



PORTAGE BANCSHARES, INC.
2015 ANNUAL REPORT



**BUILDING ON FOUNDATIONS,
VALUES AND RELATIONSHIPS**

To Our Fellow Shareholders,

On behalf of the Board of Directors and Management, I am extremely pleased to share the financial results and successful performance of Portage Bancshares, Inc. (the “Company”), parent company of Portage Community Bank (the “Bank”), for the year ended December 31, 2015. Our continued emphasis on our vision of “Neighbors Serving Neighbors,” along with local ownership, local management, and, most importantly, local decisions have contributed new records for achievement for the Company in 2015.

Following a record financial year in 2014, I am pleased to report record net income of \$2,628,891 for 2015, which is up 18.49% from net income of \$2,218,669 for 2014. Because of our strong capital position, the Board of Directors increased the cash dividend to \$0.85 per share in 2015 from \$0.80 per share in 2014 – a 6.25% increase. Basic earnings per share increased to \$5.67 for 2015 as compared to \$5.02 for 2014, resulting in an earnings improvement of 12.95% on a per share basis. We are extremely proud of these outstanding financial results.

We continue to follow a multifaceted long-term plan to grow the Company’s value through efficient operations, driving increased productivity, and the continual development, enhancement, and offering of dynamic banking solutions and resources to meet the needs of our customers. In 2015, we made investments in operations and technology to support a larger organization with more customers and a greater diversity of products. We completed the expansion of our Main Office location and began construction on our new Mortgage Division facility that replaces our previous facility next to the Kent Office on South Water Street. The improvements were considered necessary for our continued growth opportunities. Also, in order to upgrade an aging software and hardware server infrastructure, the Company completed a migration to virtualization for our server environment that included a more robust and powerful server system with the flexibility needed to respond to growth, business continuity, and disaster recovery. Additionally, we continue to keep pace with the latest electronic and mobile banking technology to serve our customers. This is consistent with our commitment to providing superior service.

In addition, we are excited to share the following other 2015 highlights:

- The Portage Community Financial Services Division continued to excel by growing assets under management to \$59.1 million in 2015, up \$8.2 million or 16.11% from 2014.
- The Mortgage Division experienced their most successful year ever with \$694,305 in secondary market fees; which is just another example of our Bank helping customers purchase the homes they desire.
- We completed a very successful fifth Super Stock Subscription offering generating 10 new shareholders and \$509,748 in additional capital.
- For the 15th consecutive quarter, Portage Community Bank received a Five-Star “Superior” rating from Bauer Financial, Inc., the nation’s leading bank rating and research firm. The Five-Star “Superior” rating is the highest rating achievable and indicates the institution is one of the strongest banks in the nation.
- We continue to achieve very strong results through our outsourced, third party internal and external bank compliance, audit, and review service providers.

The successful performance of the Company would not have been possible without the efforts of our committed Board or Directors, dedicated management team, and loyal and knowledgeable staff. We believe as we move forward into 2016, we are well positioned to continue to meet the high standards we have set and to exceed your expectations. Most of all, thank you to our customers and shareholders for your continued support and having the confidence in us to continually make our “Company” successful.

Sincerely,



Richard J. Coe
Chief Executive Officer

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INDEPENDENT AUDITORS REPORT

Board of Directors and Shareholders
Portage Bancshares, Inc.
Ravenna, Ohio

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Portage Bancshares, Inc. and subsidiary which comprise the consolidated balance sheet as of December 31, 2015 and 2014; the related consolidated statement of income, comprehensive income, changes in stockholders' equity, and cash flows for the years then ended; and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Portage Bancshares, Inc. and subsidiary as of December 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

S.R. Snodgrass, P.C.

Wexford, Pennsylvania

March 29, 2016

PORTAGE BANCSHARES, INC.
CONSOLIDATED BALANCE SHEET

December 31,

	2015	2014
Assets		
Cash and due from banks	\$ 14,985,544	\$ 6,448,981
Interest-bearing deposits in other financial institutions	1,259,396	828,488
Federal funds sold	1,000	100,000
Cash and cash equivalents	16,245,940	7,377,469
Investment securities available for sale	52,694,749	48,743,337
Loans held for sale	755,267	910,063
Loans	217,313,409	212,443,338
Less allowance for loan losses	2,856,417	3,070,857
Net loans	214,456,992	209,372,481
Regulatory stock	1,240,250	1,240,250
Premises and equipment, net	4,470,964	3,937,666
Bank-owned life insurance	6,630,830	6,461,484
Accrued interest receivable	752,680	735,879
Other assets	1,992,466	1,760,532
Total Assets	\$ 299,240,138	\$ 280,539,161
Liabilities		
Deposits		
Non-interest-bearing	\$ 35,924,405	\$ 29,483,184
Interest-bearing demand	25,390,817	21,784,953
Savings	109,519,418	103,746,176
Time	73,279,287	72,953,491
Total deposits	244,113,927	227,967,804
Federal Home Loan Bank advances	18,068,532	19,359,945
Subordinated debentures	2,450,000	2,450,000
Accrued interest payable and other liabilities	2,650,083	2,297,126
Total Liabilities	267,282,542	252,074,875
Stockholders' Equity		
Common stock, no par value; 800,000 shares authorized, 501,605 and 478,129 shares issued; 477,848 and 453,546 outstanding	18,182,189	16,908,537
Retained earnings	15,115,006	12,879,911
Accumulated other comprehensive income	463,053	473,980
Treasury stock, at cost (23,757 and 24,583 shares)	(1,802,652)	(1,798,142)
Total Stockholders' Equity	31,957,596	28,464,286
Total Liabilities and Stockholders' Equity	\$ 299,240,138	\$ 280,539,161

See accompanying notes to consolidated financial statements.

PORTAGE BANCSHARES, INC.
CONSOLIDATED STATEMENT OF INCOME

Year Ended December 31,

	2015	2014
Interest and Dividend Income		
Interest and fees on loans	\$ 9,966,345	\$ 9,552,203
Federal funds sold and other interest income	31,945	24,052
Investment securities:		
Taxable	464,625	566,297
Exempt from federal income tax	585,785	530,281
Other dividend income	56,883	56,883
Total interest and dividend income	11,105,583	10,729,716
Interest Expense		
Deposits	1,157,107	1,105,672
Federal Home Loan Bank advances	426,593	513,604
Subordinated debentures	82,178	80,558
Total interest expense	1,665,878	1,699,834
Net Interest Income	9,439,705	9,029,882
Provision for loan losses	—	355,000
Net Interest Income After Provision For Loan Losses	9,439,705	8,674,882
Noninterest Income		
Service charges on deposit accounts	144,434	165,108
Investment securities gains (losses), net	1,797	(1,667)
Secondary market fees	693,905	445,090
Earnings on bank-owned life insurance	169,346	176,736
Investment banking fees and commissions	248,542	229,698
Gain from other real estate owned	75,939	46,172
Other income	308,265	249,755
Total noninterest income	1,642,228	1,310,892
Noninterest Expense		
Salaries and employee benefits	4,167,400	3,897,985
Net occupancy and equipment expenses	390,657	396,074
Data processing	331,716	307,941
Professional fees	284,369	262,133
Marketing and business development	300,092	265,830
Franchise tax expense	192,045	172,104
Federal deposit insurance	182,409	191,262
Other expense	1,647,602	1,487,306
Total noninterest expense	7,496,290	6,980,635
Income before income taxes	3,585,643	3,005,139
Income taxes	956,752	786,470
Net Income	\$ 2,628,891	\$ 2,218,669
Earnings Per Share		
Basic	\$ 5.67	\$ 5.02
Diluted	5.42	4.73

See accompanying notes to consolidated financial statements.

PORTAGE BANCSHARES, INC.
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year Ended December 31,

	2015	2014
Net income	\$ 2,628,891	\$ 2,218,669
Other comprehensive income (loss):		
Unrealized holding gains (losses) on investment securities available for sale	(14,759)	1,208,868
Tax effect	5,018	(411,015)
Reclassification of investment securities (gains) losses recognized in net income	(1,797)	1,667
Tax effect	611	(567)
Total other comprehensive (loss) income	(10,927)	798,953
Comprehensive income	\$ 2,617,964	\$ 3,017,622

See accompanying notes to consolidated financial statements.

PORTAGE BANCSHARES, INC.
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity
Balance, December 31, 2013	\$ 15,899,100	\$ 11,015,518	\$ (324,973)	\$ (1,735,192)	\$ 24,854,453
Purchase of 7,357 shares of treasury stock				(562,002)	(562,002)
Stock-based compensation expense	15,301				15,301
Exercise of 16,768 shares of stock options	694,198				694,198
Tax benefits from exercise of stock options	211,113				211,113
Issuance of 7,350 shares of common stock for subscription and share purchase agreement	88,825			499,052	587,877
Cash dividends declared (\$0.80 per share)		(354,276)			(354,276)
Net income		2,218,669			2,218,669
Other comprehensive income, net			798,953		798,953
Balance, December 31, 2014	16,908,537	12,879,911	473,980	(1,798,142)	28,464,286
Purchase of 5,139 shares of treasury stock				(418,993)	(418,993)
Stock-based compensation expense	15,574				15,574
Exercise of 23,476 shares of stock options	1,031,485				1,031,485
Tax benefits from exercise of stock options	131,328				131,328
Issuance of 5,965 shares of common stock for subscription and share purchase agreement	95,265			414,483	509,748
Cash dividends declared (\$0.85 per share)		(393,796)			(393,796)
Net income		2,628,891			2,628,891
Other comprehensive loss, net			(10,927)		(10,927)
Balance, December 31, 2015	\$ 18,182,189	\$ 15,115,006	\$ 463,053	\$ (1,802,652)	\$ 31,957,596

See accompanying notes to consolidated financial statements.

PORTAGE BANCSHARES, INC.
CONSOLIDATED STATEMENT OF CASH FLOWS

Year Ended December 31,

	2015	2014
Operating Activities		
Net income	\$ 2,628,891	\$ 2,218,669
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	—	355,000
Depreciation	146,843	140,246
Net amortization of investment securities	489,272	625,685
Investment securities (gains) losses, net	(1,797)	1,667
Secondary market income	(693,905)	(445,090)
Originations of loans held for sale	(23,376,903)	(15,817,071)
Proceeds from sale of loans held for sale	23,531,699	15,584,100
Gain from other real estate owned	(75,939)	(46,172)
Stock-based compensation expense	15,574	15,301
Earnings on bank-owned life insurance	(169,346)	(176,736)
Deferred income taxes	(11,734)	18,247
Amortization of deferred loan fees, net	19,759	12,667
Tax benefit from exercise of stock options	(131,328)	(211,113)
Amortization of Federal Home Loan Bank restructuring fee	76,958	147,785
Other, net	659,367	694,165
Net cash provided by operating activities	3,107,411	3,117,350
Investing Activities		
Investment securities available for sale:		
Proceeds from repayments and maturities	7,517,716	8,111,398
Proceeds from sales	1,472,601	7,173,737
Purchases	(13,445,760)	(9,185,401)
Increase in loans, net	(5,215,305)	(18,824,556)
Purchase of premises and equipment	(680,141)	(101,393)
Proceeds from sale of other real estate owned	474,425	186,232
Net cash used for investing activities	(9,876,464)	(12,639,983)
Financing Activities		
Increase in deposits, net	16,146,123	1,317,104
Proceeds from Federal Home Loan Bank advances	4,500,000	6,000,000
Repayment of Federal Home Loan Bank advances	(5,868,371)	(2,556,230)
Purchases of treasury stock	(418,993)	(562,002)
Proceeds from the sale of treasury stock	509,748	587,877
Tax benefit from exercise of stock options	131,328	211,113
Proceeds from stock option exercises	1,031,485	694,198
Cash dividends paid	(393,796)	(354,276)
Net cash provided by financing activities	15,637,524	5,337,784
Increase (decrease) in cash and cash equivalents	8,868,471	(4,184,849)
Cash and Cash Equivalents at Beginning of Year	7,377,469	11,562,318
Cash and Cash Equivalents at End of Year	\$ 16,245,940	\$ 7,377,469

See accompanying notes to consolidated financial statements.

PORTAGE BANCSHARES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting and reporting policies applied in the presentation of the accompanying financial statements follows:

Nature of Operations and Basis of Presentation

Portage Bancshares, Inc. (the “Company”) is a bank holding company whose principal activity is the ownership and management of its wholly owned subsidiary, Portage Community Bank (the “Bank”). The Bank generates commercial, mortgage, and consumer loans and receives deposits from customers located primarily in Portage County in Ohio and the surrounding areas. The Bank is subject to regulations by the State of Ohio Division of Financial Institutions and the Company is subject to regulations by the Federal Reserve System through the Federal Reserve Bank of Cleveland.

The consolidated financial statements include the accounts of the Company and the Bank after elimination of all significant intercompany transactions and balances.

The accounting principles followed by the Company and the methods of applying these principles conform to U.S. generally accepted accounting principles and to general practice within the banking industry. Management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the balance sheet date and reported amounts of revenues and expenses for that period. Actual results could differ from those estimates.

Investment Securities

Currently, the Company’s investment securities portfolio is classified as available for sale. The portfolio serves principally as a source of liquidity and is carried at fair value with unrealized holding gains and losses for available for sale securities reported in other comprehensive income, net of tax, until realized. Debt securities are adjusted for amortization of premium and accretion of discount, which are computed using the interest method and recognized as adjustments of interest income. Realized security gains and losses are computed using the specific identification method. Interest and dividends on investment securities are recognized as income when earned.

Securities are periodically reviewed for other-than-temporary impairment based upon a number of factors, including, but not limited to, the length of time and extent to which the fair value has been less than cost, the financial condition of the underlying issuer, the ability of the issuer to meet contractual obligations, the likelihood of the security’s ability to recover any decline in its fair value, and whether or not the Company intends to sell the security or whether it’s more likely than not that the Company would be required to sell the security before its anticipated recovery in fair value. A decline in value that is considered to be other

than temporary is recorded as a loss within noninterest income in the Consolidated Statement of Income.

Common stock of the Federal Home Loan Bank (“FHLB”) and Federal Reserve Bank represents ownership in institutions which are wholly owned by other financial institutions.

The Bank is a member of the FHLB of Cincinnati 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 by management. 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 with 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. Management evaluated the stock and concluded that the stock was not impaired for the periods presented herein. Management 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 \$100 par value, and the resumption of dividends.

Loans Held for Sale

Loans held for sale are carried at the lower of cost or estimated fair value, as determined on an aggregate basis. Loans held for sale were \$755,267 and \$910,063 at December 31, 2015 and 2014, respectively.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, net of unearned interest, deferred loan fees and costs, and an allowance for loan losses.

Interest income is accrued on the interest method based upon the unpaid principal balance and includes amortization of net deferred loan fees and costs over the loan term. Interest income on mortgage and commercial loans is discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in process of collection. Past-due status is based on the contractual terms of the loan. Consumer loans are typically

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Loans (Continued)

charged off no later than 120 days past due. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal and interest is considered doubtful.

All interest accrued but not received for loans placed on nonaccrual is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably ensured.

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the collectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective, since it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific and general components. The specific component is related to impaired loans, which are commercial and commercial real estate loans for which it is probable that the Company will not be able to collect all amounts due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and commercial mortgage loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the loan's obtainable market price or the fair value of the collateral if the loan is collateral-dependent. The Company individually evaluates such loans for impairment and does not aggregate

loans by major risk classifications. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. A component is maintained to cover uncertainties that could affect management's estimate of probable losses. This component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

Large groups of smaller-balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer and residential mortgage loans for impairment disclosures, unless such loans are the subject of a restructuring agreement.

Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost, less accumulated depreciation. Depreciation is principally computed on the straight-line method over the estimated useful lives of the related assets, which range from 3 to 10 years for furniture, fixtures, and equipment and 25 to 50 years for building premises. Leasehold improvements are amortized over the shorter of their estimated useful lives or their respective lease terms, which range from 7 to 15 years. Expenditures for maintenance and repairs are expensed as incurred. Costs of major additions and improvements are capitalized.

Bank-Owned Life Insurance (BOLI)

The Company owns insurance on the lives of a certain group of key employees. The policies were purchased to help offset the increase in the costs of various fringe benefit plans including healthcare. The cash surrender value of these policies is included as an asset on the Consolidated Balance Sheet, and any increases in the cash surrender value are recorded as noninterest income on the Consolidated Statement of Income. In the event of the death of an insured individual under these policies, the Company would receive a death benefit, which would be recorded as non-interest income.

Other Real Estate Owned

Other real estate acquired through or in lieu of foreclosure is initially recorded at the lower of cost or fair value, less estimated costs to sell, and any loan balance in excess of fair value is charged to the allowance for loan losses. Subsequent valuations are periodically performed and write-downs are included in noninterest expense, as are gains or losses upon sale and expenses related to maintenance of the properties.

Advertising Costs

Advertising costs are expensed as incurred.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income Taxes

The Company and the Bank file a consolidated federal income tax return. Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

Benefit Plans

The 401(k) plan expense is the amount contributed and is determined by formula and by Board of Directors decision. Supplemental retirement expense allocates the benefits over the years of service. The director deferral plan expense is comprised of the annual amount of director fees deferred by participating directors and related interest earned.

Stock Options

During the years ended December 31, 2015 and 2014, the Company recorded \$15,574 and \$15,301 in compensation expenses on the Company's Consolidated Statement of Income. As of December 31, 2015 and 2014, there was \$29,616 and \$45,590 of unrecognized compensation cost related to unvested share-based compensation awards granted. That cost is expected to be recognized over the next three years.

The cash flows from the tax benefits resulting from tax deductions in excess of the compensation cost recognized for stock-based awards (excess tax benefits) are classified as financing cash flows. The Company recognized \$131,328 and \$211,113 of excess tax benefits included as a financing cash inflow for the years ended December 31, 2015 and 2014, in the Consolidated Statement of Cash Flows.

For purposes of calculating compensation expense, the Company estimated the fair values of stock options using the Black-Scholes option-pricing model. The model requires the use of subjective assumptions that can materially affect fair value estimates. The fair value of each option is amortized into compensation expense on a straight-line basis between the grant date for the option and each vesting date.

The fair value of each stock option granted was estimated using the following weighted-average assumptions:

Grant Year	Expected Dividend Yield	Risk-Free Interest Rate	Expected Volatility	Expected Life (in years)
2014	1.00%	2.23%	3.62%	7.00

The weighted-average fair value of each stock option granted for 2014 was \$6.57.

Earnings Per Share

The Company provides dual presentation of basic and diluted earnings per share. Basic earnings per share are calculated utilizing net income as reported in the numerator and average shares outstanding in the denominator. The computation of diluted earnings per share differs in that the dilutive effects of any stock options are adjusted in the denominator.

Basic weighted-average common shares outstanding totaled 463,749 and 441,591 for December 31, 2015 and 2014, respectively. Diluted weighted-average common shares outstanding totaled 484,683 and 468,742 for December 31, 2015 and 2014, respectively. The diluted weighted-average common shares outstanding are solely the result of stock options.

Comprehensive Income

The Company is required to present comprehensive income (loss) and its components in a full set of general-purpose financial statements for all periods presented. Other comprehensive income (loss) comprises unrealized holding gains (losses) on the available for sale investment securities portfolio.

Cash Flow Information

For the purposes of reporting cash flows, cash and cash equivalents include cash and due from banks, interest-bearing deposits with other financial institutions, and federal funds sold with original maturities of less than 90 days.

Cash payments for interest in 2015 and 2014 were \$1,668,550 and \$1,700,940, respectively. Income tax payments totaled \$800,000 in 2015 and \$600,000 in 2014. The Company transferred \$804,940 and \$162,537 of loans from the portfolio to other real estate owned in 2015 and 2014, respectively. Fair value adjustments for securities available for sale in 2015 and 2014 were (\$16,556) and \$1,210,535, respectively.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Reclassification

Certain items in the prior year's financial statements have been reclassified to conform to the current-year presentation. Such reclassifications did not affect consolidated net income or consolidated stockholders' equity.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 2: INVESTMENT SECURITIES AVAILABLE FOR SALE

The amortized cost, gross unrealized gains, gross unrealized losses, and fair values of investment securities available for sale are as follows:

	<u>2015</u>			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government agency securities	\$ 6,731,000	\$ 32,936	\$ (26,459)	\$ 6,737,477
Obligations of states and political subdivisions	26,878,880	640,889	(63,513)	27,456,256
Mortgage-backed securities in government-sponsored entities	18,383,273	205,360	(87,617)	18,501,016
Total	<u>\$ 51,993,153</u>	<u>\$ 879,185</u>	<u>\$ (177,589)</u>	<u>\$ 52,694,749</u>

	<u>2014</u>			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government agency securities	\$ 5,225,542	\$ 35,460	\$ (26,823)	\$ 5,234,179
Obligations of states and political subdivisions	24,141,757	487,229	(76,829)	24,552,157
Mortgage-backed securities in government-sponsored entities	18,657,887	341,808	(42,694)	18,957,001
Total	<u>\$ 48,025,186</u>	<u>\$ 864,497</u>	<u>\$ (146,346)</u>	<u>\$ 48,743,337</u>

The amortized cost and fair value of investment securities at December 31, 2015, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Due within one year	\$ 923,478	\$ 927,720
Due after one year through five years	8,847,818	8,916,625
Due after five years through ten years	13,375,610	13,678,777
Due after ten years	10,462,972	10,670,611
Mortgage-backed securities in government-sponsored entities	18,383,273	18,501,016
Total	<u>\$ 51,993,153</u>	<u>\$ 52,694,749</u>

Investment securities with a carrying value of \$11,700,172 and \$11,545,564 at December 31, 2015 and 2014, respectively, were pledged to secure deposits and other purposes as required by law.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
NOTE 2: INVESTMENT SECURITIES AVAILABLE FOR SALE (CONTINUED)

In 2015, the Company realized gross gains of \$18,742 and gross losses of \$16,945 as a result of proceeds of \$1,472,601 in investment securities available for sale. In 2014, the Company realized gross gains of \$78,971 and gross losses of \$80,638 as a result of proceeds of \$7,173,737 in investment securities available for sale.

The following table shows 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 December 31:

2015

	Less than Twelve Months		Twelve Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. government agency securities	\$ 4,726,894	\$ (24,459)	\$ —	\$ —	\$ 4,726,894	\$ (26,459)
Obligations of states and political subdivisions	2,345,853	(47,015)	275,760	(16,498)	2,621,613	(63,513)
Mortgage-backed securities in government-sponsored entities	6,035,449	(50,510)	1,361,793	(37,107)	7,397,242	(87,617)
Total	\$ 13,108,196	\$ (123,984)	\$ 1,637,553	\$ (53,605)	\$ 14,745,749	\$ (177,589)

2014

	Less than Twelve Months		Twelve Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. government agency securities	\$ 1,498,161	\$ (1,839)	\$ 1,972,585	\$ (24,984)	\$ 3,470,746	\$ (26,823)
Obligations of states and political subdivisions	2,766,779	(16,631)	1,568,167	(60,197)	4,334,946	(76,829)
Mortgage-backed securities in government-sponsored entities	2,331,762	(10,265)	1,523,856	(32,430)	3,855,618	(42,694)
Total	\$ 6,596,702	\$ (28,735)	\$ 5,064,608	\$ (117,611)	\$ 11,661,310	\$ (146,346)

The Company reviews its position quarterly and has asserted that at December 31, 2015, the declines outlined in the above table represent temporary declines and the Company does not intend to sell these securities 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 forty-one positions that were temporarily impaired at December 31, 2015. The Company has concluded that the unrealized losses disclosed above are not other than temporary but are the result of interest rate changes that are not expected to result in the noncollection of principal and interest during the period.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 3: LOANS

The composition of net loans is as follows at December 31:

	<u>2015</u>	<u>2014</u>
Commercial loans	\$ 22,537,219	\$ 22,176,420
Commercial real estate loans	109,827,706	109,682,734
Consumer loans	4,729,593	5,287,837
Residential loans	54,316,167	52,239,467
Home equity lines of credit	<u>26,156,400</u>	<u>23,331,128</u>
	217,567,085	212,717,586
Net deferred loan fees	(253,676)	(274,248)
Less allowance for loan losses	<u>(2,856,417)</u>	<u>(3,070,857)</u>
Net loans	<u><u>\$ 214,456,992</u></u>	<u><u>\$ 209,372,481</u></u>

The Company's primary business activity is with customers located within its local trade area, which is concentrated in Portage County in Ohio. Commercial loans, commercial real estate loans, consumer loans, residential loans, and home equity lines of credit are granted. Although the Company has a diversified loan portfolio at December 31, 2015 and 2014, a substantial portion of its debtors' ability to honor their loan agreements is dependent upon the economic stability of its immediate trade area. loans.

Management has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and losses inherent in the loan portfolio. For purposes of determining the allowance for loan losses, the Company has segmented certain loans in the portfolio by product type. Loans are segmented into the following pools: commercial loans, commercial real estate loans, consumer loans, residential loans, and home equity lines of credit. Historical loss percentages for each risk category are calculated and used as the basis for calculating allowance allocations. These historical loss percentages were calculated over a 24-month period for all portfolio segments for the year ended December 31, 2014 and expanded to a 60-month period for the year ended December 31, 2015. Certain qualitative factors are then added to the historical allocation percentage to get the adjusted factor to be applied to nonclassified loans.

The following qualitative factors are analyzed for each portfolio segment:

- ▶ Changes in trends in lending policies and procedures
- ▶ Changes in economic trends
- ▶ Changes in volume and terms
- ▶ Changes in experience, depth, and ability of management
- ▶ Changes in levels and trends in delinquencies
- ▶ Changes in historical loss allocations
- ▶ Changes in trends determined through loan review
- ▶ Changes in collateral dependent loan values
- ▶ Changes in concentrations of credit

▶ Changes in trends in external factors

These qualitative factors are reviewed each quarter and adjusted based upon relevant changes within the portfolio. During 2015, the qualitative factor percentages for commercial loans, commercial real estate loans, consumer loans, residential loans, and home equity lines of credit slightly increased throughout the year. The addition of a qualitative factor adjustment representing trends that could affect collateral values was the primary factor for the increase in commercial loans, commercial real estate loans, residential loans, and home equity lines of credit. Previously, the Company had considered this factor in support for prior unallocated allowances. An overall decrease in delinquencies and nonaccrual loan levels moderately offset the increasing factor adjustments for commercial loans, commercial real estate loans, and home equity lines of credit. Historical loss rates increased over the course of 2015 for commercial loans, commercial real estate loans, consumer loans, residential loans, and home equity lines of credit as a direct result of the expanded historical net charge-off period, which was considered to be more appropriate for the loan types and support the discovery, measurement, and application of adjustment factors.

The decline in the ending reserve balance in commercial real estate loans from the end of the previous year was principally the result of the effect of two significant commercial real estate loan pay-offs that had specific reserves previously applied. In addition, there were two significant charge-offs as well as two significant recoveries applied to the commercial real estate loan category in 2015. The ending reserve balances for commercial loans, consumer loans, residential loans, and home equity lines of credit remained relatively comparable to the prior end of year reserve balances.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 3: LOANS (CONTINUED)

The total allowance reflects management's estimate of loan losses inherent in the loan portfolio at the balance sheet date. The Company considers the allowance for loan losses of \$2.9 million adequate to cover loan losses inherent in the loan portfolio, at December 31, 2015. The following tables presents, by portfolio segment, the changes in the allowance for loan losses and the recorded investment in loans as of December 31:

	2015							
	Commercial	Commercial Real Estate	Consumer	Residential	Home Equity Lines of Credit	Unallocated	Total	
Allowance for loan losses:								
Beginning balance	\$ 285,516	\$ 2,094,059	\$ 110,687	\$ 416,200	\$ 107,373	\$ 57,022	\$ 3,070,857	
Charge-offs	(2,736)	(298,339)	(18,533)	(54,392)	(38,386)	—	(412,386)	
Recoveries	12,742	145,189	4,800	35,215	—	—	197,946	
Reallocations	(33,024)	(299,612)	(6,386)	105,282	74,922	158,818	—	
Ending balance	\$ 262,498	\$ 1,641,297	\$ 90,568	\$ 502,305	\$ 143,909	\$ 215,840	\$ 2,856,417	
Ending balance: individually evaluated for impairment	\$ 8,850	\$ 305,116	\$ 48,048	\$ 63,776	\$ —	\$ —	\$ 425,790	
Ending balance: collectively evaluated for impairment	\$ 253,648	\$ 1,336,181	\$ 42,520	\$ 438,529	\$ 143,909	\$ 215,840	\$ 2,430,627	
Loans receivable:								
Ending balance	\$ 22,537,219	\$ 109,827,706	\$ 4,729,593	\$ 54,316,167	\$ 26,156,400	\$ —	\$ 217,567,085	
Ending balance: individually evaluated for impairment	\$ 86,319	\$ 1,914,404	\$ 92,041	\$ 314,651	\$ —	\$ —	\$ 2,407,415	
Ending balance: collectively evaluated for impairment	\$ 22,450,900	\$ 107,913,302	\$ 4,637,552	\$ 54,001,516	\$ 26,156,400	\$ —	\$ 215,159,670	

	2014							
	Commercial	Commercial Real Estate	Consumer	Residential	Home Equity Lines of Credit	Unallocated	Total	
Allowance for loan losses:								
Beginning balance	\$ 617,582	\$ 1,947,349	\$ 61,185	\$ 432,085	\$ 197,769	\$ 34,980	\$ 3,290,950	
Charge-offs	(253,249)	(241,750)	(18,143)	(101,393)	(1,683)	—	(616,218)	
Recoveries	28,367	4,324	6,177	2,257	—	—	41,125	
Provision	(107,184)	384,136	61,468	83,251	(88,713)	22,042	355,000	
Ending balance	\$ 285,516	\$ 2,094,059	\$ 110,687	\$ 416,200	\$ 107,373	\$ 57,022	\$ 3,070,857	
Ending balance: individually evaluated for impairment	\$ 32,143	\$ 678,488	\$ 50,945	\$ 66,493	\$ —	\$ —	\$ 828,069	
Ending balance: collectively evaluated for impairment	\$ 253,373	\$ 1,415,571	\$ 59,742	\$ 349,707	\$ 107,373	\$ 57,022	\$ 2,242,788	
Loans receivable:								
Ending balance	\$ 22,176,420	\$ 109,682,734	\$ 5,287,837	\$ 52,239,467	\$ 23,331,128	\$ —	\$ 212,717,586	
Ending balance: individually evaluated for impairment	\$ 1,593,384	\$ 2,862,655	\$ 105,171	\$ 321,797	\$ —	\$ —	\$ 4,883,007	
Ending balance: collectively evaluated for impairment	\$ 20,583,036	\$ 106,820,079	\$ 5,182,666	\$ 51,917,670	\$ 23,331,128	\$ —	\$ 207,834,579	

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 3: LOANS (CONTINUED)

Credit Quality Information

The following tables represent credit exposures by internally assigned grades for the years ended December 31, 2015 and 2014, respectively. The grading analysis estimates the capability of the borrower to repay the contractual obligations of the loan agreements as scheduled or at all. The Company's internal credit risk grading system is based on experiences with similarly graded loans.

Management utilizes a seven-point internal risk rating system to monitor the credit quality of the overall portfolio. The first three categories are considered not criticized and are aggregated as Pass-rated. Pass-rated loans are protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral. The criticized rating categories utilized by management generally follow bank regulatory definitions. Special Mention category loans have a potential weakness or risk that exists, which could cause a more serious problem if not corrected. The Substandard category loans have a well-defined weakness based on objective evidence and are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. The Doubtful category loans have all the weaknesses inherent in a substandard asset. In addition, these weaknesses make collection or liquidation in full highly questionable and improbable, based on existing circumstances. The Loss category loans are considered uncollectible, or of such value that continuance as an asset is not warranted.

	As of December 31, 2015		
	Commercial	Commercial Real Estate	Total
Pass	\$ 21,603,954	\$ 101,165,829	\$ 122,769,783
Special mention	320,700	3,751,125	4,071,825
Substandard	606,443	4,910,752	5,517,195
Doubtful	6,122	—	6,122
Loss	—	—	—
Total	\$ 22,537,219	\$ 109,827,706	\$ 132,364,925

	As of December 31, 2014		
	Commercial	Commercial Real Estate	Total
Pass	\$ 19,797,351	\$ 101,104,468	\$ 120,901,819
Special mention	215,599	2,402,135	2,617,734
Substandard	2,069,273	6,176,132	8,245,405
Doubtful	94,197	—	94,197
Loss	—	—	—
Total	\$ 22,176,420	\$ 109,682,734	\$ 131,859,155

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 3: LOANS (CONTINUED)

Credit Quality Information (Continued)

For consumer loans, residential loans, and home equity lines of credit, the Company evaluates credit quality based on whether the loan is considered performing or non-performing. Non-performing loans include those loans that are considered nonaccrual and all loans past due 90 or more days. The following tables present the balances of these loans by classes of the loan portfolio based on payment performance as of December 31:

2015

	Consumer	Residential	Home Equity Lines of Credit	Total
Performing	\$ 4,711,102	\$ 53,903,526	\$ 26,111,894	
Nonperforming	18,491	412,641	44,506	
Total	\$ 4,729,593	\$ 54,316,167	\$ 26,156,400	

2014

	Consumer	Residential	Home Equity Lines of Credit	Total
Performing	\$ 5,254,749	\$ 51,617,342	\$ 23,132,444	
Nonperforming	33,088	622,125	198,685	
Total	\$ 5,287,837	\$ 52,239,467	\$ 23,331,129	

Age Analysis of Past Due Loans Receivable by Class

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by the length of time a recorded payment is past due. The following tables present the classes of the loan portfolio summarized by the aging categories of performing loans and nonaccrual loans as of December 31:

2015

	30 – 59 Days Past Due	60 – 89 Days Past Due	90 Days Or Greater & Accruing	Total Past Due	Current	Nonaccrual	Total Loans
Commercial loans	\$ —	\$ —	\$ —	\$ —	\$ 22,416,205	\$ 121,014	
Commercial real estate loans	315,731	162,643	—	478,373	108,449,333	900,000	
Consumer loans	163,395	14,110	4,743	182,249	4,533,596	13,748	
Residential loans	985,233	82,611	6,283	1,074,127	52,835,682	406,358	
Home equity lines of credit	44,949	145,456	—	190,405	25,921,489	44,506	
Total	\$ 1,509,308	\$ 404,820	\$ 11,026	\$ 1,925,154	\$ 214,156,305	\$ 1,485,626	

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
 NOTE 3: LOANS (CONTINUED)

Age Analysis of Past Due Loans Receivable by Class (Continued)

	2014							Total Loans
	30 – 59 Days Past Due	60 – 89 Days Past Due	90 Days Or Greater & Accruing	Total Past Due	Current	Nonaccrual		
Commercial loans	\$ —	\$ —	\$ —	\$ —	\$ 22,072,548	\$ 103,872	\$ 22,176,420	
Commercial real estate loans	40,754	—	—	40,754	107,318,965	2,323,015	109,682,734	
Consumer loans	104,537	—	803	105,340	5,150,212	32,285	5,287,837	
Residential loans	346,781	—	—	346,781	51,270,561	622,125	52,239,467	
Home equity lines of credit	109,357	—	—	109,357	23,023,086	198,685	23,331,128	
Total	\$ 601,429	\$ —	\$ 803	\$ 602,232	\$ 208,835,372	\$ 3,279,982	\$ 212,717,586	

Interest income that would have been recorded had nonaccrual loans not been placed on nonaccrual status was \$86,752 and \$154,856 in 2015 and 2014, respectively.

Impaired Loans

The following tables present the recorded investment and unpaid principal balances of impaired loans by class, segregated by those for which a specific allowance was required and those for which a specific allowance was not necessary as of December 31:

	2015				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial loans	\$ —	\$ —	\$ —	\$ 1,351,490	\$ 88,110
Commercial real estate loans	822,579	1,090,745	—	1,499,537	27,564
Consumer loans	43,993	91,435	—	48,719	2,908
Residential loans	94,521	96,393	—	95,389	3,737
Home equity lines of credit	—	—	—	—	—
	\$ 961,093	\$ 1,278,573	\$ —	\$ 2,995,135	\$ 122,319
With an allowance recorded:					
Commercial loans	\$ 86,319	\$ 144,481	\$ 8,850	\$ 86,364	\$ 2,022
Commercial real estate loans	1,091,825	1,599,516	305,116	1,149,180	17,607
Consumer loans	48,048	48,048	48,048	49,400	3,103
Residential loans	220,130	220,130	63,776	222,460	12,533
Home equity loans of credit	—	—	—	—	—
	\$ 1,446,322	\$ 2,012,175	\$ 425,790	\$ 1,507,404	\$ 35,265
Total:					
Commercial loans	\$ 86,319	\$ 144,481	\$ 8,850	\$ 1,437,854	\$ 90,132
Commercial real estate loans	1,914,404	2,690,261	305,116	2,648,717	45,171
Consumer loans	92,041	139,483	48,048	98,119	6,011
Residential loans	314,651	316,523	63,776	317,849	16,270
Home equity lines of credit	—	—	—	—	—
	\$ 2,407,415	\$ 3,290,748	\$ 425,790	\$ 4,502,539	\$ 157,584

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 3: LOANS (CONTINUED)

Impaired Loans (Continued)

	2014				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial loans	\$ 1,489,512	\$ 1,489,511	\$ —	\$ 1,803,357	\$ 102,740
Commercial real estate loans	755,165	1,657,341	—	1,406,222	36,416
Consumer loans	54,226	99,877	—	102,362	3,528
Residential loans	96,393	96,393	—	73,993	3,447
Home equity lines of credit	—	—	—	2,567	123
	<u>\$ 2,395,296</u>	<u>\$ 3,343,122</u>	<u>\$ —</u>	<u>\$ 3,388,501</u>	<u>\$ 146,254</u>
With an allowance recorded:					
Commercial loans	\$ 103,872	\$ 145,712	\$ 32,143	\$ 120,631	\$ 3,372
Commercial real estate loans	2,107,490	2,419,415	678,488	2,141,572	30,266
Consumer loans	50,945	50,944	50,945	52,325	3,098
Residential loans	225,404	225,404	66,493	229,050	12,624
Home equity loans of credit	—	—	—	—	—
	<u>\$ 2,487,711</u>	<u>\$ 2,841,475</u>	<u>\$ 828,069</u>	<u>\$ 2,543,578</u>	<u>\$ 49,360</u>
Total:					
Commercial loans	\$ 1,593,383	\$ 1,635,223	\$ 32,143	\$ 1,923,988	\$ 106,112
Commercial real estate loans	2,862,655	4,076,756	678,488	3,547,795	66,682
Consumer loans	105,171	150,822	50,945	154,687	6,626
Residential loans	321,797	321,797	66,493	303,043	16,071
Home equity lines of credit	—	—	—	2,567	123
	<u>\$ 4,883,006</u>	<u>\$ 6,184,597</u>	<u>\$ 828,069</u>	<u>\$ 5,932,079</u>	<u>\$ 195,614</u>

On January 1, 2015, the Company adopted Accounting Standards Update (ASU) 2014-04, Receivables - Troubled Debt Restructuring by Creditors. As of December 31, 2015, the Company had \$535,172 of foreclosed real estate property obtained by physical possession and \$405,417 of consumer mortgage loans secured by residential real estate properties for which foreclosure proceedings are in process according to local jurisdiction.

Troubled Debt Restructurings

As of December 31, 2015 and 2014, the Company has a recorded investment in troubled debt restructurings of \$1,685,977 and \$4,598,609, respectively. The Company allocated \$318,889 and \$795,925 of specific allowance for those loans at December 31, 2015 and 2014, respectively. There were no new troubled debt restructurings entered into for the year ended December 31, 2015.

The tables below summarize the Company's troubled debt restructurings before and after modifications for the year ended December 31, 2014:

	2014		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings:			
Commercial real estate loans	1	135,444	135,444
Residential loans	1	97,891	97,891

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 3: LOANS (CONTINUED)

Troubled Debt Restructurings (Continued)

The modification of the terms of the commercial real estate and residential loans performed during the year ended December 31, 2014 included extension of the terms of the originals loans and/or lowering the stated interest rates. No principal reductions were made. Additional interest income of \$62,917 and \$76,697 would have been recognized for the years ended December 31, 2015 and 2014, respectively, at the original interest rate as compared to the adjusted interest rate on the troubled debt restructurings.

The Company had payment defaults on three troubled debt restructuring contracts during 2015 comprised of three commercial real estate loans totaling \$291,689. The Company had payment defaults on seven troubled debt restructuring contracts during 2014 comprised of three commercial loans totaling \$309,443, three commercial real estate loans totaling \$120,775, and one consumer loan totaling \$6,286.

NOTE 4: PREMISES AND EQUIPMENT

Major classifications of premises and equipment are summarized as follows:

	2015	2014
Land and land improvements	\$ 1,576,056	\$ 1,561,926
Building and leasehold improvements	3,500,097	2,903,214
Furniture, fixtures, and equipment	1,907,197	1,838,070
	<hr/> 6,983,350	<hr/> 6,303,210
Less accumulated depreciation	(2,512,386)	(2,365,544)
Total	<hr/> <u>\$ 4,470,964</u>	<hr/> <u>\$ 3,937,666</u>

Depreciation charged to operations was \$146,843 in 2015 and \$140,246 in 2014.

NOTE 5: DEPOSITS

Time deposits at December 31, 2015, mature \$46,170,459, \$11,342,309, \$6,892,934, \$4,087,833, \$3,579,879, and \$1,205,873 during 2016, 2017, 2018, 2019, 2020, 2021 and thereafter, respectively.

Time deposits include certificates of deposit and other time deposits in denominations of \$100,000 or more. Such deposits aggregated \$1,632,487 and \$1,337,771 at December 31, 2015 and 2014, respectively.

The aggregate amount of time deposit accounts that meet or exceed the FDIC insurance limit of \$250,000 totaled \$1,520,416 and \$264,243 at December 31, 2014 and 2013, respectively.

Included in certificates of deposit at December 31, 2015 and 2014, were \$22,265,639 and \$23,141,712, respectively, obtained through the Certificate of Deposit Account Registry Services (CDARS). This service allows deposit customers to maintain fully insured balances in excess of the \$250,000 FDIC insurance limit without the inconvenience of having multi-banking relationships. Under the reciprocal program, which the Company is currently participating in, customers agree to allow the Company to place their deposits with participating banks in the CDARS program, in insurable amounts under \$250,000. In exchange, other banks in the program agree to place their deposits with Portage Community Bank, also in insurable amounts under \$250,000.

Related-party deposits were \$1,354,432 and \$1,003,969 at December 31, 2015 and 2014, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 6: FHLB ADVANCES

The following table sets forth information concerning other borrowings with the FHLB:

Description	Maturity range		Weighted- average interest rate	At December 31,	
	from	to		2015	2014
Mortgage match - amortizing	03/01/18	11/01/29	1.80%	\$ 13,952,732	\$ 12,409,903
Mortgage match - non-amortizing	01/06/16	02/06/19	4.15	4,115,800	6,950,042
Total			2.34%	<u>\$ 18,068,532</u>	<u>\$ 19,359,945</u>

At December 31, 2015, the Bank had a cash management line of credit enabling it to borrow up to \$15.0 million from the Federal Home Loan Bank of Cincinnati (“FHLB”). The line of credit must be renewed on an annual basis. There were no borrowings from the line of credit outstanding as of December 31, 2015 and December 31, 2014. The Bank has a remaining borrowing capacity of \$36.0 million at December 31, 2015.

Borrowings from FHLB are secured with a blanket security agreement and required investment in FHLB member bank stock. As part of the security agreement, the Bank maintains unencumbered qualifying assets (principally 1-4 family residential mortgage loans) in an amount at least as much as the advances from the FHLB. Additionally, the Bank’s FHLB stock of \$876,600 at December 31, 2015 and 2014, respectively, is pledged to secure these advances. Maturities over the next five years and thereafter were as follows:

Year Ending December 31,	Amount	Weighted- Average Rate
2016	\$ 6,246,434	1.75 %
2017	3,166,544	1.71
2018	2,130,648	1.67
2019	2,148,271	1.62
2020	1,285,993	1.62
Thereafter	3,090,642	1.62
Total	<u>\$ 18,068,532</u>	2.34 %

Monthly principal and interest payments are due on the mortgage match fixed rate amortizing borrowings; additionally, a 5 percent, 10 percent, or up to 20 percent principal curtailment is due on each borrowing’s anniversary date. Monthly interest payments are due on the mortgage match fixed rate non-amortizing borrowings and principal payments are paid in total at maturity.

The Company and Bank each maintain a \$1,000,000 unsecured line of credit with another financial institution. No amounts were outstanding under these lines of credit at December 31, 2015 and 2014.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 7: SUBORDINATED DEBENTURES

In March 2004, Portage Bancshares Capital Trust I, a trust formed by the Company, issued \$2,500,000 of floating rate, trust preferred securities as part of a pooled offering of such securities. The Company issued \$2,450,000 subordinated debentures to the trust in exchange for the proceeds of the offering. The debentures and related debt issuance costs represent the sole assets of the trust. The trust is not consolidated with the Company's financial statements, but rather the subordinated debentures are shown as a liability. The trust preferred securities must be redeemed no later than April 23, 2034. The Company had the option to call the trust preferred securities at par at five years from date of issuance. The subordinated debentures are also redeemable in whole or in part from time to time, upon the occurrence of specific events defined within the trust indenture. The Company has the option to defer interest payments on the subordinated debentures from time to time for a period not to exceed five consecutive years. The subordinated debentures may be included in Tier I capital with certain limitations applicable under current regulatory guidelines and interpretations.

The interest rate on the trust preferred securities and the subordinated debentures is computed as the three-month London Interbank Offering Rate (LIBOR) plus 285 points. At December 31, 2015 and 2014, this equated to 3.39 percent and 3.10 percent, respectively.

NOTE 8: INCOME TAXES

The provision for federal income taxes consists of:

	<u>2015</u>	<u>2014</u>
Current payable	\$ 968,486	\$ 768,223
Deferred	(11,734)	18,247
Total provision	<u>\$ 956,752</u>	<u>\$ 786,470</u>

No valuation allowance was established at December 31, 2015 and 2014, in view of the Company's ability to carryback to taxes paid in previous years and certain tax strategies, coupled with the anticipated future taxable income as evidenced by the Company's earnings potential. The tax effects of deductible and taxable temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are as follows:

	<u>2015</u>	<u>2014</u>
Deferred tax assets:		
Allowance for loan losses	\$ 655,901	\$ 706,524
Accrued expenses and employee benefits	525,220	414,012
Deferred loan fees	71,921	75,334
Stock-based compensation	88,173	89,946
Other	7,682	39,169
Deferred tax assets	<u>1,348,897</u>	<u>1,324,985</u>
Deferred tax liabilities:		
Depreciation	132,059	111,931
Unrealized gain on available-for-sale securities	238,543	244,171
Federal Home Loan Bank stock dividends	45,526	45,526
Prepaid expenses	9,968	16,515
Security accretion	1,848	3,251
Deferred tax liabilities	<u>427,944</u>	<u>421,394</u>
Net deferred tax assets	<u>\$ 920,953</u>	<u>\$ 903,591</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 8: INCOME TAXES (CONTINUED)

The reconciliation between the federal statutory rate and the Company's effective consolidated income tax rate is as follows:

	2015		2014	
	Amount	% of Pretax Income	Amount	% of Pretax Income
Provision at statutory rate	\$ 1,219,119	34.0 %	\$ 1,021,747	34.0 %
Tax-exempt interest	(198,465)	(5.5)	(181,794)	(6.0)
Earnings on bank-owned life insurance	(57,578)	(1.6)	(60,090)	(2.0)
Other	(6,324)	(0.2)	6,607	0.2
Actual tax expense and effective rate	<u>\$ 956,752</u>	<u>26.7 %</u>	<u>\$ 786,470</u>	<u>26.2 %</u>

The Company prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Benefits from tax positions should be recognized in the financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority that would have full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be derecognized in the first subsequent financial reporting period in which that threshold is no longer met.

There is currently no liability for uncertain tax positions and no known unrecognized tax benefits. The Bank recognizes, when applicable, interest and penalties related to unrecognized tax benefits in the income taxes in the Consolidated Statement of Income. With few exceptions, the Bank is no longer subject to U.S. federal income tax examinations by tax authorities for years before 2012.

NOTE 9: EMPLOYEE BENEFITS

401(k) Plan

The Company sponsors a 401(k) plan covering substantially all employees. The Company matches contributions at the rate of 100 percent of each participant's voluntary contributions, limited to a maximum of 6 percent of a covered employee's annual compensation. In addition to the Company's matching contribution, a profit sharing contribution to the plan can be made at the discretion of the Board. Employee voluntary contributions and employers' matching contributions are vested immediately. The expense related to the plan was \$183,621 and \$174,592 for the years ended December 31, 2015 and 2014, respectively.

Supplemental Retirement Plan

The Company sponsors a supplemental retirement plan ("SERP") which covers several key members of management. Participants will receive annually a percentage of their base compensation at the time of their retirement for a maximum of ten years. The liability recorded at December 31, 2015 and 2014, was \$1,253,624 and \$1,025,975, respectively. The expense related to the plan was \$253,858 and \$211,539 for 2015 and 2014, respectively. Distributions to participants were \$26,209 in 2015 and 2014, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 9: EMPLOYEE BENEFITS (CONTINUED)

Director Deferral Plan

The Company sponsors a director deferral plan to provide post-separation payments to participating directors who elect to defer their directors' fees. The plan allows participating directors to defer a portion or all director fees during any plan year. The participants' deferral account balance within the plan is credited annually with interest, based on the Bank's return on equity on a tax-deferred basis. The liability recorded at December 31, 2015 and 2014, was \$291,140 and \$191,708, respectively. The expense related to the plan was \$99,432 and \$77,040 for 2015 and 2014, respectively.

Stock Option Plan

The Company has a fixed director and employee stock-based compensation plan. Under the plan, the Company may grant options for up to 200,000 shares of common stock. The exercise price for the purchase of shares subject to a stock option may not be less than 100 percent of the fair market value of the shares covered by the option on the date of the grant. The term of stock options will not exceed ten years from the date of grant. Vesting occurs at 20 percent per year of service.

The following table presents share data related to the outstanding options:

	2015	Weighted-Average Exercise Price	2014	Weighted-Average Exercise Price
Outstanding, January 1	83,931	\$ 54.01	94,009	\$ 50.09
Granted	—	—	6,790	77.00
Exercised	(23,476)	43.94	(16,768)	41.40
Forfeited	(80)	77.00	(100)	45.00
Outstanding, December 31	<u>60,375</u>	\$ 57.89	<u>83,931</u>	\$ 54.01
Exercisable at year-end	<u>53,413</u>	\$ 55.69	<u>74,561</u>	\$ 51.47

The following table summarizes the characteristics of stock options at December 31, 2015:

Grant Date	Exercise Price	Outstanding			Exercisable		
		Shares	Remaining Average Life	Average Exercise Price	Shares	Average Exercise Price	
1/24/2007	50.00	23,160	1.06	\$ 50.00	23,160	\$ 50.00	
10/22/2008	58.50	25,675	2.81	58.50	25,675	58.50	
1/24/2011	63.10	2,400	5.06	63.10	1,920	63.10	
1/25/2012	67.65	1,700	6.07	67.65	1,020	67.65	
1/31/2013	71.50	750	7.08	71.50	300	71.50	
2/19/2014	77.00	1,950	8.14	77.00	390	77.00	
4/23/2014	77.00	4,740	8.31	77.00	948	77.00	
		<u>60,375</u>		\$ 57.89	<u>53,413</u>	\$ 55.69	

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 10: LOAN COMMITMENTS

Some financial instruments, such as loan commitments, credit lines, letters of credit, and overdraft protection, are issued to meet customer financing needs. These are agreements to provide credit or to support the credit of others, as long as conditions established in the contract are met, and usually have expiration dates. Commitments may expire without being used. Off-balance-sheet risk to credit loss exists up to the face amount of these instruments, although material losses are not anticipated. The same credit policies are used to make such commitments as are used for loans, including obtaining collateral at exercise of the commitment. Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party.

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

	2015		2014	
	Fixed Rate	Variable Rate	Fixed Rate	Variable Rate
Unused business lines of credit	\$ 762,170	\$ 20,275,585	\$ 888,380	\$ 18,105,730
Unused construction lines of credit	1,951,902	360,646	686,062	345,891
Unused consumer lines of credit	105,241	20,035,091	105,154	19,384,879
Standby letters of credit	—	131,291	—	131,291
Total	\$ 2,891,313	\$ 40,802,613	\$ 1,679,596	\$ 37,967,791

Commitments to make loans are generally made for periods of 60 days or less. The fixed rate loan commitments have interest rates ranging from 2.25 percent to 18.00 percent at December 31, 2015 and December 31, 2014.

Standby letters of credit represent conditional commitments issued to guarantee performance of a customer to a third party. The coverage period for these instruments is typically a one-year period with renewal option subject to prior approval by management. Fees earned from the issuance of these letters are recognized over the coverage period. For secured letters of credit, the collateral is typically Bank deposit instruments.

NOTE 11: REGULATORY RESTRICTIONS

Contingent Liabilities

The Company is involved in various legal actions from the normal course of business activities. Management believes the liability, if any; arising from such actions will not have a material adverse effect on the Company's financial position.

Restriction on Cash and Due From Banks

The Bank is required to maintain reserve funds in cash or on deposit with the Federal Reserve Bank. The required reserve was \$1,106,000 and \$946,000 for the years ended December 31, 2015 and 2014, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 11: REGULATORY RESTRICTIONS (CONTINUED)

Loans

Federal law prevents the Company from borrowing from the Bank unless the loans are secured by specific obligations. Further, such secured loans are limited in amount up to 10 percent of the Bank's common stock and capital surplus.

Dividends

The Bank is subject to a dividend restriction that generally limits the amount of dividends that can be paid by an Ohio state-chartered bank. Under the Ohio Banking Code, cash dividends may not exceed net profits as defined for that year, combined with retained net profits for the two preceding years less any required transfers to surplus. Under this formula, the amount available for payment of dividends in 2016 is \$5,012,108 plus 2016 profits retained up to the date of the dividend declaration.

NOTE 12: REGULATORY CAPITAL MATTERS

Banks and bank holding companies are subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Company on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital. Capital amounts and ratios for December 31, 2014 are calculated using Basel I rules. Management believes as of December 31, 2015, the Company and Bank meet all capital adequacy requirements to which they are subject.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At year-end 2015 and 2014, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the institution's category.

Actual and required capital amounts and ratios are presented below at year-end.

	Actual		Required for Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Regulations	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
2015						
Total Capital (to Risk-Weighted Assets):						
Consolidated	\$ 34,087,985	16.01%	\$ 17,030,592	8.00%	\$ 21,288,240	10.00%
Portage Community Bank	34,093,431	16.04	17,005,452	8.00	21,256,815	10.00
Tier 1 Capital (to Risk-Weighted Assets):						
Consolidated	\$ 31,424,543	14.76%	\$ 12,772,944	6.00%	\$ 17,030,592	8.00%
Portage Community Bank	31,433,868	14.79	12,754,089	6.00	17,005,452	8.00
Common Equity Tier 1 Capital (to Risk-Weighted Assets):						
Consolidated	\$ 31,424,543	14.76%	\$ 9,579,708	4.50%	\$ 13,837,356	6.50%
Portage Community Bank	31,433,868	14.79	9,565,567	4.50	13,816,929	6.50
Tier 1 Capital (to Average Assets):						
Consolidated	\$ 31,424,543	10.52%	\$ 11,944,691	4.00%	\$ 14,930,864	5.00%
Portage Community Bank	31,433,868	10.58	11,880,797	4.00	14,850,996	5.00

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 12: REGULATORY CAPITAL MATTERS (CONTINUED)

	Actual		Required for Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Regulations	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
2014						
Total Capital (to Risk-Weighted Assets):						
Consolidated	\$ 30,542,769	15.00%	\$ 16,294,288	8.00%	\$ 20,367,861	10.00%
Portage Community Bank	31,350,070	15.39	16,294,288	8.00	20,367,861	10.00
Tier 1 Capital (to Risk-Weighted Assets):						
Consolidated	\$ 27,990,306	13.74%	\$ 8,147,144	4.00%	\$ 12,220,716	6.00%
Portage Community Bank	28,797,607	14.14	8,147,144	4.00	12,220,716	6.00
Tier 1 Capital (to Average Assets):						
Consolidated	\$ 27,990,306	9.93%	\$ 11,272,579	4.00%	\$ 14,090,724	5.00%
Portage Community Bank	28,797,607	10.22	11,270,062	4.00	14,087,578	5.00

NOTE 13: 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. The three broad levels defined by U.S. generally accepted accounting principles are as follows:

- 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 the quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these assets and liabilities includes 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. The following tables set forth the Company's financial assets by level within the fair value hierarchy that were measured at fair value on a recurring basis at December 31:

	2015			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Fair value measurements on a recurring basis:				
Securities available for sale:				
U.S. government agency securities	\$ 6,737,477	\$ —	\$ 6,737,477	\$ —
Obligations of states and political subdivisions	27,456,256	—	27,456,256	—
Mortgage-backed securities in government-sponsored entities	18,501,016	—	18,501,016	—
Total	\$ 52,694,749	\$ —	\$ 52,694,749	\$ —

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 13: FAIR VALUE MEASUREMENTS (CONTINUED)

	2014			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Fair value measurements on a recurring basis:				
Securities available for sale:				
U.S. government agency securities	\$ 5,234,179	\$ —	\$ 5,234,179	\$ —
Obligations of states and political subdivisions	24,552,157	—	24,552,157	—
Mortgage-backed securities in government-sponsored entities	18,957,001	—	18,957,001	—
Total	\$ 48,743,337	\$ —	\$ 48,743,337	\$ —

The Company's investment securities are valued by a third-party pricing service commonly used in the banking industry utilizing observable inputs. The pricing provider utilizes evaluated pricing models that vary based on asset class. These models incorporate available market information including quoted prices of investment securities with similar characteristics and, because many fixed-income investment securities do not trade on a daily basis, apply available information through processes such as benchmark yield curves, benchmarking of like investment securities, sector groupings, and matrix pricing. In addition, model processes, such as an option adjusted spread model, are used to develop prepayment estimates and interest rate scenarios for investment securities with prepayment features.

Management uses a recognized third-party pricing service to obtain fair values for the Company's fixed income securities portfolio. Documentation is maintained as to the methodology and summary of inputs used by the pricing service for the various types of securities, and management notes that the servicer maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs. Management does not have access to all of the individual specific assumptions and inputs used for each security. The significant observable inputs include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data including market research publications.

Based on management's review of the methodology and summary of inputs used, management has concluded these assets are properly classified as Level 2 assets.

The following tables set forth the Company's financial and non-financial assets by level within the fair value hierarchy that were measured at fair value on a non-recurring basis at December 31:

	2015			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Impaired loans	\$ 1,730,749	\$ —	\$ —	\$ 1,730,749
Other real estate owned	535,172	—	—	535,172

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
 NOTE 13: FAIR VALUE MEASUREMENTS (CONTINUED)

2014

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Impaired loans	\$ 4,054,937	\$ —	\$ —	\$ 4,054,937
Other real estate owned	128,718	—	—	128,718

Impaired loans that are collateral-dependent are written down to fair value through the establishment of specific reserves. Techniques used to value the collateral that secures the impaired loan include: quoted market prices for identical assets classified as Level I inputs and observable inputs, employed by certified appraisers, for similar assets classified as Level II inputs. In cases where valuation techniques included inputs that are unobservable and are based on estimates and assumptions developed by management based on the best information available under each circumstance, the asset valuation is classified as Level III input.

Other real estate owned (“OREO”) is measured at fair value, less cost to sell at the date of the foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management. The assets are carried at fair value, less cost to sell. Income and expense from operations and changes in valuation allowance are included in the net expenses from OREO.

The following tables present additional quantitative information about assets measured at fair value on a nonrecurring basis for which the Company has utilized Level III inputs to determine fair value at December 31 2015 and 2014, respectively:

	Fair Value	Valuation Technique	Unobservable Inputs	Range (Weighted Averages)
Impaired loans (collateral-dependent)	\$ 1,730,749	Appraisal of collateral (1)	Appraisal adjustments (2)	0% - 38.57% (31.23%)
Other real estate owned	535,172	Appraisal of collateral (1), (3)	Appraisal adjustments (2)	9%

	Fair Value	Valuation Technique	Unobservable Inputs	Range (Weighted Averages)
Impaired loans (collateral-dependent)	\$ 4,054,937	Appraisal of collateral (1)	Appraisal adjustments (2)	0% - 44% (33.49%)
Other real estate owned	128,718	Appraisal of collateral (1), (3)	Appraisal adjustments (2)	9%

(1) Fair value is generally determined through independent appraisals of the underlying collateral, which include various Level III inputs which are not identifiable.

(2) Appraisals may be adjusted by management for qualitative factors such as economic conditions, aging, and/or estimated liquidation expenses incurred when selling collateral. The range and weighted average of appraisal adjustments and liquidation expenses are presented as a percentage of the appraisal.

(3) Includes qualitative adjustments by management and estimated liquidation expenses.

The estimated fair value of the Company's financial instruments at December 31 is as follows:

2015

	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value
Financial assets:					
Cash and cash equivalents	\$ 16,245,940	\$ 16,245,940	\$ —	\$ —	\$ 16,245,940
Investment securities					
available for sale	52,694,749	—	52,694,749	—	52,694,749
Loans held for sale	755,267	755,267	—	—	755,267
Net loans	214,456,992	—	—	214,548,018	214,548,018
Bank-owned life insurance	6,630,830	6,630,830	—	—	6,630,830
Regulatory stock	1,240,250	1,240,250	—	—	1,240,250
Accrued interest receivable	752,680	752,680	—	—	752,680
Financial liabilities:					
Deposits	\$ 244,113,927	\$ 170,834,640	\$ —	\$ 72,999,995	\$ 243,834,635
Federal Home Loan Bank advances	18,068,532	—	—	18,156,718	18,156,718
Subordinated debentures	2,450,000	—	—	2,021,250	2,021,250
Accrued interest payable	111,810	111,810	—	—	111,810

2014

	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value
Financial assets:					
Cash and cash equivalents	\$ 7,377,469	\$ 7,377,469	\$ —	\$ —	\$ 7,377,469
Investment securities					
available for sale	48,743,337	—	48,743,337	—	48,743,337
Loans held for sale	910,063	910,063	—	—	910,063
Net loans	209,372,481	—	—	214,428,037	214,428,037
Bank-owned life insurance	6,461,484	6,461,484	—	—	6,461,484
Regulatory stock	1,240,250	1,240,250	—	—	1,240,250
Accrued interest receivable	735,879	735,879	—	—	735,879
Financial liabilities:					
Deposits	\$ 227,967,804	\$ 155,014,313	\$ —	\$ 73,512,003	\$ 228,526,316
Federal Home Loan Bank advances	19,359,945	—	—	19,583,440	19,583,440
Subordinated debentures	2,450,000	—	—	1,960,000	1,960,000
Accrued interest payable	114,482	114,482	—	—	114,482

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 14: FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS (CONTINUED)

Financial instruments are defined as cash, evidence of ownership interest in an entity, or a contract which creates an obligation or right to receive or deliver cash or another financial instrument from/to a second entity on potentially favorable or unfavorable terms.

Fair value is defined as the amount at which a financial instrument could be exchanged in a current transaction between willing parties other than in a forced liquidation sale. If a quoted market price is available for a financial instrument, the estimated fair value would be calculated based upon the market price per trading unit of the instrument.

If no readily available market exists, the fair value estimates for financial instruments should be based upon management's judgment regarding current economic conditions, interest rate risk, expected cash flows, future estimated losses, and other factors as determined through various option pricing formulas or simulation modeling. As many of these assumptions result from judgments made by management based upon estimates which are inherently uncertain, the resulting estimated fair values may not be indicative of the amount realizable in the sale of a particular financial instrument. In addition, changes in assumptions on which the estimated fair values are based may have a significant impact on the resulting estimated fair values.

As certain assets such as deferred tax assets and premises and equipment are not considered financial instruments, the estimated fair value of financial instruments would not represent the full value of the Company.

The Company employed simulation modeling in determining the estimated fair value of financial instruments for which quoted market prices were not available based upon the following assumptions:

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

The fair value is equal to the current carrying value.

Investment Securities Available for Sale

The fair value of investment securities available for sale 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.

Loans Held for Sale

The carrying amount of loans held for sale is the amount funded and approximates fair value due to the insignificant time between origination and date of sale.

Net Loans

The fair value is estimated by discounting the future cash flows using a simulation model that estimates future cash flows through the utilization of current market inputs at which loans with similar terms and qualities would be made to borrowers of similar credit quality. Where quoted market prices were available, primarily for certain residential mortgage loans, such market rates were utilized as estimates of fair value.

Bank-Owned Life Insurance

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 14: FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS (CONTINUED)

Deposits, Federal Home Loan Bank Advances, and Subordinated Debentures

Demand, savings, and money market deposit accounts are valued at the amount payable on demand as of year-end. Fair value for time deposits, Federal Home Loan Bank advances, and subordinated debentures is estimated by discounting the future cash flows using a simulation model which estimates future cash flows and constructs discount rates that consider reinvestment opportunities, operating expenses, noninterest income, credit quality, and prepayment risk.

Commitments to Extend Credit

These financial instruments are generally not subject to sale, and estimated fair values are not readily available. The carrying value, represented by the net deferred fee arising from the unrecognized commitment or letter of credit, and the fair value, determined by discounting the remaining contractual fee over the term of the commitment using fees currently charged to enter into similar agreements with similar credit risk, are not considered material for disclosure. The contractual amounts of unfunded commitments and letters of credit are presented in Note 10.

NOTE 15: ACCUMULATED OTHER COMPREHENSIVE INCOME

The following tables present the changes in accumulated other comprehensive income (loss) by component net of tax for the years ended December 31, 2015 and 2014:

	Net Unrealized Gains (Losses) on <u>Investment Securities</u>
Accumulated other comprehensive income, January 1, 2015	\$ 473,980
Other comprehensive loss before reclassification, net of tax	(9,741)
Amount reclassified from accumulated other comprehensive income	<u>(1,186)</u>
Total other comprehensive loss	(10,927)
Accumulated other comprehensive income, December 31, 2015	<u>\$ 463,053</u>
	Net Unrealized Gains (Losses) on <u>Investment Securities</u>
Accumulated other comprehensive loss, January 1, 2014	\$ (324,973)
Other comprehensive income before reclassification, net of tax	797,853
Amount reclassified from accumulated other comprehensive loss	<u>1,100</u>
Total other comprehensive income	798,953
Accumulated other comprehensive income, December 31, 2014	<u>\$ 473,980</u>

The following table presents significant amounts reclassified out of accumulated other comprehensive income (loss) for the years ended December 31, 2015 and 2014:

	Amount Reclassified from Accumulated Other Comprehensive Income (Loss)	Affected Line Item on the <u>Consolidated Statement of Income</u>
Details about other comprehensive loss:		
Net unrealized gain (losses) on investment securities	\$ (1,797)	Investment securities gains (losses), net
	<u>611</u>	Income taxes
	<u>\$ (1,186)</u>	Net of tax
	Amount Reclassified from Accumulated Other Comprehensive Income (Loss)	Affected Line Item on the <u>Consolidated Statement of Income</u>
Details about other comprehensive income:		
Net unrealized gain (losses) on investment securities	\$ 1,667	Investment securities gains (losses), net
	<u>(567)</u>	Income taxes
	<u>\$ 1,100</u>	Net of tax

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 16: SUBSCRIPTION AND SHARE PURCHASE AGREEMENT

The Company offered shares of no par common stock for purchase through the terms of the Agreement entered into on December 20, 2015 and ending on December 30, 2015. The Agreement allowed the Company to sell up to 10,000 shares of common stock at an offering price of \$85.90 per share to a limited number of offerees. The minimum purchase by a subscriber was 350 shares. Through the Agreement, the Company sold 5,965 shares of its common stock and received proceeds of \$509,748, net of offering expenses of \$2,464.

The Company offered shares of no par common stock for purchase through the terms of the Agreement entered into on October 29, 2014 and ending on December 23, 2014. The Agreement allowed the Company to sell up to 10,000 shares of common stock at an offering price of \$80.45 per share to a limited number of offerees. The minimum purchase by a subscriber was 375 shares. Through the Agreement, the Company sold 7,350 shares of its common stock and received proceeds of \$587,877, net of offering expenses of \$3,431.

NOTE 17: SUBSEQUENT EVENTS

The Company assessed events occurring subsequent to December 31, 2015, through March 29, 2016, for potential recognition and disclosure in the consolidated financial statements. No events have occurred that would require additional adjustments to or disclosure in the consolidated financial statements, which were issued on March 29, 2016.

PORTAGE BANCSHARES, INC

Officers

Margaret F. Medzie

President

Thomas S. Siciliano

Treasurer

Timothy E. Crock

Secretary

PORTAGE COMMUNITY BANK

Directors

Timothy E. Crock

Chairman of the Board

Paul E. Huchok

Vice Chairman of the Board

Thomas S. Siciliano

Director

Dr. Aaron A. Moats

Director

Richard J. Coe

Director

Kevin T. Lewis

Director

Dr. Emilio D. Ferrara

Director

James V. Damicone

Director

Richard L. Leonard

Director

Margaret F. Medzie

Director

Lee L. Jenior

Director

DIVISIONAL RESPONSIBILITIES

Adam B. Rubin

Vice President, Real Estate Division

Dennis P. Juvan

Registered Representative

Portage Community Financial Services

PORTAGE COMMUNITY BANK

Officers

Richard J. Coe

Chief Executive Officer

Kevin T. Lewis

President & Chief Lending Officer

Donald D. Herman

Vice President & Chief Financial Officer

Constance M. Bennett

Vice President & Chief Operations Officer

Jill M. Conard

Vice President & Main Office Administrator

Dominic Bellino

Vice President, Loan Operations

Deborah A. Bish

Vice President, Commercial Lending

Douglas L. Blay

Vice President, Commercial Lending

Thomas K. Cargo

Vice President, Commercial Lending

Karen L. Duffy

Vice President, Kent Office Manager

Robert S. Standardi

Vice President, Controller

Tracy L. Cettomai

Assistant Vice President, Consumer Lending

Grace H. Beers

Compliance Officer

Thomas M. Biltz

Loan Operations Officer

Pamela M. England

Marketing Officer

Shelly K. Feciuch

Loan Operations Officer

Marissa L. Platt

Mortgage Loan Underwriting Officer

Michelle A. Spellman

Operations Officer

