

CNB FINANCIAL CORP/PA  
Form 10-Q  
May 07, 2010  
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, 2010

or

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

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

Commission File Number 0-13396

**CNB FINANCIAL CORPORATION**

(Exact name of registrant as specified in its charter)

**Pennsylvania**  
(State or other jurisdiction of  
incorporation or organization)

**25-1450605**  
(I.R.S. Employer  
Identification No.)

**1 South Second Street**

**P.O. Box 42**

**Clearfield, Pennsylvania 16830**

(Address of principal executive offices)

**Registrant's telephone number, including area code, (814) 765-9621**

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 periods 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 (section 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, or a non-accelerated filer, or a smaller reporting company. See definitions 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  Smaller reporting company

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

The number of shares outstanding of the issuer's common stock as of May 3, 2010

COMMON STOCK: \$0 PAR VALUE, 8,797,287 SHARES

**Table of Contents**

**INDEX**

**PART I.  
FINANCIAL INFORMATION**

**Sequential**

**Page Number**

ITEM 1 Financial Statements (unaudited)

PAGE 3. Consolidated Balance Sheets March 31, 2010 and December 31, 2009

PAGE 4. Consolidated Statements of Income Three months ended March 31, 2010 and 2009

PAGE 5. Consolidated Statements of Comprehensive Income Three months ended March 31, 2010 and 2009

PAGE 6. Consolidated Statements of Cash Flows Three months ended March 31, 2010 and 2009

PAGE 7. Notes to Consolidated Financial Statements

ITEM 2 Management's Discussion and Analysis

PAGE 20. Management's Discussion and Analysis of Financial Condition and Results of Operations

ITEM 3 Quantitative and Qualitative Disclosures

PAGE 30. Quantitative and Qualitative Disclosures about Market Risk

ITEM 4 Controls and Procedures

PAGE 31. Controls and Procedures

**PART II.  
OTHER INFORMATION**

PAGE 32. ITEM 1 Legal Proceedings

PAGE 32. ITEM 1A Risk Factors

PAGE 32. ITEM 2 Unregistered Sales of Equity Securities and Use of Proceeds

PAGE 32. ITEM 3 Defaults Upon Senior Securities

PAGE 32. ITEM 4 [Removed and Reserved]

PAGE 32. ITEM 5 Other Information

PAGE 32. ITEM 6 Exhibits

PAGE 33. Signatures

**Table of Contents**

**CNB FINANCIAL CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**

Dollars in thousands

	(unaudited) March 31, 2010	December 31, 2009
<b><u>ASSETS</u></b>		
Cash and due from banks	\$ 52,883	\$ 19,959
Interest bearing deposits with other banks	2,460	2,399
Total cash and cash equivalents	55,343	22,358
Interest bearing time deposits with other banks	5,164	6,388
Securities available for sale	389,519	345,415
Trading securities	1,037	955
Loans held for sale	3,321	1,218
Loans	714,033	718,022
Less: unearned discount	(2,651)	(2,880)
Less: allowance for loan losses	(9,914)	(9,795)
Net loans	701,468	705,347
FHLB and other equity interests	6,824	6,907
Premises and equipment, net	24,321	23,355
Bank owned life insurance	19,142	16,440
Mortgage servicing rights	940	876
Goodwill	10,821	10,821
Other intangible assets	60	85
Accrued interest receivable and other assets	21,854	21,426
<b>TOTAL</b>	<b>\$ 1,239,814</b>	<b>\$ 1,161,591</b>
<b><u>LIABILITIES AND SHAREHOLDERS' EQUITY</u></b>		
Non-interest bearing deposits	\$ 115,801	\$ 116,310
Interest bearing deposits	916,691	840,548
Total deposits	1,032,492	956,858
Treasury, tax and loan borrowings	1,149	1,380
FHLB and other borrowings	99,975	100,003
Subordinated debentures	20,620	20,620
Accrued interest payable and other liabilities	13,694	13,321
Total liabilities	1,167,930	1,092,182
Common stock, \$0 par value; authorized 50,000,000 shares; issued 9,233,750 shares		
Additional paid in capital	12,525	12,631
Retained earnings	69,387	68,676

Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

Treasury stock, at cost (434,007 shares at March 31, 2010 and 472,477 shares at December 31, 2009)	(6,476)	(7,023)
Accumulated other comprehensive loss	(3,552)	(4,875)

Total shareholders equity	71,884	69,409
---------------------------	--------	--------

TOTAL	\$ 1,239,814	\$ 1,161,591
-------	--------------	--------------

See Notes to Consolidated Financial Statements

**Table of Contents****CNB FINANCIAL CORPORATION****CONSOLIDATED STATEMENTS OF INCOME (unaudited)**

Dollars in thousands, except per share data

	<b>Three months ended March 31,</b>	
	<b>2010</b>	<b>2009</b>
<b>INTEREST AND DIVIDEND INCOME:</b>		
Loans including fees	\$ 11,312	\$ 11,430
Deposits with banks	32	72
Securities:		
Taxable	2,340	1,906
Tax-exempt	476	537
Dividends	8	10
 Total interest and dividend income	 14,168	 13,955
<b>INTEREST EXPENSE:</b>		
Deposits	3,440	3,331
Borrowed funds	1,098	1,191
Subordinated debentures	189	230
 Total interest expense	 4,727	 4,752
 NET INTEREST INCOME	 9,441	 9,203
PROVISION FOR LOAN LOSSES	585	862
 NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	 8,856	 8,341
<b>NON-INTEREST INCOME:</b>		
Trust and asset management fees	246	210
Service charges on deposit accounts	945	933
Other service charges and fees	301	349
Net realized and unrealized gains (losses) on securities for which fair value was elected	82	(151)
Mortgage banking	201	153
Bank owned life insurance	202	180
Wealth management	149	160
Other	260	133
	2,386	1,967
Total other-than-temporary impairment losses on available-for-sale securities	(834)	
Less portion of loss recognized in other comprehensive income (loss)	50	
Net impairment losses recognized in earnings	(784)	
Net realized gains (losses) on available-for-sale securities	432	(16)
Net impairment losses recognized in earnings and realized gains (losses) on available-for-sale securities	(352)	(16)

Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

Total non-interest income	2,034	1,951
<b>NON-INTEREST EXPENSES:</b>		
Salaries and benefits	3,977	3,565
Net occupancy expense of premises	1,135	1,104
FDIC insurance premiums	389	273
Amortization of intangibles	25	25
Other	2,563	2,392
Total non-interest expenses	8,089	7,359
INCOME BEFORE INCOME TAXES	2,801	2,933
INCOME TAX EXPENSE	641	707
NET INCOME	\$ 2,160	\$ 2,226
<b>EARNINGS PER SHARE:</b>		
Basic	\$ 0.25	\$ 0.26
Diluted	\$ 0.25	\$ 0.26
<b>DIVIDENDS PER SHARE,</b>		
Cash dividends per share	\$ 0.165	\$ 0.165

See Notes to Consolidated Financial Statements

**Table of Contents****CNB FINANCIAL CORPORATION****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (unaudited)****Dollars in thousands**

	<b>Three months ended March 31,</b>	
	<b>2010</b>	<b>2009</b>
<b>NET INCOME</b>	<b>\$ 2,160</b>	<b>\$ 2,226</b>
Other comprehensive income (loss), net of tax:		
Change in fair value of interest rate swap agreement designated as a cash flow hedge, net of tax of \$32 and (\$13), respectively	(59)	23
Net change in unrealized gains (losses) on securities available for sale:		
Unrealized losses on other-than-temporarily impaired securities available for sale:		
Unrealized losses arising during the period, net of tax of \$17	(33)	
Reclassification adjustment for losses included in net income, net of tax of (\$274)	510	
	477	
Unrealized gains (losses) on other securities available for sale:		
Unrealized gains (losses) arising during the period, net of tax of (\$639) and \$629, respectively	1,186	(1,173)
Reclassification adjustment for accumulated (gains) losses included in net income, net of tax of \$151 and (\$5), respectively	(281)	11
	905	(1,162)
Other comprehensive income (loss)	1,323	(1,139)
<b>COMPREHENSIVE INCOME</b>	<b>\$ 3,483</b>	<b>\$ 1,087</b>

See Notes to Consolidated Financial Statements



**Table of Contents****CNB FINANCIAL CORPORATION****CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)**

Dollars in thousands

	Three months ended March 31,	
	2010	2009
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$ 2,160	\$ 2,226
Adjustments to reconcile net income to net cash provided by operations:		
Provision for loan losses	585	862
Depreciation and amortization	509	501
Amortization, accretion and deferred loan fees and costs	491	205
Net impairment losses recognized in earnings and realized gains (losses) on available-for-sale securities	352	16
Net realized and unrealized (gains) losses on securities for which fair value was elected	(82)	151
Gain on sale of loans	(169)	(122)
Net gains on dispositions of premises and equipment and foreclosed assets	(23)	
Proceeds from sale of loans	3,695	10,241
Origination of loans held for sale	(5,750)	(10,177)
Increase in bank owned life insurance	(202)	(180)
Stock-based compensation expense	77	25
Changes in:		
Accrued interest receivable and other assets	(938)	945
Accrued interest payable and other liabilities	(232)	450
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>473</b>	<b>5,143</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Net decrease in interest bearing time deposits with other banks	1,224	574
Proceeds from maturities, prepayments and calls of securities	18,822	20,514
Proceeds from sales of securities	26,970	32,012
Purchase of securities	(88,643)	(52,071)
Loan origination and payments, net	3,086	(6,235)
Purchase of bank owned life insurance	(2,500)	
Redemption (purchase) of FHLB and other equity interests	83	(1,036)
Purchase of premises and equipment	(879)	(342)
Proceeds from the sale of premises and equipment and foreclosed assets	82	
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(41,755)</b>	<b>(6,584)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net change in:		
Checking, money market and savings accounts	50,550	27,345
Certificates of deposit	25,084	(17,250)
Proceeds from sale of treasury stock	299	288
Proceeds from exercise of stock options	42	17
Cash dividends paid	(1,449)	(1,422)
Repayment of long-term borrowings	(28)	(23)
Net change in short-term borrowings	(231)	242

Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

NET CASH PROVIDED BY FINANCING ACTIVITIES	74,267	9,197
NET INCREASE IN CASH AND CASH EQUIVALENTS	32,985	7,756
CASH AND CASH EQUIVALENTS, Beginning	22,358	31,256
CASH AND CASH EQUIVALENTS, Ending	\$ 55,343	\$ 39,012
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>		
Cash paid (refunded) during the period for:		
Interest	\$ 4,760	\$ 4,923
Income taxes	\$ 370	\$ (573)
<b>SUPPLEMENTAL NONCASH DISCLOSURES:</b>		
Transfers to other real estate owned	\$ 238	\$ 14
Grant of restricted stock awards from treasury stock	\$ 233	\$ 5

See Notes to Consolidated Financial Statements

**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(UNAUDITED)****BASIS OF PRESENTATION**

The accompanying consolidated financial statements have been prepared pursuant to rules and regulations of the Securities and Exchange Commission (SEC) and in compliance with accounting principles generally accepted in the United States of America. Because this report is based on an interim period, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted.

In the opinion of management of the registrant, the accompanying consolidated financial statements as of March 31, 2010 and for the three months ended March 31, 2010 and 2009 include all adjustments, consisting of only normal recurring adjustments, necessary for a fair presentation of the financial condition and the results of operations for the period. The financial performance reported for CNB Financial Corporation (the Corporation) for the three months ended March 31, 2010 is not necessarily indicative of the results to be expected for the full year. This information should be read in conjunction with the Corporation's Form 10-K for the period ended December 31, 2009.

**STOCK COMPENSATION**

The Corporation has a stock incentive plan for key employees and independent directors. The Stock incentive plan, which is administered by a committee of the Board of Directors, provides for up to 500,000 shares of common stock in the form of nonqualified options or restricted stock. For key employees, the plan vesting is one-fourth of the granted options or restricted stock per year beginning one year after the grant date, with 100% vested on the fourth anniversary of the grant. For independent directors, the vesting schedule is one-third of the granted options per year beginning one year after the grant date, with 100% vested on the third anniversary of the grant.

At March 31, 2010, there was no unrecognized compensation cost related to nonvested stock options granted under this plan, and no stock options were granted during the three or nine months periods then ended.

Compensation expense for the restricted stock awards is recognized over the requisite service period noted above based on the fair value of the shares at the date of grant. Unearned restricted stock awards are recorded as a reduction of shareholders' equity until earned. Compensation expense resulting from these restricted stock awards was \$77,000 and \$25,000 for the three months ended March 31, 2010 and 2009, respectively. As of March 31, 2010, there was \$510,000 of total unrecognized compensation cost related to unvested restricted stock awards.

A summary of changes in unvested restricted stock awards for the three months ended March 31, 2010 follows:

	Shares	Weighted Average Grant Date Fair Value
Nonvested at beginning of period	30,144	\$ 14.83
Granted	16,500	15.00
Vested	(9,810)	14.06
Forfeited		
Nonvested at end of period	36,834	\$ 15.11

---

**Table of Contents**

**CNB FINANCIAL CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(UNAUDITED)**

**FAIR VALUE**

***Fair Value Option***

Management elected to adopt the fair value option for its investment in perpetual preferred equity securities issued by the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation as well as its investment in certain other equity securities. Management elected the fair value option for these securities to provide financial statement users with greater visibility into the Corporation's financial instruments that do not have a defined maturity date.

Fair value changes attributable to unrealized gains (losses) that were included in earnings for the three months ended March 31, 2010 and 2009 were \$82,000 and (\$151,000), respectively. There were no sales of securities for which the fair value option was elected during the three months ended March 31, 2010 and 2009.

Dividend income is recorded based on cash dividends and comprises the Dividends line item in the accompanying consolidated statement of income. Dividend income was \$8,000 and \$10,000 for the three months ended March 31, 2010 and 2009, respectively.

***Fair Value Measurement***

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. A fair value hierarchy has also been established which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following three levels of inputs are used to measure fair value:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The fair values of most trading securities and securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs). The fair values of certain mortgage-backed securities and one corporate bond classified as available for sale have been determined by using Level 3 inputs. The Corporation has engaged valuation experts to price these securities using proprietary models, which incorporate assumptions that market participants would use in pricing the securities, including bid/ask spreads and liquidity and credit premiums.

Trust preferred securities which are issued by financial institutions and insurance companies are priced using Level 3 inputs. The decline in the level of observable inputs and market activity in this class of investments by the measurement date has been significant and resulted in unreliable external pricing. Broker pricing and bid/ask spreads, when available, vary widely, and the once active market has become comparatively inactive.

The Corporation engaged a third party consultant who has developed a model for pricing these securities. Information such as historical and current performance of the underlying collateral, deferral and default rates, collateral coverage ratios, break in yield calculations, cash flow

## Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

projections, liquidity and credit premiums required by a market participant, and financial trend analysis with respect to the individual issuing financial institutions and insurance companies are utilized in determining individual security valuations. Due to the current market conditions as well as the limited trading activity of these securities, the market value of the securities is highly sensitive to assumption changes and market volatility.

**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(UNAUDITED)

The Corporation's derivative instrument is an interest rate swap that trades in liquid markets. As such, significant fair value inputs can generally be verified and do not typically involve significant management judgments (Level 2 inputs).

The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

Assets and liabilities measured at fair value on a recurring basis are as follows at March 31, 2010 and December 31, 2009:

Description	Total	Fair Value Measurements at March 31, 2010 Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Other Inputs (Level 3) Unobservable
<b>Assets:</b>				
<b>Securities Available For Sale:</b>				
U.S. Treasury	\$ 10,264	\$	\$ 10,264	\$
U.S. Government sponsored entities States and political subdivisions	138,969 61,710	12,030 10,248	126,939 51,462	
Residential mortgage and asset backed Corporate notes and bonds	150,986 10,996	15,910	134,616 9,636	460 1,360
Pooled trust preferred Pooled SBA	1,894 13,003			1,894
Other securities	1,697	1,697		
<b>Total Securities Available For Sale</b>	<b>\$ 389,519</b>	<b>\$ 50,983</b>	<b>\$ 334,822</b>	<b>\$ 3,714</b>
<b>Trading Securities:</b>				
Equity securities financial services	\$ 496	\$ 496	\$	\$
Equity securities health care	161	161		
Equity securities energy	118	118		
Equity securities U.S. Government sponsored entities	98	98		
Equity securities industrials	109	109		
Equity securities utilities	55	55		
<b>Total Trading Securities</b>	<b>\$ 1,037</b>	<b>\$ 1,037</b>	<b>\$</b>	<b>\$</b>
<b>Liabilities Interest rate swap</b>	<b>\$ (792)</b>	<b>\$</b>	<b>\$ (792)</b>	<b>\$</b>

**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(UNAUDITED)

Description	Total	Fair Value Measurements at December 31, 2009 Using Quoted Prices		
		in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets:</b>				
<b>Securities Available For Sale:</b>				
U.S. Treasury	\$ 10,269	\$	\$ 10,269	\$
U.S. Government sponsored entities	106,961	30,643	76,318	
States and political subdivisions	56,561	3,273	53,288	
Residential mortgage and asset backed	145,400	5,625	139,272	503
Corporate notes and bonds	13,631		13,631	
Pooled trust preferred	1,909			1,909
Pooled SBA	8,989	5,017	3,972	
Other securities	1,695	1,695		
<b>Total Securities Available For Sale</b>	<b>\$ 345,415</b>	<b>\$ 46,253</b>	<b>\$ 296,750</b>	<b>\$ 2,412</b>
<b>Trading Securities:</b>				
Equity securities financial services	\$ 440	\$ 440	\$	\$
Equity securities health care	164	164		
Equity securities energy	109	109		
Equity securities U.S. Government sponsored entities	102	102		
Equity securities industrials	81	81		
Equity securities other	59	59		
<b>Total Trading Securities</b>	<b>\$ 955</b>	<b>\$ 955</b>	<b>\$</b>	<b>\$</b>
Liabilities Interest rate swap	\$ (701)	\$	\$ (701)	\$

The table below presents a reconciliation and income statement classification of gains and losses for all securities available for sale measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended March 31, 2010 and the year ended December 31, 2009:

	Quarter ended March 31, 2010			Year ended December 31, 2009	
	Residential mortgage and asset backed	Corporate notes and bonds	Pooled trust preferred	Residential mortgage and asset backed	Pooled trust preferred
Beginning balance	\$ 503	\$	\$ 1,909	\$ 4,318	\$ 3,079
Transfers into Level 3 (a) (c)		1,040			

Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

Transfers out of Level 3 (b) (c)				(1,415)	
Total gains or losses (realized/unrealized):					
Included in earnings			(784)		(2,415)
Included in other comprehensive income	320		769		1,318
Purchases, issuances, sales, and settlements:					(73)
Sales				(2,400)	
Settlements	(43)				
Ending balance	\$ 460	\$ 1,360	\$ 1,894	\$ 503	\$ 1,909



**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(UNAUDITED)

- (a) Transferred from Level 2 to Level 3 because of lack of observable market data due to decrease in market activity for this security.  
 (b) Transferred from Level 3 to Level 2 since observable market data became available to value the security.  
 (c) The Corporation's policy is to recognize transfers in and transfers out as of the actual date of the event or change in circumstances that caused the transfer.

The unrealized losses reported in earnings for the three months ended March 31, 2010 and for the year ended December 31, 2009 for Level 3 assets that are still held at March 31, 2010 and December 31, 2009 relate to pooled trust preferred securities deemed to be other-than-temporarily impaired.

During the quarter ended March 31, 2010, the following available for sale securities reported as Level 1 securities as of the beginning of the period were transferred to the Level 2 category:

Description	Fair value on date of transfer
U.S. Government sponsored entities	\$ 28,643
States and political subdivisions	3,273
Residential mortgage and asset backed	5,384
Total	\$ 37,300

These securities were transferred from the Level 1 category to the Level 2 category since there were no longer quoted prices for identical assets in active markets that the Corporation had the ability to access. There were no transfers of securities from the Level 2 category to the Level 1 category during the quarter ended March 31, 2010.

Assets and liabilities measured at fair value on a non-recurring basis are as follows at March 31, 2010 and December 31, 2009:

Description	Total	Fair Value Measurements at March 31, 2010 Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Assets, Impaired loans	\$ 11,440	\$	\$	\$ 11,440

Fair Value Measurements at December 31, 2009 Using		
Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)

Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

Description	Total	Identical Assets (Level 1)	(Level 2)	(Level 3)
Assets,				
Impaired loans	\$ 9,471	\$	\$	\$ 9,471

Impaired loans, which are measured for impairment using the fair value of collateral for collateral dependent loans, had a principal balance of \$13,133, with a valuation allowance of \$1,693 as of March 31, 2010, resulting in an additional provision for loan losses of \$384 for the three months then ended. Impaired loans had a principal balance of \$10,880, with a valuation allowance of \$1,409 as of December 31, 2009, resulting in an additional provision for loan losses of \$730 for the year then ended.

***Fair Value of Financial Instruments***

Carrying amount is the estimated fair value for cash and cash equivalents, accrued interest receivable and payable, demand deposits, other borrowings, and variable rate loans, deposits or borrowings that reprice frequently and fully. For fixed rate

**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(UNAUDITED)

loans or deposits and for variable rate loans or deposits with infrequent repricing or repricing limits, fair value is based on discounted cash flows using current market rates applied to the estimated life and credit risk. Fair value of loans held for sale is based on market quotes. Fair value of debt is based on current rates for similar financing. It is not practical to determine the fair value of FHLB stock and other equity interests due to restrictions placed on the transferability of these instruments. The fair value of off balance sheet items is based on the current fees or cost that would be charged to enter into or terminate such arrangements. The fair value of off balance sheet items is not material.

While these estimates of fair value are based on management's judgment of the most appropriate factors as of the balance sheet date, there is no assurance that the estimated fair values would have been realized if the assets had been disposed of or the liabilities settled at that date, since market values may differ depending on various circumstances. The estimated fair values would also not apply to subsequent dates.

In addition, other assets and liabilities that are not financial instruments, such as premises and equipment, are not included in the disclosures. Also, non-financial instruments typically not recognized on the balance sheet may have value but are not included in the fair value disclosures. These include, among other items, the estimated earnings power of core deposits, the earnings potential of trust accounts, the trained workforce, customer goodwill, and similar items.

The following table presents the carrying amount and fair value of financial instruments at March 31, 2010 and December 31, 2009:

	March 31, 2010		December 31, 2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>ASSETS</b>				
Cash and cash equivalents	\$ 55,343	\$ 55,343	\$ 22,358	\$ 22,358
Interest bearing time deposits with other banks	5,164	5,196	6,388	6,565
Securities available for sale	389,519	389,519	345,415	345,415
Trading securities	1,037	1,037	955	955
Loans held for sale	3,321	3,349	1,218	1,228
Net loans	701,468	722,200	705,347	728,074
FHLB and other equity interests	6,824	N/A	6,907	N/A
Accrued interest receivable	5,229	5,229	4,728	4,728
<b>LIABILITIES</b>				
Deposits	\$ (1,032,492)	\$ (1,014,935)	\$ (956,858)	\$ (956,231)
FHLB, Treasury, tax and loan, and other borrowings	(101,124)	(104,773)	(101,383)	(109,753)
Subordinated debentures	(20,620)	(10,536)	(20,620)	(10,609)
Interest rate swap	(792)	(792)	(701)	(701)
Accrued interest payable	(1,873)	(1,873)	(1,906)	(1,906)

**SECURITIES**

Securities available for sale at March 31, 2010 and December 31, 2009 were as follows (in thousands):

	Amortized Cost	March 31, 2010 Unrealized		Fair Value	Amortized Cost	December 31, 2009 Unrealized		Fair Value
		Gains	Losses			Gains	Losses	
U.S. Treasury	\$ 10,249	\$ 16	\$ (1)	\$ 10,264	\$ 10,288	\$ 5	\$ (24)	\$ 10,269

Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

U.S. Gov t sponsored entities	139,846	238	(1,115)	138,969	107,615	94	(748)	106,961
State & political subdivisions	60,636	1,130	(56)	61,710	55,710	991	(140)	56,561
Residential mortgage & asset backed	149,915	1,426	(355)	150,986	144,878	1,188	(666)	145,400
Corporate notes & bonds	15,329		(4,333)	10,996	18,713		(5,082)	13,631
Pooled trust preferred	3,810	35	(1,951)	1,894	4,594		(2,685)	1,909
Pooled SBA	12,887	116		13,003	8,894	102	(7)	8,989
Other securities	1,670	29	(2)	1,697	1,670	28	(3)	1,695
<b>Total</b>	<b>\$ 394,342</b>	<b>\$ 2,990</b>	<b>\$ (7,813)</b>	<b>\$ 389,519</b>	<b>\$ 352,362</b>	<b>\$ 2,408</b>	<b>\$ (9,355)</b>	<b>\$ 345,415</b>

**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(UNAUDITED)

At March 31, 2010, there were no holdings of securities of any one issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of shareholders' equity.

Securities with unrealized losses at March 31, 2010 and December 31, 2009, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, are as follows (in thousands):

March 31, 2010	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Description of Securities						
U.S. Treasury	\$ 1,014	\$ (1)	\$	\$	\$ 1,014	\$ (1)
U.S. Gov't sponsored entities	84,436	(1,114)	1,000	(1)	85,436	(1,115)
State & political subdivisions	3,985	(29)	2,481	(27)	6,466	(56)
Residential mortgage & asset backed	40,384	(353)	2,502	(2)	42,886	(355)
Corporate notes & bonds			10,996	(4,333)	10,996	(4,333)
Pooled trust preferred			704	(1,951)	704	(1,951)
Pooled SBA						
Other securities			147	(2)	147	(2)
	\$ 129,819	\$ (1,497)	\$ 17,830	\$ (6,316)	\$ 147,649	\$ (7,813)

December 31, 2009	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Description of Securities						
U.S. Treasury	\$ 6,201	\$ (24)	\$	\$	\$ 6,201	\$ (24)
U.S. Gov't sponsored entities	49,420	(748)			49,420	(748)
State & political subdivisions	9,865	(103)	3,710	(37)	13,575	(140)
Residential mortgage & asset backed	68,293	(644)	3,198	(22)	71,491	(666)
Corporate notes & bonds			13,631	(5,082)	13,631	(5,082)
Pooled trust preferred			1,909	(2,685)	1,909	(2,685)
Pooled SBA	1,009	(7)			1,009	(7)
Other securities			146	(3)	146	(3)
	\$ 134,788	\$ (1,526)	\$ 22,594	\$ (7,829)	\$ 157,382	\$ (9,355)

The Corporation evaluates securities for other-than-temporary impairment on a quarterly basis, or more frequently when economic or market conditions warrant such an evaluation.

At March 31, 2010, management evaluated the structured pooled trust preferred securities for other-than-temporary impairment by estimating the cash flows expected to be received from each security within the collateral pool, taking into account estimated levels of deferrals and defaults by the underlying issuers, and discounting those cash flows at the appropriate accounting yield. Management also assumed that all issuers in deferral will default prior to their next payment date. Trust preferred collateral is deeply subordinated within issuers' capital structures, so large recoveries are unlikely. Accordingly, management assumed 10% recoveries on bank collateral and none on collateral issued by other companies. Due to the current crisis in the U.S. economy, management also added a baseline default rate of 2% annually for the next two years.

to our default projections for specific issuers. This percentage represents the peak, post-war bank default rate that occurred at the height of the savings and loan crisis, which we believe is an accurate proxy for the current environment. Within the next two years, management expects that credit markets will normalize and that banks with the financial strength to survive will default at a .36% average annual rate, which represents Moody's idealized default probability for BBB corporate credits, and is in line with historical bank failure rates.

Using this methodology, four of the Corporation's structured pooled trust preferred securities are deemed to be other-than-temporarily impaired. An impairment loss for the entire cost basis of two of these securities was recognized in earnings prior to 2010, and an impairment loss was recognized in earnings for one of these securities during the quarter ended March 31, 2010. The Corporation separated the other-than-temporary impairment related to these structured pooled trust preferred securities into (a) the amount of the total impairment related to credit loss, which is recognized in the income statement, and (b) the amount of the total impairment related to all other factors, which is recognized in other comprehensive income. The

**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(UNAUDITED)**

Corporation measured the credit loss component of other-than-temporary impairment based on the difference between the cost basis and the present value of cash flows expected to be collected. The amount of other-than-temporary impairment recognized in income and in total comprehensive income for the three months ended March 31, 2010 was \$784,000 and (\$50,000), respectively.

The following table provides detailed information related to the Corporation's structured pooled trust preferred securities as of and for the three months ended March 31, 2010:

	Adjusted Amortized Cost	Unrealized Gain (Loss)	Fair Value	Credit Losses Realized in Earnings
ALESCO Preferred Funding V, Ltd.	\$ 1,240	\$ (760)	\$ 480	\$
ALESCO Preferred Funding XII, Ltd.	429	(392)	37	784
ALESCO Preferred Funding XVII, Ltd.				
Preferred Term Securities XVI, Ltd.	986	(799)	187	
US Capital Funding VI, Ltd.				
MM Community Funding II, Ltd.	1,155	35	1,190	
<b>Total</b>	<b>\$ 3,810</b>	<b>\$ (1,916)</b>	<b>\$ 1,894</b>	<b>\$ 784</b>

A roll-forward of the other-than-temporary impairment amount related to credit losses for the three months ended March 31, 2010 is as follows:

Balance of credit losses on debt securities for which a portion of other-than-temporary impairment was recognized in other comprehensive income, beginning of period	\$ 1,415
Additional credit loss for which other-than-temporary impairment was not previously recognized	784
<b>Balance of credit losses on debt securities for which a portion of other-than-temporary impairment was recognized in other comprehensive income, end of period</b>	<b>\$ 2,199</b>

At March 31, 2010, approximately 25% of the total unrealized losses relate to structured pooled trust preferred securities, primarily from issuers in the financial services industry, which are not currently trading in an active, open market with readily observable prices. As a result, these securities were classified within Level 3 of the valuation hierarchy. The fair values of these securities have been calculated using a discounted cash flow model and market liquidity premium. With the current market conditions, the assumptions used to determine the fair value of Level 3 securities has greater subjectivity due to the lack of observable market transactions. The fair values of these securities have declined due to the fact that subsequent offerings of similar securities pay a higher market rate of return. This higher rate of return reflects the increased credit and liquidity risks in the marketplace. Except as described above, based on management's evaluation of the structured pooled trust preferred securities, the present value of the projected cash flows is sufficient for full repayment of the amortized cost of the securities and, therefore, it is believed that the decline in fair value is temporary due to current market conditions. However, without recovery of these securities, other-than-temporary impairments may occur in future periods.

For all of the securities that comprise corporate notes and bonds, management monitors publicly available financial information such as filings with the Securities and Exchange Commission in order to evaluate the securities for other-than-temporary impairment. For financial institution issuers, management also monitors information from quarterly call report filings that are used to generate Uniform Bank Performance Reports.

## Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

When reviewing this information, management considers the financial condition and near term prospects of the issuer and whether downgrades by bond rating agencies have occurred. Management also considers the length of time and extent to which fair value has been less than cost and the intent and ability of the Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.



**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(UNAUDITED)**

As of March 31, 2010 and December 31, 2009, management concluded that the previously mentioned securities were not other-than-temporarily impaired for the following reasons:

There is no indication of any significant deterioration of the creditworthiness of the institutions that issued the securities.

The unrealized losses are predominantly attributable to liquidity disruptions within the credit markets and the generally stressed condition of the financial services industry.

All contractual interest payments on the securities have been received as scheduled, and no information has come to management's attention through the processes previously described which would lead to a conclusion that future contractual payments will not be received timely.

The Corporation does not intend to sell and it is not more likely than not that it will be required to sell the securities in an unrealized loss position before recovery of its amortized cost basis.

Information pertaining to security sales is as follows:

	<b>Proceeds</b>	<b>Gross Gains</b>	<b>Gross Losses</b>
Three months ended March 31, 2010	\$ 26,970	\$ 446	\$ (14)

The following is a schedule of the contractual maturity of securities available for sale, excluding equity securities, at March 31, 2010 and December 31, 2009:

	<b>March 31, 2010</b>		<b>December 31, 2009</b>	
	<b>Amortized Cost</b>	<b>Fair Value</b>	<b>Amortized Cost</b>	<b>Fair Value</b>
1 year or less	\$ 37,533	\$ 37,393	\$ 27,183	\$ 27,175
1 year 5 years	72,650	72,872	74,532	74,608
5 years 10 years	86,915	86,610	61,617	61,077
After 10 years	45,659	39,961	42,482	35,460
	242,757	236,836	205,814	198,320
Residential mortgage & asset backed securities	149,915	150,986	144,878	145,400
<b>Total debt securities</b>	<b>\$ 392,672</b>	<b>\$ 387,822</b>	<b>\$ 350,692</b>	<b>\$ 343,720</b>

Mortgage and asset backed securities are not due at a single date; periodic payments are received based on the payment patterns of the underlying collateral.

**LOANS**

Total loans at March 31, 2010 and December 31, 2009 are summarized as follows:

	<b>March 31, 2010</b>	<b>December 31, 2009</b>
Commercial, industrial, and agricultural	\$ 240,457	\$ 240,357
Residential mortgage	225,996	225,845
Commercial mortgage	192,551	194,718
Consumer and other	55,029	57,102
	<b>\$ 714,033</b>	<b>\$ 718,022</b>

At March 31, 2010 and December 31, 2009, net unamortized loan costs and fees of (\$387) and (\$417), respectively, have been included in the carrying value of loans.

**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(UNAUDITED)

The Corporation's outstanding loans and related unfunded commitments are primarily concentrated within Central and Western Pennsylvania. The Bank attempts to limit concentrations within specific industries by utilizing dollar limitations to single industries or customers, and by entering into participation agreements with third parties. Collateral requirements are established based on management's assessment of the customer.

Deposit accounts that have overdrawn their current balance, known as overdrafts, are reclassified to loans. Overdrafts included in loans are \$376 at March 31, 2010 and \$391 at December 31, 2009.

Impaired loans are as follows at March 31, 2010 and December 31, 2009:

	March 31, 2010	December 31, 2009
Loans with no allocated allowance for loan losses	\$ 3,003	\$ 3,182
Loans with allocated allowance for loan losses	13,133	10,880
	\$ 16,136	\$ 14,062
Amount of the allowance for loan losses allocated	\$ 1,693	\$ 1,409

Average impaired loans outstanding during the quarter ended March 31, 2010 and the year ended December 31, 2009 were \$15,099 and \$10,812, respectively. Interest income recognized during impairment and cash basis interest income recognized was not material in any year presented.

Nonaccrual loans and loans past 90 days still on accrual at March 31, 2010 and December 31, 2009 are as follows:

	March 31, 2010	December 31, 2009
Loans past due over 90 days still on accrual	\$ 1,727	\$ 584
Nonaccrual loans	12,841	12,757

Nonaccrual loans and loans past 90 days still on accrual include impaired loans and smaller balance homogeneous loans, such as residential mortgage and consumer loans, that are collectively evaluated for impairment.

**FEDERAL HOME LOAN BANK (FHLB) STOCK**

As a member of the Federal Home Loan Bank of Pittsburgh ( FHLB ), the Corporation is required to purchase and hold stock in the FHLB to satisfy membership and borrowing requirements. This stock is restricted in that it can only be sold to the FHLB or to another member institution, and all sales of FHLB stock must be at par. As a result of these restrictions, FHLB stock is unlike other investment securities insofar as there is no trading market for FHLB stock and the transfer price is determined by FHLB membership rules and not by market participants.

As of March 31, 2010, the Corporation holds \$5,401 of stock in FHLB. In December 2008, the FHLB voluntarily suspended dividend payments on its stock, as well as the repurchase of excess stock from members. The FHLB cited a significant reduction in the level of core earnings

## Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

resulting from lower short-term interest rates, the increased cost of liquidity, and constrained access to the debt markets at attractive rates and maturities as the main reasons for the decision to suspend dividends and the repurchase of excess capital stock. The FHLB last paid a dividend in the third quarter of 2008.

**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(UNAUDITED)

FHLB stock is held as a long-term investment and its value is determined based on the ultimate recoverability of the par value. The Company evaluates impairment quarterly. The decision of whether impairment exists is a matter of judgment that reflects our view of the FHLB's long-term performance, which includes factors such as the following:

its operating performance;

the severity and duration of declines in the fair value of its net assets related to its capital stock amount;

its commitment to make payments required by law or regulation and the level of such payments in relation to its operating performance;

the impact of legislative and regulatory changes on the FHLB, and accordingly, on the members of FHLB; and

its liquidity and funding position

After evaluating all of these considerations, the Corporation concluded that the par value of its investment in FHLB stock will be recovered. Accordingly, no impairment charge was recorded on these securities in 2009. Our evaluation of the factors described above in future periods could result in the recognition of impairment charges on FHLB stock.

**DEPOSITS**

Total deposits at March 31, 2010 and December 31, 2009 are summarized as follows (in thousands):

	Percentage Change	March 31, 2010	December 31, 2009
Checking, non-interest bearing	(0.4)%	\$ 115,801	\$ 116,310
Checking, interest bearing	1.6%	248,163	244,218
Savings accounts	17.3%	320,210	273,096
Certificates of deposit	7.8%	348,318	323,234
	7.9%	\$ 1,032,492	\$ 956,858

**EARNINGS PER SHARE**

Basic earnings per share is computed by dividing net income by the weighted average number of shares outstanding during the applicable period, excluding outstanding participating securities. Diluted earnings per share is computed using the weighted average number of shares determined for the basic computation plus the dilutive effect of potential common shares issuable under certain stock compensation plans. For the three month period ended March 31, 2010 and 2009, 86,750 and 157,348 shares under option were excluded from the diluted earnings per

share calculations as they were anti-dilutive.

Unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and are included in the computation of earnings per share pursuant to the two-class method. The Corporation has determined that its outstanding non-vested stock awards are participating securities.

**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(UNAUDITED)

The computation of basic and diluted EPS is shown below (in thousands except per share data):

	<b>Three months ended March 31,</b>	
	<b>2010</b>	<b>2009</b>
Net income per consolidated statements of income	\$ 2,160	\$ 2,226
Net earnings allocated to participating securities	(9)	(5)
<b>Net earnings allocated to common stock</b>	<b>\$ 2,151</b>	<b>\$ 2,221</b>
<b>Basic earnings per common share computation:</b>		
Distributed earnings allocated to common stock	\$ 1,444	\$ 1,417
Undistributed earnings allocated to common stock	707	804
<b>Net earnings allocated to common stock</b>	<b>\$ 2,151</b>	<b>\$ 2,221</b>
Weighted average common shares outstanding, including shares considered participating securities	8,783	8,608
Less: Average participating securities	(34)	(17)
Weighted average shares	8,749	8,591
<b>Basic earnings per common share</b>	<b>\$ 0.25</b>	<b>\$ 0.26</b>
<b>Diluted earnings per common share computation:</b>		
<b>Net earnings allocated to common stock</b>	<b>\$ 2,151</b>	<b>\$ 2,221</b>
Weighted average common shares outstanding for basic earnings per common share	8,749	8,591
Add: Dilutive effects of assumed exercises of stock options	13	7
Weighted average shares and dilutive potential common shares	8,762	8,598
<b>Diluted earnings per common share</b>	<b>\$ 0.25</b>	<b>\$ 0.26</b>

**DERIVATIVE INSTRUMENTS**

The Corporation records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and the resulting designation. Derivatives used to hedge the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives used to

hedge the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges.

For derivatives designated as cash flow hedges, the effective portion of the changes in the fair value of the derivative is initially reported in other comprehensive income (outside of earnings) and subsequently reclassified into earnings when the hedged transaction affects earnings, and the ineffective portion of changes in the fair value of the derivative is recognized directly in earnings. The Corporation assesses the effectiveness of each hedging relationship by comparing the changes in cash flows of the derivative hedging instrument with the changes in cash flows of the designated hedged item or transaction.

On August 1, 2008, the Corporation executed an interest rate swap agreement with a 5 year term to hedge \$10 million of a subordinated note that was entered into by the Corporation during 2007 and elected cash flow hedge accounting for the agreement. The Corporation's objective in using this derivative is to add stability to interest expense and to manage its exposure to interest rate risk. The interest rate swap involves the receipt of variable-rate amounts in exchange for fixed-rate payments over the life of the agreement without exchange of the underlying notional amount. At March 31, 2010, the variable rate on the subordinated debt was 1.81% (LIBOR plus 155 basis points) and the Corporation was paying 5.84% (4.29% fixed rate plus 155 basis points).



**Table of Contents****CNB FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

(UNAUDITED)

As of March 31, 2010, no derivatives were designated as fair value hedges or hedges of net investments in foreign operations. Additionally, the Corporation does not use derivatives for trading or speculative purposes and currently does not have any derivatives that are not designated as hedges.

The following tables provide information about the amounts and locations of activity related to the interest rate swap designated as a cash flow hedge within the Corporation's consolidated balance sheet and statement of income as of and for the three months ended March 31, 2010 (in thousands):

As of March 31, 2010	Liability Derivative Balance Sheet	Fair Value
	Location	
Interest rate contract	Accrued interest payable and other liabilities	\$(792)

**For the Three Months**

Ended March 31, 2010	(a)	(b)	(c)	(d)	(e)
Interest rate contract		Interest expense		Other	
	\$(59)	subordinated debentures	(\$101)	income	\$

- (a) Amount of Gain or (Loss) Recognized in Other Comprehensive Loss on Derivative (Effective Portion), net of tax  
 (b) Location of Gain or (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion)  
 (c) Amount of Gain or (Loss) Reclassified from Accumulated Other Comprehensive Loss into Income (Effective Portion)  
 (d) Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)  
 (e) Amount of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)
- Amounts reported in accumulated other comprehensive loss related to the interest rate swap will be reclassified to interest expense as interest payments are made on the subordinated debentures. Such amounts reclassified from accumulated other comprehensive loss to interest expense in the next 12 months are expected to approximate \$403,000.

**RECENT ACCOUNTING PRONOUNCEMENTS**

In June 2009, the Financial Accounting Standards Board ( FASB ) amended previous guidance relating to transfers of financial assets and eliminates the concept of a qualifying special purpose entity. This guidance must be applied as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. This guidance must be applied to transfers occurring on or after the effective date. Additionally, on and after the effective date, the concept of a qualifying special-purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special-purpose entities should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance. The disclosure provisions were also amended and apply to transfers that occurred both before and after the effective date of this guidance. The adoption of this standard did not have a material effect on the Corporation's results of operations or financial position.

## Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

In June 2009, the FASB amended guidance for consolidation of variable interest entity guidance by replacing the quantitative-based risks and rewards calculation for determining which enterprise, if any, has a controlling financial interest in a variable interest entity with an approach focused on identifying which enterprise has the power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance and (1) the obligation to absorb

**Table of Contents**

**CNB FINANCIAL CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**(UNAUDITED)**

losses of the entity or (2) the right to receive benefits from the entity. Additional disclosures about an enterprise's involvement in variable interest entities are also required. This guidance is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Early adoption is prohibited. The adoption of this standard did not have a material effect on the Corporation's results of operations or financial position.

In January 2010, the FASB issued Accounting Standards Update No. 2010-4, Accounting for Various Topics, Technical Corrections to SEC Paragraphs. In addition, in February 2010, the FASB issued Accounting Standards Update No. 2010-8, Technical Corrections to Various Topics. These updates covered a wide variety of accounting matters, including subsequent events, goodwill, derivative financial instruments, and investments in limited partnerships. The most significant provisions of these updates were effective upon issuance and did not have a material effect on the Corporation's results of operations or financial position.

In January 2010, the FASB issued Accounting Standards Update No. 2010-6, Fair Value Measurements and Disclosures. This update requires new disclosures concerning transfers in and out of Level 1 and Level 2 securities within the fair value hierarchy and a more detailed reconciliation of activity in Level 3 securities. The update also provides amendments that clarify existing disclosures concerning the level of disaggregation in fair value disclosures, as well as disclosures about inputs and valuation techniques. Finally, the update includes conforming amendments to the guidance on employers' disclosures about postretirement benefit plan assets. The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this update did not have a material effect on the Corporation's results of operations or financial position.

In February 2010, the FASB issued Accounting Standards Update No. 2010-09, Subsequent Events. This update removes the requirement for an SEC filer to disclose a subsequent events evaluation date in both issued and revised financial statements. The update was effective on issuance and did not have a material effect on the Corporation's results of operations or financial position.

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

The following discussion and analysis of the consolidated financial statements of CNB Financial Corporation (the Corporation) is presented to provide insight into management's assessment of financial results. The Corporation's subsidiary CNB Bank (the Bank) provides financial services to individuals and businesses primarily within the west central Pennsylvania counties of Cambria, Clearfield, Centre, Elk, Jefferson and McKean. ERIEBANK, a division of CNB Bank, provides financial services to individuals and business in the northwestern Pennsylvania counties of Erie and Crawford. The Bank is subject to regulation, supervision and examination by the Pennsylvania State Department of Banking as well as the Federal Deposit Insurance Corporation. The financial condition and results of operations are not necessarily indicative of future performance. One of the Corporation's subsidiaries, CNB Securities Corporation, is incorporated in Delaware and currently maintains investments in debt and equity securities. County Reinsurance Company, also a subsidiary, is an Arizona Corporation, and provides credit life and disability insurance for customers of CNB Bank. CNB Insurance Agency, incorporated in Pennsylvania, provides for the sale of nonproprietary annuities and other insurance products. Holiday Financial Services Corporation (Holiday), incorporated in Pennsylvania, offers small balance unsecured loans and secured loans, primarily collateralized by automobiles and equipment, to borrowers with higher risk characteristics. Management's discussion and analysis should be read in conjunction with the audited consolidated financial statements and related notes.

Risk identification and management are essential elements for the successful management of the Corporation. In the normal course of business, the Corporation is subject to various types of risk, including interest rate, credit, and liquidity risk. These risks are controlled through policies and procedures established throughout the Corporation.

Interest rate risk is the sensitivity of net interest income and the market value of financial instruments to the direction and frequency of changes in interest rates. Interest rate risk results from various repricing frequencies and the maturity structure



## **Table of Contents**

of the financial instruments owned by the Corporation. The Corporation uses its asset/liability management policy and systems to control, monitor and manage interest rate risk.

Credit risk represents the possibility that a customer may not perform in accordance with contractual terms. Credit risk results from loans with customers and the purchase of securities. The Corporation manages credit risk by following an established credit policy and through a disciplined evaluation of the adequacy of the allowance for loan losses. Also, the investment policy limits the amount of credit risk that may be taken in the securities portfolio.

Liquidity risk represents the inability to generate or otherwise obtain funds at reasonable rates to satisfy commitments to borrowers and obligations to depositors. The Corporation has established guidelines within its asset liability management policy to manage liquidity risk. These guidelines include contingent funding alternatives.

## ***GENERAL OVERVIEW***

In September 2009, the Corporation expanded its ERIEBANK franchise by opening a temporary location in Meadville, Pennsylvania. Construction of a full service office is underway with opening expected in the second quarter of 2010. Management believes that our ERIEBANK division, along with our traditional CNB Bank market areas, should provide the Bank with moderate loan growth during 2010. Deposit growth was significant in 2009 and the first quarter of 2010 as a result of the Corporation's continued offering of competitive rates and growth of its ERIEBANK franchise. Deposit growth is expected to be moderate throughout the remainder of 2010 due to the continued historically low interest rate environment and the resulting adjustments that management made to certain deposit rates in the first quarter of 2010.

The Corporation has a total of eight offices within Holiday Financial Services Corporation. Although the consumer discount loan business is relatively new to the Corporation, management has made the necessary investments in experienced personnel and technology which has facilitated the growth of Holiday into a successful and profitable subsidiary of the Corporation.

While non-interest costs are expected to increase with the growth of the Corporation's banking and consumer discount loan franchises, these new ventures will continue to provide growth in earning assets as well as growth in relationships and enhanced non-interest income which we believe will more than offset these costs in 2010 and beyond. In addition, throughout 2009 and the first quarter of 2010, management conducted a cost management study covering all areas of non-interest expense. Cost savings as a result of this study were recognized in 2009 and the first quarter of 2010, with benefits continuing into subsequent periods.

The interest rate environment will continue to play an important role in the future earnings of the Corporation. We experienced some compression of our net interest margin in the first quarter of 2010 as a result of the current interest rate environment. However, management will continue to apply a disciplined approach to managing our balance sheet in these uncertain times. We have taken measures such as instituting rate floors on our commercial lines of credit and home equity lines as a result of the historic lows on various key interest rates such as the Prime Rate and 3-month LIBOR. In addition, we will implement strategies to effectively reduce our cost of funds. Due to our continued growth, non-interest income should be enhanced in several areas including trust income, service charges and other fees. While our business plan continues to focus on commercial lending, we also offer a full service approach to servicing the needs of high net worth individuals through our Private Banking groups in both our CNB Bank and ERIEBANK franchises.

Management concentrates on return on average equity and earnings per share evaluations, plus other methods to measure and direct the performance of the Corporation. While past results are not an indication of future earnings, we feel the Corporation is well positioned to sustain core earnings through the remainder of 2010.

## ***CASH AND CASH EQUIVALENTS***

Cash and cash equivalents totaled \$55.3 million at March 31, 2010 compared to \$22.4 million at December 31, 2009. Cash and cash equivalents will fluctuate based on the timing and amount of liquidity events that occur in the normal course of business. In March 2010, the Corporation had significant deposit growth that was not immediately invested in the securities portfolio. During the second quarter of 2010, management expects to reduce its cash and cash equivalents balance as a result of loan growth and new investments in the securities portfolio.

---

**Table of Contents**

We believe the liquidity needs of the Corporation are satisfied by the current balance of cash and cash equivalents, readily available access to traditional funding sources, and the portion of the investment and loan portfolios that mature within one year. These sources of funds will enable the Corporation to meet cash obligations and off-balance sheet commitments as they come due.

***SECURITIES***

Securities available for sale and trading securities have combined to increase \$44.2 million or 12.8% since December 31, 2009. The increase is primarily the result of purchases of securities issued by government sponsored entities and resulted from deposit growth not reinvested in loans.

The Corporation's structured pooled trust preferred securities currently do not trade in an active, open market with readily observable prices and are therefore classified within Level 3 of the valuation hierarchy. The fair value of these securities has been calculated using a discounted cash flow model and market liquidity premium. With the current market conditions, the assumptions used to determine the fair value of Level 3 securities has greater subjectivity due to the lack of observable market transactions. The fair values of these securities have declined due to the fact that the subsequent offerings of similar securities pay a higher market rate of return. This higher rate of return reflects the increased credit and liquidity risks in the marketplace.

When the structured pooled trust preferred securities were purchased, they were considered to be investment grade based on ratings assigned by Moody's. As a result of liquidity disruptions within the credit markets and the generally stressed conditions within the financial services industry, Moody's has downgraded the rating of these securities since they were purchased by the Corporation. As of March 31, 2010, the Corporation held three structured pooled trust preferred securities rated Ca by Moody's having an amortized cost of \$2,655,000 and fair value of \$704,000, and one structured pooled trust preferred security rated Baa2 by Moody's having an amortized cost of \$1,155,000 and fair value of \$1,190,000.

Based on our evaluation of certain structured pooled trust preferred securities, the present value of the projected cash flows was not sufficient for full repayment of the amortized cost for one of the securities resulting in total impairment charges realized during the first quarter of 2010 of \$784 thousand. For the other pooled trust preferred securities, the present value of the projected cash flows was sufficient for full repayment of amortized cost, and, therefore, it is believed the decline in fair value is temporary due to current market conditions. However, without recovery of these securities, other-than-temporary impairments may occur in future periods.

During the first quarter of 2010, management sold certain debt securities in an attempt to re-position a portion of its portfolio into lower risk-weighted assets. Proceeds from the sales were reinvested in other available for sale securities. Individually and in the aggregate, none of these sales resulted in the realization of a significant loss.

The Corporation generally buys into the market over time and does not attempt to time its transactions. In doing this, the highs and lows of the market are averaged into the portfolio and minimize the overall effect of different rate environments. We monitor the earnings performance and the effectiveness of the liquidity of the securities portfolio on a regular basis through Asset/Liability Committee (ALCO) meetings. The ALCO also reviews and manages interest rate risk for the Corporation. Through active balance sheet management and analysis of the securities portfolio, we maintain a sufficient level of liquidity to satisfy depositor requirements and various credit needs of our customers.

***LOANS***

The Corporation experienced a slight decrease in loans during the first quarter of 2010. Our lending is focused in the west, central and northwest Pennsylvania markets and consists principally of commercial and retail lending, which includes single family residential mortgages and other consumer loans. The Corporation views commercial lending as its competitive advantage and continues to focus on this area by hiring and retaining experienced loan officers and supporting them with quality credit analysis. The Corporation expects moderate loan demand throughout the remainder of 2010.

**Table of Contents****ALLOWANCE FOR LOAN LOSSES**

The allowance for loan losses is established by provisions for losses in the loan portfolio as well as overdrafts in deposit accounts. These provisions are charged against current income. Loans and overdrafts deemed not collectible are charged off against the allowance while any subsequent collections are recorded as recoveries and increase the allowance. The table below shows activity within the allowance account (in thousands):

	Three months ending March 31, 2010	Year ending December 31, 2009	Three months ending March 31, 2009
Balance at beginning of period	\$ 9,795	\$ 8,719	\$ 8,719
Charge-offs:			
Commercial, industrial, and agricultural	157	860	
Commercial mortgages	28	381	78
Residential mortgages	46	378	53
Consumer	268	1,723	435
Overdraft deposit accounts	42	269	51
	541	3,611	617
Recoveries:			
Commercial, industrial, and agricultural	2	2	
Commercial mortgages			
Residential mortgages	2	1	
Consumer	31	75	15
Overdraft deposit accounts	40	144	45
	75	222	60
Net charge-offs	(466)	(3,389)	(557)
Provision for loan losses	585	4,465	862
Balance at end of period	\$ 9,914	\$ 9,795	\$ 9,024
Loans, net of unearned	\$ 711,382	\$ 715,142	\$ 677,165
Allowance to net loans	1.39%	1.37%	1.33%
Net charge-offs to average loans	0.26%	0.49%	0.33%
Nonperforming assets	\$ 15,046	\$ 13,557	\$ 4,862
Nonperforming % of total assets	1.21%	1.17%	0.47%

The adequacy of the allowance for loan losses is subject to a formal analysis by the credit administrator of the Corporation. As part of the formal analysis, delinquencies and losses are monitored monthly. The loan portfolio is divided into several categories in order to better analyze the entire pool. First is a selection of classified loans that is given a specific reserve. The remaining loans are pooled, by category, into these segments:

*Reviewed*

Commercial, industrial, and agricultural

Commercial mortgages  
*Homogeneous*

Residential real estate

Consumer

Credit cards

Overdrafts



## Table of Contents

The reviewed loan pools are further segregated into four categories: special mention, substandard, doubtful, and unclassified. Historical loss factors are calculated for each pool excluding overdrafts based on the previous eight quarters of experience. The homogeneous pools are evaluated by analyzing the historical loss factors from the most previous quarter end and the two most recent year ends. The historical loss factors for both the reviewed and homogeneous pools are adjusted based on these six qualitative factors:

Levels of and trends in delinquencies, non-accrual loans, and classified loans

Trends in volume and terms of loans

Effects of any changes in lending policies and procedures

Experience, ability and depth of management

National and local economic trends and conditions

Concentrations of credit

The methodology described above was created using the experience of our credit administrator, guidance from the regulatory agencies, expertise of our loan review partner, and discussions with our peers. The resulting factors are applied to the pool balances in order to estimate the probable risk of loss within each pool. Prudent business practices dictate that the level of the allowance, as well as corresponding charges to the provision for loan losses, should be commensurate with identified areas of risk within the loan portfolio and the attendant risks inherent therein. The quality of the credit risk management function and the overall administration of this vital segment of the Corporation's assets are critical to the ongoing success of the Corporation.

The previously mentioned analysis considered numerous historical and other factors to analyze the adequacy of the allowance and current period charges against the provision for loan losses. Management paid special attention to a section of the analysis that compared and plotted the actual level of the allowance against the aggregate amount of loans adversely classified in order to compute the estimated potential losses associated with those loans. By noting the spread at the present time, as well as prior periods, management can determine the current adequacy of the allowance as well as evaluate trends that may be developing. The volume and composition of the Corporation's loan portfolio continue to reflect growth in commercial credits including commercial real estate loans.

As mentioned in the Loans section of this analysis, management considers commercial lending a competitive advantage and continues to focus on this area as part of its strategic growth initiatives. However, management must also consider the fact that the inherent risk is more pronounced in these types of credits and is also driven by the economic environment of its market areas.

During the three month period ended March 31, 2010, the Corporation decreased its provision for loan losses and allowance as compared to the three month period ended March 31, 2009. The decrease was a result of reductions in net charge-offs, primarily in the consumer discount portfolio, as well as a lack of loan growth during the quarter ended March 31, 2010.

Nonperforming loans have increased significantly from March 31, 2009 to March 31, 2010, primarily due to the effect of the overall challenging economic environment on certain borrowers. One large commercial loan, a shared national credit in which the Corporation participates, with a carrying value of \$5.0 million was placed on nonaccrual status during the quarter ended September 30, 2009. Management has reviewed this loan to determine if a specific loss allocation was required and has determined that no significant allocation is warranted at this time. In addition, most of the Corporation's loans that have nonaccrual status are also impaired and subject to the Corporation's specific loss allocation process. The resulting specific losses identified have remained consistent. As such, during the twelve month period ended March 31, 2010, the allowance for loan losses as a percentage of net loans only increased by six basis points from 1.33% at March 31, 2009 to 1.39% at March 31, 2010 due to reserves related to loans that do not require a specific allocation, primarily as a result of the current economic environment.

Management believes that both its 2010 provision and allowance for loan losses are reasonable and adequate to absorb probable incurred losses in its portfolio at March 31, 2010.

**Table of Contents****PREMISES AND EQUIPMENT**

Premises and equipment increased \$966 thousand, or 4.1%, since December 31, 2009. This increase is the result of growth initiatives with the ERIEBANK division. As mentioned in the General Overview section, the Corporation is currently constructing a full service branch that is expected to be opened in Meadville, Pennsylvania in the second quarter of 2010.

**BANK OWNED LIFE INSURANCE**

The Corporation has periodically purchased Bank Owned Life Insurance (BOLI). The policies cover executive officers and a select group of other employees with the Bank being named as beneficiary. Earnings from the BOLI assist the Corporation in offsetting its benefit costs. During the first quarter of 2010, additional BOLI of \$2.5 million was purchased.

**FUNDING SOURCES**

The Corporation considers deposits, short-term borrowings, and term debt when evaluating funding sources. Traditional deposits continue to be the main source of funds in the Corporation increasing \$75.6 million from \$956.9 million at December 31, 2009 to \$1,032.5 million at March 31, 2010. The growth in deposits was the result of increases in savings accounts of \$47.1 million and certificates of deposit of \$25.1 million. The increase in savings accounts occurred as a result of the Corporation's continued offering of competitive rates and growth of its ERIEBANK franchise. The increase in certificates of deposit resulted from a \$24.4 million increase in the Corporation's EZ Access product which provides customers the ability to make deposits to and withdrawals from a traditional time deposit. During the first quarter, the Corporation also continued to expand its business and consumer relationships in the ERIEBANK market, including the territory which will be served by its new Meadville, Pennsylvania branch that is scheduled to open in 2010. In addition, a large regional bank that had a significant presence in northwestern Pennsylvania merged with another financial institution in 2009, resulting in opportunities to market the Corporation's deposit products to potential new customers.

Periodically, the Corporation utilizes term borrowings from the Federal Home Loan Bank (FHLB) and other lenders to meet funding needs. Management plans to maintain access to short and long-term borrowings as an available funding source when deemed appropriate.

**SHAREHOLDERS' EQUITY**

The Corporation's capital continues to provide a base for profitable growth. Total shareholders' equity was \$71.9 million at March 31, 2010 and \$69.4 million at December 31, 2009. In the first three months of 2010, the Corporation earned \$2.2 million and declared dividends of \$1.4 million, a dividend payout ratio of 67.1% of net income. The Corporation has also complied with the standards of capital adequacy mandated by the banking regulators. Bank regulators have established risk-based capital requirements designed to measure capital adequacy. Risk-based capital ratios reflect the relative risks of various assets banks hold in their portfolios. A weight category of 0% (lowest risk assets), 20%, 50%, or 100% (highest risk assets), is assigned to each asset on the balance sheet. The Bank's capital ratios as of March 31, 2010 and December 31, 2009, and well-capitalized minimum ratios are as follows:

	March 31, 2010	December 31, 2009	Well-capitalized minimum ratio
Total risk-based capital ratio	11.61%	11.56%	10.0%
Tier 1 capital ratio	10.47%	10.42%	6.0%
Leverage ratio	6.95%	7.27%	5.0%

The Corporation's total risk-based capital, Tier 1 capital and leverage ratios all exceed well-capitalized standards as well. The ratios provide quantitative data demonstrating the strength and future opportunities for use of the Corporation's capital base. An evaluation of risk-based capital ratios and the capital position of the Corporation is part of its budgeting and strategic planning processes.

**Table of Contents**

***LIQUIDITY AND INTEREST RATE SENSITIVITY***

Liquidity measures an organizations ability to meet cash obligations as they come due. The consolidated statement of cash flows presented on page 6 provides analysis of the Corporation s cash and cash equivalents. Additionally, management considers that portion of the loan and investment portfolio that matures within one year as part of the Corporation s liquid assets. The Corporation s liquidity is monitored by both management and the Board s ALCO Committee, which establishes and monitors ranges of acceptable liquidity. Management believes the Corporation s current liquidity and interest rate position is acceptable.

***OFF BALANCE SHEET ACTIVITIES***

Some financial instruments, such as loan commitments, credit lines, letters of credit and overdraft protection, are issued to meet customer financing needs. The contractual amount of financial instruments with off-balance sheet risk was as follows at March 31, 2010 (in thousands):

Commitments to extend credit	\$ 194,683
Standby letters of credit	21,699
	\$ 216,382

**Table of Contents****CNB FINANCIAL CORPORATION****CONSOLIDATED YIELD COMPARISONS****AVERAGE BALANCES AND NET INTEREST MARGIN FOR THE THREE MONTHS ENDED**

Dollars in thousands

	March 31, 2010			March 31, 2009		
	Average Balance	Annual Rate	Interest Inc./Exp.	Average Balance	Annual Rate	Interest Inc./Exp.
<b>ASSETS:</b>						
Interest-bearing deposits with other banks	\$ 8,021	1.60%	\$ 32	\$ 8,693	3.31%	\$ 72
Federal funds sold and securities purchased under agreements to resell				5	0.00%	
Securities:						
Taxable (1)	316,944	2.89%	2,340	188,543	3.82%	1,906
Tax-Exempt (1,2)	55,387	5.13%	696	52,635	6.00%	774
Equity Securities (1,2)	1,644	2.43%	10	1,363	3.82%	13
Total securities	373,975	3.21%	3,046	242,541	4.27%	2,693
Loans:						
Commercial (2)	251,358	5.63%	3,541	241,012	5.71%	3,440
Mortgage (2)	413,494	6.15%	6,353	386,901	6.53%	6,313
Consumer	47,098	13.66%	1,608	47,930	15.09%	1,808
Total loans (3)	711,950	6.46%	11,502	675,843	6.84%	11,561
Total earning assets	1,093,946	5.30%	\$ 14,580	927,082	6.12%	\$ 14,326
Non interest-bearing assets:						
Cash and due from banks	39,748			32,882		
Premises and equipment	23,650			23,573		
Other assets	55,007			48,228		
Allowance for loan losses	(9,910)			(8,935)		
Total non interest-bearing assets	108,495			95,748		
<b>TOTAL ASSETS</b>	<b>\$ 1,202,441</b>			<b>\$ 1,022,830</b>		
<b>LIABILITIES AND SHAREHOLDERS EQUITY:</b>						
Demand - interest-bearing	\$ 246,208	0.71%	439	\$ 235,934	0.97%	573
Savings	304,857	1.60%	1,220	154,175	1.84%	711
Time	333,493	2.14%	1,781	328,066	2.50%	2,047
Total interest-bearing deposits	884,558	1.56%	3,440	718,175	1.86%	3,331

Edgar Filing: CNB FINANCIAL CORP/PA - Form 10-Q

Short-term borrowings	1,239	0.32%	1	3,563	0.45%	4
Long-term borrowings	99,984	4.39%	1,097	107,463	4.42%	1,187
Subordinated debentures	20,620	3.67%	189	20,620	4.46%	230
Total interest-bearing liabilities	1,006,401	1.88%	\$ 4,727	849,821	2.24%	\$ 4,752
Demand - non interest-bearing	110,979			98,245		
Other liabilities	13,319			11,148		
Total liabilities	1,130,699			959,214		
Shareholders equity	71,742			63,616		
<b>TOTAL LIABILITIES AND SHAREHOLDERS EQUITY</b>	<b>\$ 1,202,441</b>			<b>\$ 1,022,830</b>		
Interest income/Earning assets		5.30%	\$ 14,580		6.12%	\$ 14,326
Interest expense/Interest-bearing liabilities		1.88%	4,727		2.24%	4,752
Net interest spread		3.42%	\$ 9,853		3.88%	\$ 9,574
Interest income/Earning assets		5.30%	14,580		6.12%	14,326
Interest expense/Earning assets		1.73%	4,727		2.05%	4,752
Net interest margin		3.57%	\$ 9,853		4.07%	\$ 9,574

- (1) Includes unamortized discounts and premiums. Average balance is computed using the carrying value of securities. The average yield has been computed using the historical amortized cost average balance for available for sale securities.
- (2) Average yields are stated on a fully taxable equivalent basis.
- (3) Average outstanding includes the average balance outstanding of all non-accrual loans. Loans consist of the average of total loans less average unearned income. The amount of loan fees included in the interest income on loans is not material.

**Table of Contents**

**RESULTS OF OPERATIONS**

**OVERVIEW OF THE INCOME STATEMENT**

The Corporation had net income of \$2,160,000 for the first quarter of 2010 compared to \$2,226,000 for the same period of 2009. The earnings per diluted share was \$0.25 in the first quarter of 2010 and \$0.26 for the first quarter of 2009. The Corporation's first quarter 2010 results of operations were negatively affected by other-than-temporary impairment charges of \$784 thousand related to one structured pooled trust preferred security. The return on assets and return on equity for the first quarter of 2010 are 0.72% and 12.04% compared to 0.88% and 14.19% for the first quarter of 2009.

**INTEREST INCOME AND EXPENSE**

Net interest income totaled \$9.4 million, an increase of \$238 thousand, or 2.6% over the first quarter of 2009. Total interest and dividend income increased by \$213 thousand, or 1.5%, as compared to the first quarter of 2009. Although the Corporation's earning assets continue to grow, these increases have been offset by decreases in the yield on earning assets. Total interest expense decreased \$25 thousand, or 0.5%, as compared to the first quarter of 2009. The Corporation experienced significant deposit growth in the latter part of 2009 and continuing into 2010; however, interest expense has been positively impacted by historically low interest rates, as well as interest rate reductions implemented on certain savings and time deposit accounts in the first quarter of 2010.

**PROVISION FOR LOAN LOSSES**

The Corporation recorded a provision for loan losses of \$585 thousand in the first quarter of 2010 compared to \$862 thousand in the first quarter of 2009. As noted in the allowance for loan loss table, the Corporation experienced fewer charge-offs during the first quarter of 2010 compared to the first quarter of 2009 and the Corporation had slight loan shrinkage during the first quarter of 2010. In addition, net charge-offs as a percentage of average loans remain at a modest level in comparison to our peer group. These factors resulted in the need for a lower provision for loan losses in the first quarter of 2010 than was recorded in the first quarter of 2009. Management believes the charges to the provision in the first quarter are appropriate and the allowance for loan losses is adequate to absorb probable incurred losses in our portfolio as of March 31, 2010.

**NON-INTEREST INCOME**

Non-interest income increased \$83 thousand, or 4.3%, in the first quarter of 2010 as compared to the first quarter of 2009. The Corporation recorded other-than-temporary impairment charges in the first quarter of 2010 of \$784 thousand, which was offset by realized gains on available-for-sale securities of \$432 thousand. In addition, the Corporation recorded unrealized gains (losses) during the quarters ended March 31, 2010 and 2009 of \$82 and (\$151), respectively, for securities for which the fair value option was elected.

Excluding the effects of securities transactions, the Corporation's non-interest income increased \$186 thousand, or 8.8% in the first quarter of 2010 as compared to the same period in 2009. The most significant change was in net debit card transaction income, which increased \$88 thousand from the first quarter of 2009 to 2010 due to increases in the volume of debit card transactions.

## **Table of Contents**

### **NON-INTEREST EXPENSE**

Non-interest expense increased by \$730 thousand, or 9.9%, to \$8.1 million in the first quarter of 2010. The Corporation's insurance premiums due to the Federal Deposit Insurance Corporation ( FDIC ) increased by \$116 thousand as a result of increases in the deposits on which the premium assessment is based and higher assessment rates in 2010. In addition, employee benefit plan expenses increased by \$278 thousand, primarily as a result of an increase in health insurance expenses as well as expenses related to the Corporation's supplemental executive retirement plan.

### **INCOME TAX EXPENSE**

Income tax expense was \$641 thousand in the first quarter of 2010 as compared to \$707 thousand in the first quarter of 2009, resulting in an effective tax rate of 22.9% and 24.1%, respectively. The effective rate for the periods differed from the federal statutory rate of 35.0% principally as a result of tax exempt income from securities and loans as well as earnings from bank owned life insurance.

### **CRITICAL ACCOUNTING POLICIES**

The accounting and reporting policies of CNB Financial Corporation are in accordance with accounting principles generally accepted in the United States of America and conform to general practices within the financial services industry. Accounting and reporting practices for the allowance for loan losses and fair value of securities are deemed critical since they involve the use of estimates and require significant management judgments. Application of assumptions different than those used by management could result in material changes in CNB Financial Corporation's financial position or results of operations. Note 1 (Summary of Significant Accounting Policies), Note 3 (Securities), and Note 5 (Allowance for Loan Losses), of the 2009 Form 10-K, provide detail with regard to the Corporation's accounting for the allowance for loan losses and fair value of securities. There have been no significant changes in the application of accounting policies since December 31, 2009.

### **SAFE HARBOR STATEMENT UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995**

Certain statements contained in the report that are not historical facts are forward looking statements that are subject to certain risks and uncertainties. When used herein, the terms anticipates, plans, expects, believes, estimate, projected, forecast, should, or gravitate to expressions as they relate to CNB Financial Corporation or its management are intended to identify such forward looking statements. CNB Financial Corporation's actual results, performance or achievements may materially differ from those expressed or implied in the forward-looking statements. Risks and uncertainties that could cause or contribute to such material differences include, but are not limited to, general economic conditions, interest rate environment, competitive conditions in the financial services industry, changes in law, governmental policies and regulations, and rapidly changing technology affecting financial services.



**Table of Contents**

**ITEM 3      QUANTITATIVE & QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Market risk is the risk of loss arising from adverse changes in the fair value of financial instruments due to changes in interest rates, exchange rates, and equity prices. As a financial institution, the Corporation is primarily sensitive to the interest rate risk component. Changes in interest rates will affect the levels of income and expense recorded on a large portion of the Bank's assets and liabilities. Additionally, such fluctuations in interest rates will impact the market value of all interest sensitive assets. The Asset/Liability Committee (ALCO) is responsible for reviewing the interest rate sensitivity position and establishing policies to control exposure to interest rate fluctuations. The primary goal established by this policy is to increase total income within acceptable risk limits.

The Corporation monitors interest rate risk through the use of two models: earnings simulation and static gap. Each model standing alone has limitations; however taken together they represent a reasonable view of the Corporation's interest rate risk position.

*STATIC GAP:* Gap analysis is intended to provide an approximation of projected repricing of assets and liabilities at a point in time on the basis of stated maturities, prepayments, and scheduled interest rate adjustments within selected time intervals. A gap is defined as the difference between the principal amount of assets and liabilities which reprice within those time intervals. The cumulative one year gap at March 31, 2010 was (0.22%) of total earning assets compared to policy guidelines of plus or minus 15.0%.

Fixed rate securities, loans and CDs are included in the gap repricing based on time remaining until maturity. Mortgage prepayments are included in the time frame in which they are expected to be received.

Certain shortcomings are inherent in the method of analysis presented in Static Gap. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may not react correspondingly to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate with changes in market interest rates, while interest rates on other types of assets may lag behind changes in market rates. Additionally, certain assets, such as adjustable-rate loans, have features, like annual and lifetime rate caps, which restrict changes in interest rates both on a short-term basis and over the life of the asset. Further, in the event of a change in interest rates, prepayment and early withdrawal levels would likely deviate from those assumed in the table. Finally, the ability of certain borrowers to make scheduled payments on their adjustable-rate loans may decrease in the event of an interest rate increase.

*EARNINGS SIMULATION:* This model forecasts the projected change in net income resulting from an increase or decrease in the level of interest rates. The model assumes a one time shock of plus or minus 200 basis points or 2%.

The model makes various assumptions about cash flows and reinvestments of these cash flows in the different rate environments. Generally, repayments, maturities and calls are assumed to be reinvested in like instruments and no significant change in the balance sheet mix is assumed. Actual results could differ significantly from these estimates which would produce significant differences in the calculated projected change in income. The limits stated above do not necessarily represent measures that would be taken by management in order to stabilize income results. The instruments on the balance sheet do react at different speeds to various changes in interest rates as discussed under Static Gap. In addition, there are strategies available to management that minimize the decline in income caused by a rapid rise in interest rates.

**Table of Contents**

The following table below summarizes the information from the interest rate risk measures reflecting rate sensitive assets to rate sensitive liabilities at March 31, 2010 and December 31, 2009:

	March 31, 2010	December 31, 2009
Static 1-Yr. Cumulative Gap	(0.22)%	(0.60)%
Earnings Simulation:		
-200 bps vs. Stable Rate	9.84%	14.43%
+200 bps vs. Stable Rate	(10.69)%	(6.57)%

The interest rate sensitivity position at March 31, 2010 was close to neutral but slightly liability sensitive in the short-term, which is consistent with December 31, 2009. Management measures the potential impact of significant changes in interest rates on both earnings and equity. By the use of computer generated models, the potential impact of these changes has been determined to be acceptable with modest effects on net income and equity given an interest rate shock of an increase or decrease in rates of 2.0%. We continue to monitor the interest rate sensitivity through the ALCO and use the data to make strategic decisions.

**ITEM 4 CONTROLS AND PROCEDURES**

As of the end of the period covered by this quarterly report, an evaluation was carried out under the supervision and with the participation of the Corporation's management, including our Chief Executive Officer and Principal Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on their evaluation, our Chief Executive Officer and Principal Financial Officer have concluded that the Corporation's disclosure controls and procedures are, to the best of their knowledge, effective to ensure that information required to be disclosed by the Corporation in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms. Subsequent to the date of their evaluation, our Chief Executive Officer and Principal Financial Officer have concluded that there were no significant changes in the Corporation's internal controls or in other factors that could significantly affect its internal controls, including any corrective actions with regard to significant deficiencies and material weaknesses.

**Table of Contents**

**PART II OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS** None

**ITEM 1A. RISK FACTORS** There have been no material changes to the factors disclosed in Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2009.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS** There were no shares purchased as part of publicly announced plans or programs from January 1, 2010 to March 31, 2010. The maximum number of shares that may yet be purchased under publicly announced plans or programs is 168,386.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES** None

**ITEM 4. [REMOVED AND RESERVED]**

**ITEM 5. OTHER INFORMATION** None

**ITEM 6. EXHIBITS**

- EXHIBIT 31.1 CEO Certification
- EXHIBIT 31.2 Principal Financial Officer Certification
- EXHIBIT 32 Certifications

**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.

CNB FINANCIAL CORPORATION  
(Registrant)

DATE: May 7, 2010

/s/ JOSEPH B. BOWER, JR.  
**Joseph B. Bower, Jr.**  
**President and Director**

**(Principal Executive Officer)**

DATE: May 7, 2010

/s/ CHARLES R. GUARINO  
**Charles R. Guarino**  
**Treasurer**  
**(Principal Financial Officer)**