the Company's other financial instruments.

As certain assets and liabilities, such as deferred tax assets, premises and equipment, and many other operational elements of the Company, are not considered financial instruments but have value, this estimated fair value of financial instruments would not represent the full market value of the Company.

The fair values of the Company's financial instruments are as follows at March 31, 2012 and December 31, 2011:

Table of Contents

(In Thousands)	Fair Value Measurements at March 31, 2012				
	Carrying Value	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level I)	Significant Other Observable Inputs (Level II)	Significant Unobservable Inputs (Level III)
<b>Financial assets:</b>					
Cash and cash equivalents	\$ 23,431	\$ 23,431	\$ 23,431	\$	\$
<b>Investment securities:</b>					
Available for sale	284,778	284,778	13,442	271,336	
Held to maturity	55	55	55		
Loans held for sale	2,065	2,065	2,065		
Loans, net	435,832	430,454		416,595	13,859
Bank-owned life insurance	15,973	15,973	15,973		
Accrued interest receivable	4,100	4,100	4,100		
<b>Financial liabilities:</b>					
Interest-bearing deposits	\$ 505,271	\$ 503,592	\$	\$ 503,592	
Noninterest-bearing deposits	116,271	116,271	116,271		
Short-term borrowings	14,768	14,768	14,768		
Long-term borrowings, FHLB	61,278	66,304		66,304	
Accrued interest payable	506	506	506		

(In Thousands)	December 31, 2011	
	Carrying Value	Fair Value
<b>Financial assets:</b>		
Cash and cash equivalents	\$ 13,885	\$ 13,885
<b>Investment securities:</b>		
Available for sale	270,097	270,097
Held to maturity	54	55
Loans held for sale	3,787	3,787
Loans, net	428,805	424,586
Bank-owned life insurance	16,065	16,065
Accrued interest receivable	3,905	3,905
<b>Financial liabilities:</b>		
Interest-bearing deposits	\$ 470,310	\$ 471,212
Noninterest-bearing deposits	111,354	111,354
Short-term borrowings	29,598	29,598
Long-term borrowings, FHLB	61,278	65,848
Accrued interest payable	536	536

**Cash and Cash Equivalents, Loans Held for Sale, Accrued Interest Receivable, Short-term Borrowings, and Accrued Interest Payable:**

The fair value is equal to the carrying value.

**Investment Securities:**

The fair value of investment securities available for sale and held to maturity is equal to the available quoted market price. If no quoted market price is available, fair value is estimated using the quoted market price for similar securities. Regulatory stocks fair value is equal to the carrying value.



**Loans:**

Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as commercial, commercial real estate, residential real estate, construction real estate, and installment loans to individuals. Each loan category is further segmented into fixed and adjustable rate interest terms and by performing and nonperforming categories.

The fair value of performing loans is calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan. The estimate of maturity is based on the Company's historical experience with repayments for each loan classification, modified, as required, by an estimate of the effect of current economic and lending conditions.

Fair value for significant nonperforming loans is based on recent external appraisals. If appraisals are not available, estimated cash

Table of Contents

flows are discounted using a rate commensurate with the risk associated with the estimated cash flows. Assumptions regarding credit risk, cash flows, and discounted rates are judgmentally determined using available market information and specific borrower information.

**Bank-Owned Life Insurance:**

The fair value is equal to the cash surrender value of the life insurance policies.

**Deposits:**

The fair value of deposits with no stated maturity, such as noninterest-bearing demand deposits, savings, NOW, and money market accounts, is equal to the amount payable on demand. The fair value of certificates of deposit is based on the discounted value of contractual cash flows.

The fair value estimates above do not include the benefit that results from the low-cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market, commonly referred to as the core deposit intangible.

**Long Term Borrowings:**

The fair value of long term borrowings is based on the discounted value of contractual cash flows.

**Commitments to Extend Credit, Standby Letters of Credit, and Financial Guarantees Written:**

There is no material difference between the notional amount and the estimated fair value of off-balance sheet items. The contractual amounts of unfunded commitments and letters of credit are presented in Note 9 (Off Balance Sheet Risk).

**Note 12 Reclassification of Comparative Amounts**

Certain comparative amounts for the prior period have been reclassified to conform to current period presentations. Such reclassifications had no effect on net income or shareholders' equity.

**CAUTIONARY STATEMENT FOR PURPOSES OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995**

This Report contains certain forward-looking statements including statements concerning plans, objectives, future events or performance and assumptions and other statements which are other than statements of historical fact. The Company cautions readers that the following important factors, among others, may have affected and could in the future affect the Company's actual results and could cause the Company's actual results

## Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

for subsequent periods to differ materially from those expressed in any forward-looking statement made by or on behalf of the Company herein: (i) the effect of changes in laws and regulations, including federal and state banking laws and regulations, with which the Company must comply, and the associated costs of compliance with such laws and regulations either currently or in the future as applicable; (ii) the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies as well as by the Financial Accounting Standards Board, or of changes in the Company's organization, compensation and benefit plans; (iii) the effect on the Company's competitive position within its market area of the increasing consolidation within the banking and financial services industries, including the increased competition from larger regional and out-of-state banking organizations as well as non-bank providers of various financial services; (iv) the effect of changes in interest rates; and (v) the effect of changes in the business cycle and downturns in the local, regional or national economies.

You should not put undue reliance on any forward-looking statements. These statements speak only as of the date of this Quarterly Report on Form 10-Q, even if subsequently made available by the Company on its website or otherwise. The Company undertakes no obligation to update or revise these statements to reflect events or circumstances occurring after the date of this Quarterly Report on Form 10-Q.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operation****EARNINGS SUMMARY****Comparison of the Three Months Ended March 31, 2012 and 2011****Summary Results**

Net income for the three months ended March 31, 2012 was \$3,689,000 compared to \$2,853,000 for the same period of 2011 as after-tax securities gains increased \$306,000 (from a gain of \$83,000 to a gain of \$389,000). In addition, a gain of \$109,000 on a death benefit related to bank owned life insurance was recorded during the three months ended March 31, 2012. Basic and diluted earnings per share for the three months ended March 31, 2012 were \$0.96 compared to \$0.74 for the three months ended March 31, 2011. Return on average assets and return on average equity were 1.91% and 17.39% for the three months ended March 31, 2012 compared to 1.65% and 16.62% for the corresponding period of 2011. Net income from core operations ( operating earnings ) increased to \$3,191,000 for the three months ended March 31, 2012 compared to \$2,770,000 for the same period of 2011. Operating earnings per share for the three months ended March 31, 2012 were \$0.83 basic and dilutive compared to \$0.72 basic and dilutive for the three months ended March 31, 2011.

Management uses the non-GAAP measure of net income from core operations, or operating earnings, in its analysis of the Company's performance. This measure, as used by the Company, adjusts net income by excluding significant gains or losses that are unusual in nature. Because certain of these items and their impact on the Company's performance are difficult to predict, management believes the presentation of financial measures excluding the impact of such items provides useful supplemental information in evaluating the operating results of the Company's core businesses. For purposes of this Quarterly Report on Form 10-Q, net income from core operations, or operating earnings, means net income adjusted to exclude after-tax net securities gains or losses. These disclosures should not be viewed as a substitute for net income determined in accordance with GAAP, nor are they necessarily comparable to non-GAAP performance measures that may be presented by other companies.

**Reconciliation of GAAP and Non-GAAP Income**

(Dollars in Thousands, Except Per Share Data)	Three Months Ended March 31,	
	2012	2011
GAAP net income	\$ 3,689	\$ 2,853
Less: net securities and bank-owned life insurance gains, net of tax	498	83
Non-GAAP operating earnings	\$ 3,191	\$ 2,770

	Three Months Ended March 31,	
	2012	2011
Return on average assets (ROA)	1.91%	1.65%

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Less: net securities and bank-owned life insurance gains, net of tax	0.26%	0.05%
Non-GAAP operating ROA	1.65%	1.60%

	Three Months Ended March 31,	
	2012	2011
Return on average equity (ROE)	17.39%	16.62%
Less: net securities and bank-owned life insurance gains, net of tax	2.35%	0.48%
Non-GAAP operating ROE	15.04%	16.14%

	Three Months Ended March 31,			
	2012		2011	
Basic earnings per share (EPS)	\$	0.96	\$	0.74
Less: net securities and bank-owned life insurance gains, net of tax		0.13		0.02
Non-GAAP basic operating EPS	\$	0.83	\$	0.72

Table of Contents

	Three Months Ended			
	2012		2011	
	March 31,			
Dilutive EPS	\$	0.96	\$	0.74
Less: net securities and bank-owned life insurance gains, net of tax		0.13		0.02
Non-GAAP dilutive operating EPS	\$	0.83	\$	0.72

**Interest and Dividend Income**

Interest and dividend income increased to \$9,285,000 for the three months ended March 31, 2012 compared to \$8,982,000 for the same period of 2011. Loan interest including fees remained flat as the impact of portfolio growth was offset by a yield that decreased 35 basis points ( bp ) due to the downward pressure on current loan offerings and the downward repricing of the variable rate segment of the loan portfolio. Investment portfolio interest increased due to growth in the average investment portfolio of \$59,942,000 primarily from the addition of corporate and municipal bonds to the portfolio, which offset a decline in the average taxable equivalent yield of 83 bp. Dividend and other interest income increased due to a focus on purchasing dividend-yielding investments.

Interest and dividend income composition for the three months ended March 31, 2012 and 2011 was as follows:

(In Thousands)	March 31, 2012		For The Three Months Ended March 31, 2011		Change	
	Amount	% Total	Amount	% Total	Amount	%
Loans including fees	\$ 6,314	68.00%	\$ 6,288	70.00%	\$ 26	0.41%
Investment securities:						
Taxable	1,474	15.88	1,375	15.31	99	7.20
Tax-exempt	1,405	15.13	1,267	14.11	138	10.89
Dividend and other interest income	92	0.99	52	0.58	40	76.92
Total interest and dividend income	\$ 9,285	100.00%	\$ 8,982	100.00%	\$ 303	3.37%

**Interest Expense**

Interest expense for the three months ended March 31, 2012 decreased \$370,000 to \$1,615,000 compared to \$1,985,000 for the same period of 2011. The substantial decrease associated with deposits is primarily the result of a reduction of 37 bp in the rate paid on time deposits and a shift from higher cost time deposits to core deposits, with emphasis on money market and NOW accounts. Factors that led to the rate decreases include, but are not limited to, Federal Open Market Committee ( FOMC ) interest rate actions and campaigns conducted by the Company to focus on core deposit growth (non-time deposits) as the building block to solid customer relationships. In addition, during the past two years the time deposit portfolio has been shortened in order to increase repricing frequency. The time deposit portfolio is now being lengthened to build protection when interest rates begin to increase with a focus on maturities of 36 months and greater. Borrowing interest expense decreased as the significant growth in deposits has allowed for a reduction in the average balance of total borrowings.

Interest expense composition for the three months ended March 31, 2012 and 2011 was as follows:

(In Thousands)	March 31, 2012		For The Three Months Ended March 31, 2011		Change	
	Amount	% Total	Amount	% Total	Amount	%
Deposits	\$ 961	59.50%	\$ 1,194	60.15%	\$ (233)	(19.51)%
Short-term borrowings	34	2.11	57	2.87	(23)	(40.35)
Long-term borrowings, FHLB	620	38.39	734	36.98	(114)	(15.53)
Total interest expense	\$ 1,615	100.00%	\$ 1,985	100.00%	\$ (370)	(18.64)%

### Net Interest Margin

The net interest margin ( NIM ) for the three months ended March 31, 2012 was 4.72% compared to 4.89% for the corresponding period of 2011. While the net interest margin has decreased year over year, net interest income on a fully taxable equivalent basis has increased \$743,000 to \$8,498,000 for the three months ended March 31, 2012 compared to the corresponding period of 2011. Driving this increase is the continued emphasis on core deposit growth. These deposits represent a lower cost funding source than time deposits and comprise 71.5% of total deposits at March 31, 2012 compared to 64.9% at March 31, 2011. The average rate paid on total interest-bearing deposits decreased 33 bp for the three months ended March 31, 2012 compared to the same period of 2011. The decrease was led by the rate paid on time deposits decreasing 37 bp for the three months ended March 31, 2012 compared to the same period of 2011. The duration of the time deposit portfolio, which was shortened over the past several years, is now being slowly lengthened due to the apparent bottoming or near bottoming of deposit rates. FHLB long-term borrowings have been reduced by

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Table of Contents

\$10,500,000 since March 31, 2011 as borrowings carrying an average rate of 4.60% matured during the three months ended December 31, 2011.

The following is a schedule of average balances and associated yields for the three months ended March 31, 2012 and 2011:

(In Thousands)	AVERAGE BALANCES AND INTEREST RATES			AVERAGE BALANCES AND INTEREST RATES		
	Three Months Ended March 31, 2012			Three Months Ended March 31, 2011		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
<b>Assets:</b>						
Tax-exempt loans	\$ 21,591	\$ 309	5.76%	\$ 20,377	\$ 308	6.13%
All other loans	422,098	6,110	5.82%	399,599	6,085	6.18%
Total loans	443,689	6,419	5.82%	419,976	6,393	6.17%
Taxable securities	147,200	1,566	4.26%	114,740	1,427	4.97%
Tax-exempt securities	130,590	2,128	6.52%	103,108	1,920	7.45%
Total securities	277,790	3,694	5.32%	217,848	3,347	6.15%
Interest-bearing deposits	2,037		0.00%	2,002		0.00%
Total interest-earning assets	723,516	10,113	5.61%	639,826	9,740	6.14%
Other assets	50,914			53,883		
Total assets	\$ 774,430			\$ 693,709		
<b>Liabilities and shareholders equity:</b>						
Savings	\$ 73,628	11	0.06%	\$ 66,510	35	0.21%
Super Now deposits	108,369	142	0.53%	69,177	83	0.49%
Money market deposits	127,387	205	0.65%	109,196	265	0.98%
Time deposits	177,083	603	1.37%	188,561	811	1.74%
Total interest-bearing deposits	486,467	961	0.79%	433,444	1,194	1.12%
Short-term borrowings	22,058	34	0.62%	19,207	57	1.20%
Long-term borrowings, FHLB	61,278	620	4.00%	71,778	734	4.09%
Total borrowings	83,336	654	3.11%	90,985	791	3.48%
Total interest-bearing liabilities	569,803	1,615	1.13%	524,429	1,985	1.53%
Demand deposits	108,081			91,473		
Other liabilities	11,669			9,155		
Shareholders equity	84,877			68,652		
Total liabilities and shareholders equity	\$ 774,430			\$ 693,709		
Interest rate spread			4.48%			4.61%
Net interest income/margin		\$ 8,498	4.72%		\$ 7,755	4.89%



- 
1. Information on this table has been calculated using average daily balance sheets to obtain average balances.
  
  2. Nonaccrual loans have been included with loans for the purpose of analyzing net interest earnings.
  
  3. Income and rates on a fully taxable equivalent basis include an adjustment for the difference between annual income from tax-exempt obligations and the taxable equivalent of such income at the standard 34% tax rate.

The following table presents the adjustment to convert net interest income to net interest income on a fully taxable equivalent basis for the three months ended March 31, 2012 and 2011.

Table of Contents

(In Thousands)	For the Three Months Ended March 31,			
	2012		2011	
Total interest income	\$	9,285	\$	8,982
Total interest expense		1,615		1,985
Net interest income		7,670		6,997
Tax equivalent adjustment		828		758
Net interest income (fully taxable equivalent)	\$	8,498	\$	7,755

The following table sets forth the respective impact that both volume and rate changes have had on net interest income on a fully taxable equivalent basis for the three months ended March 31, 2012 and 2011:

(In Thousands)	Three Months Ended March 31, 2012 vs. 2011					
	Volume	Increase (Decrease) Due to Rate		Net		
<b>Interest income:</b>						
Loans, tax-exempt	\$	38	\$	(37)	\$	1
Loans		708		(683)		25
Taxable investment securities		365		(226)		139
Tax-exempt investment securities		468		(260)		208
Interest bearing deposits						
Total interest-earning assets		1,579		(1,206)		373
<b>Interest expense:</b>						
Savings deposits		9		(33)		(24)
Super Now deposits		52		7		59
Money market deposits		98		(158)		(60)
Time deposits		(46)		(162)		(208)
Short-term borrowings		21		(44)		(23)
Long-term borrowings, FHLB		(99)		(15)		(114)
Total interest-bearing liabilities		35		(405)		(370)
Change in net interest income	\$	1,544	\$	(801)	\$	743

**Provision for Loan Losses**

The provision for loan losses is based upon management's quarterly review of the loan portfolio. The purpose of the review is to assess loan quality, identify impaired loans, analyze delinquencies, ascertain loan growth, evaluate potential charge-offs and recoveries, and assess general economic conditions in the markets served. An external independent loan review is also performed annually for the Bank. Management remains committed to an aggressive program of problem loan identification and resolution.

The allowance for loan losses is determined by applying loss factors to outstanding loans by type, excluding loans for which a specific allowance has been determined. Loss factors are based on management's consideration of the nature of the portfolio segments, changes in mix and volume of the loan portfolio, and historical loan loss experience. In addition, management considers industry standards and trends with respect to non-performing loans and its knowledge and experience with specific lending segments.

## Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Although management believes it uses the best information available to make such determinations and that the allowance for loan losses is adequate at March 31, 2012, future adjustments could be necessary if circumstances or economic conditions differ substantially from the assumptions used in making the initial determinations. A downturn in the local economy, increased unemployment, and delays in receiving financial information from borrowers could result in increased levels of nonperforming assets, charge-offs, loan loss provisions, and reductions in income. Additionally, as an integral part of the examination process, bank regulatory agencies periodically review the Bank's loan loss allowance. The banking agencies could require the recognition of additions to the loan loss allowance based on their judgment of information available to them at the time of their examination.

When determining the appropriate allowance level, management has attributed the allowance for loan losses to various portfolio segments; however, the allowance is available for the entire portfolio as needed.

The allowance for loan losses increased from \$7,154,000 at December 31, 2011 to \$7,745,000 at March 31, 2012. At March 31, 2012 and December 31, 2011, the allowance for loan losses to total loans was 1.75% and 1.64%, respectively.

Table of Contents

The provision for loan losses totaled \$600,000 for the three months ended March 31, 2012 and 2011. The amount of the provision was the result of several factors, including but not limited to, a ratio of nonperforming loans to total loans of 2.55% at March 31, 2012 and a ratio of the allowance for loan losses to nonperforming loans of 68.49% at March 31, 2012. Nonperforming loans decreased to \$11,308,000 at March 31, 2012 from \$12,900,000 at March 31, 2011 due to primarily to a partial charge-off of \$1,500,000 during the second quarter of 2011. The nonperforming loan portfolio is centered on several loans that are either in a secured position and have sureties with a strong underlying financial position or have a specific allocation for any impairment recorded within the allowance for loan losses. Internal loan review and analysis and the continued uncertainty surrounding the economy, coupled with the ratios noted previously, dictated the level of provision for loan losses for the three month period despite the decrease in nonperforming loans.

The following is a table showing total nonperforming loans as of:

(In Thousands)	Total Nonperforming Loans		
	Nonaccrual	90 Days Past Due	Total
March 31, 2012	\$ 11,307	\$ 1	\$ 11,308
December 31, 2011	11,625	384	12,009
September 30, 2011	11,885	2,459	14,344
June 30, 2011	10,911		10,911
March 31, 2011	12,797	103	12,900

**Non-interest Income**

Total non-interest income for the three months ended March 31, 2012 compared to the same period in 2011 increased \$818,000 to \$2,763,000. Excluding net securities gains, non-interest income for the three months ended March 31, 2012 would have increased \$354,000 compared to the 2011 period. Deposit service charges decreased due to a change in the overdraft program that allows for a de minimus overdraft prior to any fees being charged. Bank owned life insurance income increased due to a gain on death benefit of \$109,000. Gain on sale of loans decreased primarily due to a shift in product mix. Other income increased as debit and credit card related income continues to build as debit cards continue to gain in popularity, while an increasing number of merchants utilize our merchant card services.

Insurance and brokerage commissions for the three months ended March 31, 2012 increased due to continued efforts to add sales representatives. Management of The M Group continues to pursue new and build upon current relationships. The sales call program continues to expand to other financial institutions, which results in additional revenue for The M Group if an additional sales outlet is added. However, the addition of a sales outlet for The M Group can take up to a year or more to be completed.

Non-interest income composition for the three months ended March 31, 2012 and 2011 was as follows:

(In Thousands)	March 31, 2012		For the Three Months Ended March 31, 2011		Change	
	Amount	% Total	Amount	% Total	Amount	%
Deposit service charges	\$ 447	16.18%	\$ 503	25.85%	\$ (56)	(11.13)%
Securities gains, net	589	21.32	125	6.43	464	371.20

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Bank owned life insurance	268	9.70	174	8.95	94	54.02
Gain on sale of loans	183	6.62	249	12.80	(66)	(26.51)
Insurance commissions	442	16.00	209	10.75	233	111.48
Brokerage commissions	212	7.67	274	14.09	(62)	(22.63)
Other	622	22.51	411	21.13	211	51.34
Total non-interest income	\$ 2,763	100.00%	\$ 1,945	100.00%	\$ 818	42.06%

**Non-interest Expense**

Total non-interest expense increased \$476,000 for the three months ended March 31, 2012 compared to the same period of 2011. The increase in salaries and employee benefits was attributable to increases in health insurance, salaries, and bonus accrual. FDIC deposit insurance decreased due to a change in the assessment base from a deposit to asset based calculation. Other expenses increased primarily due to expenses associated with the opening of a new branch in Danville, Montour County with emphasis on marketing costs.

Non-interest expense composition for the three months ended March 31, 2012 and 2011 was as follows:

Table of Contents

(In Thousands)	March 31, 2012		For the Three Months Ended March 31, 2011		Change	
	Amount	% Total	Amount	% Total	Amount	%
Salaries and employee benefits	\$ 3,017	55.22%	\$ 2,632	52.76%	\$ 385	14.63%
Occupancy, net	328	6.00	348	6.98	(20)	(5.75)
Furniture and equipment	346	6.33	308	6.17	38	12.34
Pennsylvania shares tax	169	3.09	172	3.45	(3)	(1.74)
Amortization of investment in limited partnerships	165	3.02	166	3.33	(1)	(0.60)
FDIC deposit insurance	123	2.25	187	3.75	(64)	(34.22)
Other	1,316	24.09	1,175	23.56	141	12.00
Total non-interest expense	\$ 5,464	100.00%	\$ 4,988	100.00%	\$ 476	9.54%

**Provision for Income Taxes**

Income taxes increased \$179,000 for the three months ended March 31, 2012 compared to the same periods of 2011. The primary cause of the increase in tax expense for the three month periods ended March 31, 2012 compared to 2011 is the impact of increased net interest income in addition to an increase in net security gains. Excluding the impact of the net securities gains, the effective tax rate for the three months ended March 31, 2012 was 12.70% compared to 14.18% for the same period of 2011. The Company currently is in a deferred tax asset position due to the low income housing tax credits earned both currently and previously. Management has reviewed the deferred tax asset and has determined that the asset will be utilized within the appropriate carry forward period and therefore does not require a valuation allowance.

**ASSET/LIABILITY MANAGEMENT****Cash and Cash Equivalents**

Cash and cash equivalents increased \$9,546,000 from \$13,885,000 at December 31, 2011 to \$23,431,000 at March 31, 2012 primarily as a result of the following activities during the three months ended March 31, 2012:

**Loans Held for Sale**

Activity regarding loans held for sale resulted in loan originations trailing sale proceeds, less \$183,000 in realized gains, by \$1,722,000 for the three months ended March 31, 2012.

**Loans**

## Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Gross loans increased \$7,618,000 since December 31, 2011 due primarily to an increase of residential real estate loans.

The allocation of the loan portfolio, by category, as of March 31, 2012 and December 31, 2011 is presented below:

(In Thousands)	March 31, 2012		December 31, 2011		Change	
	Amount	% Total	Amount	% Total	Amount	%
Commercial and agricultural	\$ 53,550	12.07%	\$ 53,129	12.19%	\$ 421	0.79%
Real estate mortgage:						
Residential	186,369	42.02	179,383	41.15	6,986	3.89
Commercial	164,204	37.02	164,288	37.68	(84)	(0.05)
Construction	30,180	6.80	29,457	6.76	723	2.45
Installment loans to individuals	10,834	2.44	11,297	2.59	(463)	(4.10)
Less: Net deferred loan fees and discounts	(1,560)	(0.35)	(1,595)	(0.37)	35	(2.19)
Gross loans	\$ 443,577	100.00%	\$ 435,959	100.00%	\$ 7,618	1.75%

### Investments

The fair value of the investment securities portfolio at March 31, 2012 increased \$14,681,000 since December 31, 2011. The change is primarily due to purchases of short-term other debt securities coupled with a net unrealized gain of \$8,836,000 at March 31, 2012 compared to an unrealized gain of \$4,415,000 at December 31, 2011. The unrealized losses within the debt securities portfolio are the result of market activity, not credit issues/ratings, as approximately 93% of the debt securities portfolio on an amortized cost basis is currently rated A or higher by either S&P or Moody's.

The Company considers various factors, which include examples from applicable accounting guidance, when analyzing the available for sale portfolio for possible other than temporary impairment. The Company primarily considers the following factors in its analysis: length of time and severity of the market value being less than carrying value; reduction of dividend paid (equities);

Table of Contents

continued payment of dividend/interest, credit rating, and financial condition of an issuer; intent and ability to hold until anticipated recovery (which may be maturity); and general outlook for the economy, specific industry, and entity in question.

The bond portion of the portfolio review is conducted with emphases on several factors. Continued payment of principal and interest is given primary importance with credit rating and financial condition of the issuer following as the next most important. Credit ratings were reviewed with the ratings of the bonds being satisfactory. Bonds that were not currently rated were discussed with a third party and/or underwent an internal financial review. The Company also monitors whether each of the investments incurred a decline in market value from carrying value of at least 20% for twelve consecutive months or a similar decline of at least 50% for three consecutive months. Each bond is reviewed to determine whether it is a general obligation bond, which is backed by the credit and taxing power of the issuing jurisdiction, or revenue bond, which is only payable from specified revenues. Based on the review undertaken by the Company, the Company determined that the decline in value of the various bond holdings were temporary and were the result of the general market downturns and interest rate/yield curve changes, not credit issues. The fact that almost all of such bonds are general obligation bonds further solidified the Company's determination that the decline in the value of these bond holdings is temporary.

The fair value of the equity portfolio continues to fluctuate as the economic turbulence both domestic and global continues to impact financial sector stock pricing. The amortized cost of the equity securities portfolio has decreased \$640,000 to \$12,050,000 at March 31, 2012 from \$12,690,000 at December 31, 2011 as the Company sold certain holdings within the portfolio. These holdings were sold due to the determination that their value was fully measured and as part of a strategy to shift the portfolio from a reliance on financial institution securities to a portfolio containing a greater amount of sector and geographic diversity as seen in the growth of non-financial institution holdings.

The equity portion of the portfolio is reviewed for possible other than temporary impairment in a similar manner to the bond portfolio with greater emphasis placed on the length of time the market value has been less than the carrying value and financial sector outlook. The Company also reviews dividend payment activities and, in the case of financial institutions, whether or not such issuer was participating in the TARP Capital Purchase Program. The starting point for the equity analysis is the length and severity of a market price decline. The Company monitors two primary measures: 20% decline in market value from carrying value for twelve consecutive months and 50% decline for three consecutive months.

The distribution of credit ratings by amortized cost and fair values for the debt security portfolio at March 31, 2012 follows:

(In Thousands)	A- to AAA		B- to BBB+		C to CCC+		Not Rated		Total	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for sale (AFS)										
U.S. Government and agency securities	\$ 21,801	\$ 23,499	\$	\$	\$	\$	\$	\$	\$ 21,801	\$ 23,499
State and political securities	160,213	167,360	7,011	6,414			8,697	8,397	175,921	182,171
Other debt securities	64,574	64,171	600	601			996	894	66,170	65,666
Total debt securities AFS	\$ 246,588	\$ 255,030	\$ 7,611	\$ 7,015	\$	\$	\$ 9,693	\$ 9,291	\$ 263,892	\$ 271,336
Held to maturity (HTM)										



Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Other debt securities	\$	55	\$	55	\$	\$	\$	\$	\$	\$	55	\$	55
Total debt securities HTM	\$	55	\$	55	\$	\$	\$	\$	\$	\$	55	\$	55

**Financing Activities**

**Deposits**

Total deposits increased \$39,878,000 from December 31, 2011 to March 31, 2012. The growth was led by an increase in money market and NOW accounts from December 31, 2011 to March 31, 2012 of 14.07% and 6.97%, respectively. The increase in core deposits (deposits less time deposits) has provided relationship driven funding for the loan and investment portfolios, while also reducing the utilization of FHLB borrowings. The increase in deposits is the result of our focus on building relationships with money market accounts being the key building block. Time deposits have increased as efforts to slowly lengthen the portfolio have begun; however, time deposits remain as complementary accounts to core deposits. To facilitate this strategy we are actively working single product time deposit relationships to create a solid relationship through the addition of other products to the customer's portfolio.

Deposit balances and their changes for the periods being discussed follow:

Table of Contents

(In Thousands)	March 31, 2012		December 31, 2011		Change	
	Amount	% Total	Amount	% Total	Amount	%
Demand deposits	\$ 116,271	18.71%	\$ 111,354	19.14%	\$ 4,917	4.42%
NOW accounts	108,904	17.52	101,808	17.50	7,096	6.97
Money market deposits	141,830	22.82	124,335	21.38	17,495	14.07
Savings deposits	77,253	12.43	71,646	12.32	5,607	7.83
Time deposits	177,284	28.52	172,521	29.66	4,763	2.76
Total deposits	\$ 621,542	100.00%	\$ 581,664	100.00%	\$ 39,878	6.86%

**Borrowed Funds**

Total borrowed funds decreased 16.32% or \$14,830,000 to \$76,046,000 at March 31, 2012 compared to \$90,876,000 at December 31, 2011. The decrease in borrowed funds is primarily the result of growth in deposits as the deposit growth provided loan portfolio funding and funds to reduce the level of total borrowings. FHLB repurchase agreements were utilized as their structure allowed for a reduction in interest expense, while providing the ability to reduce the borrowings at our discretion as deposit levels increased.

(In Thousands)	March 31, 2012		December 31, 2011		Change	
	Amount	% Total	Amount	% Total	Amount	%
Short-term borrowings:						
FHLB repurchase agreements	\$		\$ 16,445	18.10%	\$ (16,445)	(100.00)%
Securities sold under agreement to repurchase	14,768	19.42	13,153	14.47	1,615	12.28
Total short-term borrowings	14,768	19.42	29,598	32.57	(14,830)	(50.10)
Long-term borrowings,						
FHLB	61,278	80.58	61,278	67.43		
Total borrowed funds	\$ 76,046	100.00%	\$ 90,876	100.00%	\$ (14,830)	(16.32)%

**Capital**

The adequacy of the Company's capital is reviewed on an ongoing basis with reference to the size, composition, and quality of the Company's resources and regulatory guidelines. Management seeks to maintain a level of capital sufficient to support existing assets and anticipated asset growth, maintain favorable access to capital markets, and preserve high quality credit ratings.

Bank holding companies are required to comply with the Federal Reserve Board's risk-based capital guidelines. The risk-based capital rules are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and bank holding companies and to minimize disincentives for holding liquid assets. Specifically, each is required to maintain certain minimum dollar amounts and ratios of total risk-based, tier I risk-based, and tier I leverage capital. In addition to the capital requirements, the Federal Deposit Insurance Corporation Improvements Act (FDICIA) established five capital categories ranging from well capitalized to critically undercapitalized. To be classified as well capitalized, total risk-based, tier I risk-based, and tier I leverage capital ratios must be at least 10%, 6%, and 5%, respectively.

Edgar Filing: PENNS WOODS BANCORP INC - Form 10-Q

Capital ratios as of March 31, 2012 and December 31, 2011 were as follows:

(In Thousands)	March 31, 2012		December 31, 2011	
	Amount	Ratio	Amount	Ratio
<b>Total Capital (to</b>				
<b>Risk-weighted Assets)</b>				
Actual	\$ 80,200	15.11%	\$ 77,863	15.27%
For Capital Adequacy Purposes	42,458	8.00	40,796	8.00
To Be Well Capitalized	53,073	10.00	50,995	10.00
<b>Tier I Capital (to</b>				
<b>Risk-weighted Assets)</b>				
Actual	\$ 73,002	13.76%	\$ 71,064	13.94%
For Capital Adequacy Purposes	21,229	4.00	20,398	4.00
To Be Well Capitalized	31,844	6.00	30,597	6.00
<b>Tier I Capital (to Average</b>				
<b>Assets)</b>				
Actual	\$ 73,002	9.66%	\$ 71,064	9.57%
For Capital Adequacy Purposes	30,217	4.00	29,688	4.00
To Be Well Capitalized	37,771	5.00	37,110	5.00

Table of Contents

**Liquidity; Interest Rate Sensitivity and Market Risk**

The asset/liability committee addresses the liquidity needs of the Company to ensure that sufficient funds are available to meet credit demands and deposit withdrawals as well as to the placement of available funds in the investment portfolio. In assessing liquidity requirements, equal consideration is given to the current position as well as the future outlook.

The following liquidity measures are monitored for compliance and were within the limits cited at March 31, 2012:

1. Net Loans to Total Assets, 85% maximum
2. Net Loans to Total Deposits, 100% maximum
3. Cumulative 90 day Maturity GAP %, +/- 20% maximum
4. Cumulative 1 Year Maturity GAP %, +/- 25% maximum

Fundamental objectives of the Company's asset/liability management process are to maintain adequate liquidity while minimizing interest rate risk. The maintenance of adequate liquidity provides the Company with the ability to meet its financial obligations to depositors, loan customers, and shareholders. Additionally, it provides funds for normal operating expenditures and business opportunities as they arise. The objective of interest rate sensitivity management is to increase net interest income by managing interest sensitive assets and liabilities in such a way that they can be repriced in response to changes in market interest rates.

The Bank, like other financial institutions, must have sufficient funds available to meet its liquidity needs for deposit withdrawals, loan commitments and originations, and expenses. In order to control cash flow, the Bank estimates future cash flows from deposits, loan payments, and investment security payments. The primary sources of funds are deposits, principal and interest payments on loans and investment securities, FHLB borrowings, and brokered deposits. Management believes the Bank has adequate resources to meet its normal funding requirements.

Management monitors the Company's liquidity on both a long and short-term basis, thereby providing management necessary information to react to current balance sheet trends. Cash flow needs are assessed and sources of funds are determined. Funding strategies consider both customer needs and economical cost. Both short and long-term funding needs are addressed by maturities and sales of available for sale investment securities, loan repayments and maturities, and liquidating money market investments such as federal funds sold. The use of these resources, in conjunction with access to credit provides core funding to satisfy depositor, borrower, and creditor needs.

Management monitors and determines the desirable level of liquidity. Consideration is given to loan demand, investment opportunities, deposit pricing and growth potential, as well as the current cost of borrowing funds. As of March 31, 2012, the Company has a current borrowing capacity at the FHLB of \$209,690,000. In addition to this credit arrangement, the Company has additional lines of credit with correspondent banks of \$27,317,000. Management believes it has sufficient liquidity to satisfy estimated short-term and long-term funding needs. FHLB borrowings totaled \$61,278,000 as of March 31, 2012.

Interest rate sensitivity, which is closely related to liquidity management, is a function of the repricing characteristics of the Company's portfolio of assets and liabilities. Asset/liability management strives to match maturities and rates between loan and investment security assets with the deposit liabilities and borrowings that fund them. Successful asset/liability management results in a balance sheet structure which can cope effectively with market rate fluctuations. The matching process is affected by segmenting both assets and liabilities into future time periods (usually 12 months, or less) based upon when repricing can be effected. Repriceable assets are subtracted from repriceable liabilities, for a specific time period to determine the gap, or difference. Once known, the gap is managed based on predictions about future market interest rates. Intentional mismatching, or gapping, can enhance net interest income if market rates move as predicted. However, if market rates behave in a manner contrary to predictions, net interest income will suffer. Gaps, therefore, contain an element of risk and must be prudently managed. In addition to gap management, the Company has an asset/liability management policy which incorporates a market value at risk calculation which is used to determine the effects of interest rate movements on shareholders' equity and a simulation analysis to monitor the effects of interest rate changes on the Company's balance sheet.

The Company currently maintains a GAP position of being liability sensitive. The Company has strategically taken this position as it has decreased the duration of the time deposit portfolio, while continuing to maintain a primarily fixed rate earning asset portfolio with a duration greater than the liabilities utilized to fund earning assets. Lengthening of the liability portfolio coupled with the addition of limited short-term assets is being undertaken. These actions are expected to reduce, but not eliminate, the liability sensitive structure of the balance sheet.

A market value at risk calculation is utilized to monitor the effects of interest rate changes on the Company's balance sheet and more specifically shareholders' equity. The Company does not manage the balance sheet structure in order to maintain compliance with this calculation. The calculation serves as a guideline with greater emphases placed on interest rate sensitivity. Changes to calculation results from period to period are reviewed as changes in results could be a signal of future events. As of the most recent analysis, the results of the market value at risk calculation were outside of established guidelines due to the strategic direction being taken.

Table of Contents**Interest Rate Sensitivity**

In this analysis the Company examines the result of various changes in market interest rates in 100 basis point increments and their effect on net interest income. It is assumed that the change is instantaneous and that all rates move in a parallel manner. Assumptions are also made concerning prepayment speeds on mortgage loans and mortgage securities.

The following is a rate shock forecast for the twelve month period ending March 31, 2013 assuming a static balance sheet as of March 31, 2012.

(In Thousands)	Parallel Rate Shock in Basis Points						
	-200	-100	Static	+100	+200	+300	+400
Net interest income	\$ 27,245	\$ 27,983	\$ 28,461	\$ 28,754	\$ 29,053	\$ 29,247	\$ 29,205
Change from static	(1,216)	(478)		293	592	786	744
Percent change from static	-4.27%	-1.68%		1.03%	2.08%	2.76%	2.61%

The model utilized to create the report presented above makes various estimates at each level of interest rate change regarding cash flow from principal repayment on loans and mortgage-backed securities and/or call activity on investment securities. Actual results could differ significantly from these estimates which would result in significant differences in the calculated projected change. In addition, the limits stated above do not necessarily represent the level of change under which management would undertake specific measures to realign its portfolio in order to reduce the projected level of change. Generally, management believes the Company is well positioned to respond expeditiously when the market interest rate outlook changes.

**Inflation**

The asset and liability structure of a financial institution is primarily monetary in nature. Therefore, interest rates rather than inflation have a more significant impact on the Company's performance. Interest rates are not always affected in the same direction or magnitude as prices of other goods and services, but are reflective of fiscal policy initiatives or economic factors which are not measured by a price index.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Market risk for the Company is comprised primarily of interest rate risk exposure and liquidity risk. Interest rate risk and liquidity risk management is performed at the Bank level as well as the Company level. The Company's interest rate sensitivity is monitored by management through selected interest rate risk measures produced by an independent third party. There have been no substantial changes in the Company's gap analyses or simulation analyses compared to the information provided in the Annual Report on Form 10-K for the period ended December 31, 2011. Additional information and details are provided in the Liquidity and Interest Rate Sensitivity section of Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Generally, management believes the Company is well positioned to respond in a timely manner when the market interest rate outlook changes.

**Item 4. Controls and Procedures**

An analysis was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of March 31, 2012. There were no changes in the Company's internal control over financial reporting that occurred during the quarter ended March 31, 2012, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Table of Contents**Part II. OTHER INFORMATION****Item 1. Legal Proceedings**

None.

**Item 1A. Risk Factors**

There are no material changes to the risk factors set forth in Part I, Item 1A, Risk Factors, of the Company's Annual Report on Form 10-K for the year ended December 31, 2011. Please refer to that section for disclosures regarding the risks and uncertainties related to the Company's business.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

<b>Period</b>	<b>Total Number of Shares (or Units) Purchased</b>	<b>Average Price Paid per Share (or Unit) Purchased</b>	<b>Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs</b>
Month #1 (January 1 - January 31, 2012)		\$		76,776
Month #2 (February 1 - February 29, 2012)				76,776
Month #3 (March 1 - March 31, 2012)				76,776

On April 24, 2012, the Board of Directors extended the previously approved authorization to repurchase up to 197,000 shares, or approximately 5%, of the outstanding shares of the Company for an additional year to April 30, 2013. To date, there have been 120,224 shares repurchased under this plan.

On April 25, 2012, the Shareholders of the Corporation authorized an amendment to the Articles of Incorporation to increase the number of shares of common stock from 10,000,000 to 15,000,000 and authorized 3,000,000 shares of preferred stock.



**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

- 3(i) Articles of Incorporation of the Registrant, as presently in effect.
- 3(ii) Bylaws of the Registrant as presently in effect (incorporated by reference to Exhibit 3(ii) of the Registrant's Current Report on Form 8-K filed June 17, 2005).
- 10(i) Employment Agreement, dated October 25, 2010, between Robert J. Glunk, Penns Woods Bancorp, Inc. and Jersey Shore State Bank.
- 31(i) Rule 13a-14(a)/Rule 15d-14(a) Certification of Chief Executive Officer.
- 31(ii) Rule 13a-14(a)/Rule 15d-14(a) Certification of Chief Financial Officer.
- 32(i) Section 1350 Certification of Chief Executive Officer.
- 32(ii) Section 1350 Certification of Chief Financial Officer.
- 101 Interactive data file containing the following financial statements formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Balance Sheet at March 31, 2012 and December 31, 2011; (ii) the Consolidated Statement of Income for the three months ended March 31, 2012 and 2011; (iii) the Consolidated Statements of Shareholders' Equity for the three months ended March 31, 2012 and 2011; (iv) Consolidated Statement of Comprehensive Income for the three months ended March 31, 2012 and 2011; (v) the Consolidated Statement of Cash Flows for the three months ended March 31, 2012 and 2011; and, (vi) the Notes to Consolidated Financial Statements, tagged as blocks of text. As provided in Rule 406T of Regulation S-T, this interactive data file shall not be deemed to be filed for purposes of Section 18 of the Securities Exchange Act of 1934, and shall not be deemed filed or part of any registration statement or prospectus for purposes of Section 11 or 12 under the Securities Act of 1933, or otherwise subject to liability under those sections.

Table of Contents

**SIGNATURES**

Pursuant to the requirements 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.

PENNS WOODS BANCORP, INC.  
(Registrant)

Date: May 9, 2012

/s/ Richard A. Grafmyre  
Richard A. Grafmyre, President and Chief Executive Officer  
(Principal Executive Officer)

Date: May 9, 2012

/s/ Brian L. Knepp  
Brian L. Knepp, Chief Financial Officer  
(Principal Financial Officer and Principal Accounting  
Officer)

Table of Contents

**EXHIBIT INDEX**

Exhibit 3(i)	Articles of Incorporation of the Registrant, as presently in effect.
Exhibit 10(i)	Employment Agreement, dated October 25, 2010, between Robert J. Glunk, Penns Woods Bancorp, Inc. and Jersey Shore State Bank.
Exhibit 31(i)	Rule 13a-14(a)/Rule 15d-14(a) Certification of Chief Executive Officer
Exhibit 31(ii)	Rule 13a-14(a)/Rule 15d-14(a) Certification of Chief Financial Officer
Exhibit 32(i)	Section 1350 Certification of Chief Executive Officer
Exhibit 32(ii)	Section 1350 Certification of Chief Financial Officer
Exhibit 101	Interactive data file containing the following financial statements formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Balance Sheet at March 31, 2012 and December 31, 2011; (ii) the Consolidated Statement of Income for the three months ended March 31, 2012 and 2011; (iii) the Consolidated Statements of Shareholders' Equity for the three months ended March 31, 2012 and 2011; (iv) Consolidated Statement of Comprehensive Income for the three months ended March 31, 2012 and 2011; (v) the Consolidated Statement of Cash Flows for the three months ended March 31, 2012 and 2011; and, (vi) the Notes to Consolidated Financial Statements, tagged as blocks of text. As provided in Rule 406T of Regulation S-T, this interactive data file shall not be deemed to be filed for purposes of Section 18 of the Securities Exchange Act of 1934, and shall not be deemed filed or part of any registration statement or prospectus for purposes of Section 11 or 12 under the Securities Act of 1933, or otherwise subject to liability under those sections.