ACNB CORP
Form 10-Q
November 01, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2013

Commission file number 0-11783

ACNB CORPORATION

(Exact name of Registrant as specified in its charter)

Pennsylvania	**23-2233457**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
16 Lincoln Square, Gettysburg, Pennsylvania	**17325**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(717) 334-3161**

Title of each class	Name of each exchange on which registered
Common Stock, $2.50 par value per share	The NASDAQ Stock Market, LLC

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes x No o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

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

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

The number of shares of the Registrant s Common Stock outstanding on November 1, 2013, was 5,986,661.

PART I - FINANCIAL INFORMATION

ACNB CORPORATION

ITEM 1 - FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF CONDITION (UNAUDITED)

Dollars in thousands, except per share data	September 30, 2013	September 30, 2012	December 31, 2012
ASSETS			
Cash and due from banks	**$ 16,371**	$ 12,338	$ 19,078
Interest bearing deposits with banks	**2,856**	52,165	32,307
Total Cash and Cash Equivalents	**19,227**	64,503	51,385
Securities available for sale	**135,163**	175,889	165,790
Securities held to maturity, fair value $94,667; $48,971; $50,980	**96,255**	48,016	50,159
Loans held for sale	**603**	3,618	6,687
Loans, net of allowance for loan losses $16,797; $15,993; $16,825	**701,251**	686,082	691,311
Premises and equipment	**15,545**	14,529	15,131
Restricted investment in bank stocks	**4,189**	5,887	5,318
Investment in bank-owned life insurance	**32,003**	30,876	31,122
Investments in low-income housing partnerships	**5,233**	5,562	5,440
Goodwill	**6,308**	6,308	6,308
Intangible assets	**1,928**	2,570	2,409
Foreclosed assets held for resale	**1,608**	4,901	4,247
Other assets	**15,217**	14,282	14,688
Total Assets	**$ 1,034,530**	$ 1,063,023	$ 1,049,995
LIABILITIES AND STOCKHOLDERS EQUITY			
LIABILITIES			
Deposits:			
Non-interest bearing	**$ 130,110**	$ 119,086	$ 119,297
Interest bearing	**689,121**	712,265	714,879
Total Deposits	**819,231**	831,351	834,176
Short-term borrowings	**57,418**	52,926	47,303
Long-term borrowings	**47,767**	70,015	59,954
Other liabilities	**7,094**	7,054	7,298
Total Liabilities	**931,510**	961,346	948,731
STOCKHOLDERS EQUITY			
Preferred Stock, $2.50 par value; 20,000,000 shares authorized; no shares outstanding			

Common stock, $2.50 par value; 20,000,000 shares authorized; 6,049,261, 6,023,320 and 6,027,968 shares issued; 5,986,661, 5,960,720 and 5,965,368 shares outstanding	**15,123**	15,058	15,070
Treasury stock, at cost (62,600 shares)	**(728)**	(728)	(728)
Additional paid-in capital	**9,557**	9,183	9,246
Retained earnings	**81,532**	76,802	77,888
Accumulated other comprehensive (loss) income	**(2,464)**	1,362	(212)
Total Stockholders Equity	**103,020**	101,677	101,264
Total Liabilities and Stockholders Equity	**$ 1,034,530**	$ 1,063,023	$ 1,049,995

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

ACNB CORPORATION

CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

Dollars in thousands, except per share data	Three Months Ended September 30, 2013	2012	Nine Months Ended September 30, 2013	2012
INTEREST INCOME				
Loans, including fees	**$ 7,840**	$ 8,484	**$ 24,074**	$ 25,551
Securities:				
Taxable	**1,078**	1,158	**3,166**	3,758
Tax-exempt	**280**	393	**922**	1,130
Dividends	**6**	4	**16**	11
Other	**16**	28	**64**	51
Total Interest Income	**9,220**	10,067	**28,242**	30,501
INTEREST EXPENSE				
Deposits	**500**	864	**1,721**	2,652
Short-term borrowings	**17**	19	**44**	60
Long-term borrowings	**419**	643	**1,321**	2,040
Total Interest Expense	**936**	1,526	**3,086**	4,752
Net Interest Income	**8,284**	8,541	**25,156**	25,749
PROVISION FOR LOAN LOSSES	**150**	1,125	**1,300**	3,375
Net Interest Income after Provision for Loan Losses	**8,134**	7,416	**23,856**	22,374
OTHER INCOME				
Service charges on deposit accounts	**596**	648	**1,682**	1,803
Income from fiduciary activities	**333**	288	**976**	932
Earnings on investment in bank-owned life insurance	**246**	255	**741**	735
Gain on life insurance proceeds		63		63
Net gains on sales or calls of securities				7
Service charges on ATM and debit card transactions	**376**	323	**1,051**	955
Commissions from insurance sales	**1,079**	1,133	**3,609**	3,633
Other	**217**	262	**873**	725
Total Other Income	**2,847**	2,972	**8,932**	8,853
OTHER EXPENSES				
Salaries and employee benefits	**4,546**	4,527	**14,158**	13,772
Net occupancy	**463**	487	**1,471**	1,477
Equipment	**727**	573	**2,177**	1,855
Other tax	**199**	221	**669**	614
Professional services	**232**	186	**667**	628
Supplies and postage	**127**	141	**443**	468
Marketing and corporate relations	**81**	67	**293**	257
FDIC and regulatory	**191**	189	**592**	640
Intangible assets amortization	**160**	160	**481**	481
Foreclosed real estate expenses	**503**	116	**410**	346
Other operating	**817**	825	**2,458**	2,334
Total Other Expenses	**8,046**	7,492	**23,819**	22,872

Income before Income Taxes	**2,935**	2,896	**8,969**	8,355
PROVISION FOR INCOME TAXES	**627**	592	**1,921**	1,687
Net Income	**$ 2,308**	$ 2,304	**$ 7,048**	$ 6,668
PER SHARE DATA				
Basic earnings	**$ 0.39**	$ 0.39	**$ 1.18**	$ 1.12
Cash dividends declared	**$ 0.19**	$ 0.19	**$ 0.57**	$ 0.57

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

ACNB CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

Dollars in thousands	Three Months Ended September 30, 2013	2012	Nine Months Ended September 30, 2013	2012
NET INCOME	**$ 2,308**	$ 2,304	**$ 7,048**	$ 6,668
OTHER COMPREHENSIVE (LOSS) INCOME				
SECURITIES				
Unrealized (losses) gains arising during the period, net of income taxes of $(82), $208, $(1,336) and $196, respectively	**(159)**	407	**(2,595)**	386
Reclassification adjustment for net gains included in net income, net of income taxes of $0, $0, $0 and $(2), respectively (A) (C)				(5)
PENSION				
Change in plan assets and benefit obligations, net of income taxes of $58, $56, $176 and $170, respectively (B) (C)	**115**	109	**343**	326
TOTAL OTHER COMPREHENSIVE (LOSS) INCOME	**(44)**	516	**(2,252)**	707
TOTAL COMPREHENSIVE INCOME	**$ 2,264**	$ 2,820	**$ 4,796**	$ 7,375

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

(A) Amounts are included in net gains on sales or calls of securities on the Consolidated Statements of Income in total other income.

(B) Amounts are included in the computation of net periodic benefit cost and are included in salaries and employee benefits on the Consolidated Statements of Income in total other expenses.

(C) Income tax amounts are included in the provision for income taxes on the Consolidated Statements of Income.

ACNB CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (UNAUDITED)

Nine Months Ended September 30, 2013 and 2012

Dollars in thousands	Common Stock	Treasury Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
BALANCE JANUARY 1, 2012	$ 15,021	$ (728)	$ 9,000	$ 73,526	$ 655	$ 97,474
Net income				6,668		6,668
Other comprehensive income, net of taxes					707	707
Common stock shares issued (14,911 shares)	37		183			220
Cash dividends declared				(3,392)		(3,392)
BALANCE SEPTEMBER 30, 2012	$ 15,058	$ (728)	$ 9,183	$ 76,802	$ 1,362	$ 101,677
BALANCE JANUARY 1, 2013	**$ 15,070**	**$ (728)**	**$ 9,246**	**$ 77,888**	**$ (212)**	**$ 101,264**
Net income				**7,048**		**7,048**
Other comprehensive loss, net of taxes					**(2,252)**	**(2,252)**
Common stock shares issued (21,293 shares)	**53**		**311**			**364**
Cash dividends declared				**(3,404)**		**(3,404)**
BALANCE SEPTEMBER 30, 2013	**$ 15,123**	**$ (728)**	**$ 9,557**	**$ 81,532**	**$ (2,464)**	**$ 103,020**

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

ACNB CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

Dollars in thousands	Nine Months Ended September 30, 2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	**$ 7,048**	$ 6,668
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on sales of loans	**(417)**	(192)
Loss on sales of assets held for resale, including writedowns	**173**	143
Earnings on investment in bank-owned life insurance	**(741)**	(735)
Gain on life insurance proceeds		(63)
Gain on sales or calls of securities		(7)
Depreciation and amortization	**1,500**	1,527
Provision for loan losses	**1,300**	3,375
Net amortization of investment securities premiums	**739**	657
Decrease in accrued interest receivable	**226**	87
Decrease in accrued interest payable	**(419)**	(109)
Mortgage loans originated for sale	**(18,882)**	(19,534)
Proceeds from sales of loans originated for sale	**25,383**	16,445
Decrease in other assets	**861**	1,594
Increase in other liabilities	**734**	257
Net Cash Provided by Operating Activities	**17,505**	10,113
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from maturities of investment securities held to maturity	**7,223**	1,576
Proceeds from maturities of investment securities available for sale	**33,202**	51,695
Purchase of investment securities held to maturity	**(53,689)**	(39,651)
Purchase of investment securities available for sale	**(6,875)**	(18,341)
Net increase in loans	**(11,741)**	(12,283)
Redemption of restricted investment in bank stocks	**1,129**	1,259
Investment in low-income housing project	**(249)**	(2,106)
Purchase of bank-owned life insurance	**(140)**	(1,940)
Capital expenditures	**(1,433)**	(1,092)
Proceeds from life insurance death benefits		273
Proceeds from sale of foreclosed real estate	**2,967**	1,205
Net Cash Used in Investing Activities	**(29,606)**	(19,405)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in demand deposits	**10,813**	6,839
Net (decrease) increase in time certificates of deposits and interest bearing deposits	**(25,758)**	41,717
Net increase in short-term borrowings	**10,115**	6,964
Dividends paid	**(3,404)**	(3,392)
Common stock issued	**364**	220
Proceeds from long-term borrowings	**2,000**	10,000
Repayments on long-term borrowings	**(14,187)**	(11,176)
Net Cash (Used in) Provided by Financing Activities	**(20,057)**	51,172
Net (Decrease) Increase in Cash and Cash Equivalents	**(32,158)**	41,880
CASH AND CASH EQUIVALENTS BEGINNING	**51,385**	22,623

CASH AND CASH EQUIVALENTS ENDING	**$**	**19,227**	$	64,503
Interest paid	**$**	**3,505**	$	4,861
Incomes taxes paid	**$**	**2,225**	$	250
Loans transferred to foreclosed assets held for resale	**$**	**501**	$	1,812

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

ACNB CORPORATION

ITEM 1 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. **Basis of Presentation**

ACNB Corporation, headquartered in Gettysburg, Pennsylvania, provides banking, insurance, and financial services to businesses and consumers through its wholly-owned subsidiaries, ACNB Bank and Russell Insurance Group, Inc. (RIG). The Bank engages in full-service commercial and consumer banking and trust services through its nineteen retail banking office locations in Adams, Cumberland and York Counties, Pennsylvania. There are also two loan production offices situated in York and Franklin Counties, Pennsylvania.

RIG is a full-service insurance agency based in Westminster, Maryland. The agency offers a broad range of property and casualty, life, and health insurance to both commercial and individual clients. In 2008, due to an agency acquisition, a second location of RIG was established in Germantown, Maryland.

The Corporation, along with seven other banks, entered into a joint venture to form BankersRe Insurance Group, SPC (formerly Pennbanks Insurance Co., SPC), an offshore reinsurance company. Each participating entity owned an insurance cell through which its premiums and losses from credit life, disability, and accident insurance are funded. Each entity was responsible for the activity in its respective cell. The financial activity for the Corporation s insurance cell has been included in the consolidated financial statements and is not material to the consolidated financial statements. The segregated portfolio was novated to a third party during 2012.

The Corporation s primary source of revenue is interest income on loans and investment securities and fee income on its products and services. Expenses consist of interest expense on deposits and borrowed funds, provisions for loan losses, and other operating expenses.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments necessary to present fairly ACNB Corporation s financial position and the results of operations, comprehensive income, changes in stockholders equity, and cash flows. All such adjustments are of a normal recurring nature.

The accounting policies followed by the Corporation are set forth in Note A to the Corporation s consolidated financial statements in the 2012 ACNB Corporation Annual Report on Form 10-K, filed with the SEC on March 15, 2013. It is suggested that the consolidated financial statements contained herein be read in conjunction with the consolidated financial statements and notes included in the Corporation s Annual Report on Form 10-K. The results of operations for the three and nine month periods ended September 30, 2013, are not necessarily indicative of the results to be expected for the full year.

The Corporation has evaluated events and transactions occurring subsequent to the statement of condition date of September 30, 2013, for items that should potentially be recognized or disclosed in the consolidated financial statements. The evaluation was conducted through the date these consolidated financial statements were issued.

2. **Earnings Per Share**

The Corporation has a simple capital structure. Basic earnings per share of common stock is computed based on 5,973,418 and 5,951,102 weighted average shares of common stock outstanding for the nine months ended September 30, 2013 and 2012, respectively, and 5,981,936 and 5,956,380 for the three months ended September 30, 2013 and 2012, respectively. The Corporation does not have dilutive securities outstanding.

3. **Retirement Benefits**

The components of net periodic benefit cost related to the non-contributory, defined benefit pension plan for the three and nine month periods ended September 30 were as follows:

In thousands	Three Months Ended September 30, 2013	2012	Nine Months Ended September 30, 2013	2012
Service cost	**$ 194**	$ 163	**$ 582**	$ 488
Interest cost	**223**	231	**669**	694
Expected return on plan assets	**(489)**	(443)	**(1,467)**	(1,329)
Amortization of net loss	**163**	153	**489**	459
Amortization of transition obligation		2		7
Amortization of prior service cost	**10**	10	**30**	30
Net Periodic Benefit Cost	**$ 101**	$ 116	**$ 303**	$ 349

The Corporation previously disclosed in its consolidated financial statements for the year ended December 31, 2012, that it had not yet determined the amount the Bank planned on contributing to the defined benefit plan in 2013. As of September 30, 2013, this contribution amount has still not been determined. Effective April 1, 2012, no inactive or former participant in the plan is eligible to again participate in the plan, and no employee hired after March 31, 2012, is eligible to participate in the plan. As of the last annual census, ACNB Bank had a combined 368 active, vested terminated, and retired persons in the plan.

4. **Guarantees**

The Corporation does not issue any guarantees that would require liability recognition or disclosure, other than its standby letters of credit. Standby letters of credit are written conditional commitments issued by the Corporation to guarantee the performance of a customer to a third party. Generally, all letters of credit, when issued, have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as those that are involved in extending loan facilities to customers. The Corporation generally holds collateral and/or personal guarantees supporting these commitments. The Corporation had $4,285,000 in standby letters of credit as of September 30, 2013. Management believes that the proceeds obtained through a liquidation of collateral and the enforcement of guarantees would be sufficient to cover the potential amount of future payments required under the corresponding guarantees. The current amount of the liability, as of September 30, 2013, for guarantees under standby letters of credit issued is not material.

5. **Accumulated Other Comprehensive Income (Loss)**

The components of accumulated other comprehensive income (loss), net of taxes, are as follows:

In thousands		Unrealized Gains on Securities	Pension Liability	Accumulated Other Comprehensive Income (Loss)
BALANCE	**SEPTEMBER 30, 2013**	**$ 3,019**	**$ (5,483)**	**$ (2,464)**
BALANCE	DECEMBER 31, 2012	$ 5,614	$ (5,826)	$ (212)
BALANCE	SEPTEMBER 30, 2012	$ 6,377	$ (5,015)	$ 1,362

6. **Segment Reporting**

Russell Insurance Group, Inc. (RIG) is managed separately from the banking segment, which includes the Bank and related financial services that the Corporation offers through its banking subsidiary. RIG offers a broad range of property and casualty, life, and health insurance to both commercial and individual clients.

Segment information for the nine month periods ended September 30, 2013 and 2012, is as follows:

In thousands	Banking	Insurance	Total
2013			
Net interest income and other income from external customers	**$ 30,786**	**$ 3,302**	**$ 34,088**
Income before income taxes	**8,470**	**499**	**8,969**
Total assets	**1,024,946**	**9,584**	**1,034,530**
Capital expenditures	**1,426**	**7**	**1,433**
2012			
Net interest income and other income from external customers	$ 31,117	$ 3,485	$ 34,602
Income before income taxes	7,857	498	8,355
Total assets	1,052,755	10,268	1,063,023
Capital expenditures	1,020	72	1,092

Segment information for the three month periods ended September 30, 2013 and 2012, is as follows:

In thousands	Banking	Insurance	Total
2013			
Net interest income and other income from external customers	**$ 10,343**	**$ 788**	**$ 11,131**
Income before income taxes	**2,813**	**122**	**2,935**
Total assets	**1,024,946**	**9,584**	**1,034,530**
Capital expenditures	**734**		**734**
2012			
Net interest income and other income from external customers	$ 10,512	$ 1,001	$ 11,513
Income before income taxes	2,809	87	2,896
Total assets	1,052,755	10,268	1,063,023
Capital expenditures	148		148

Intangible assets, representing customer lists, are amortized over 10 years on a straight line basis. Goodwill is not amortized, but rather is analyzed annually for impairment. If certain events occur which might indicate goodwill has been impaired, the goodwill is tested for impairment when such events occur. Amortization of goodwill and the intangible assets is deductible for tax purposes.

7. **Securities**

Debt securities that management has the positive intent and ability to hold to maturity are classified as held to maturity and recorded at amortized cost. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as available for sale and recorded at fair value, with unrealized gains and losses excluded from earnings and reported, net of tax, in other comprehensive income (loss).

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held to maturity and available for sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses on debt securities, management considers (1) whether management intends to sell the security, or (2) if it is more likely than not that management will be required to sell the security before recovery, or (3) if management does not expect to recover the entire amortized cost basis. In assessing potential other-than-temporary impairment for equity securities, consideration is given to management s intention and ability to hold the securities until recovery of unrealized losses. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Amortized cost and fair value of securities at September 30, 2013, and December 31, 2012, were as follows:

In thousands	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
SECURITIES AVAILABLE FOR SALE				
SEPTEMBER 30, 2013				
U.S. Government and agencies	**$ 21,127**	**$ 642**	**$**	**$ 21,769**
Mortgage-backed securities, residential	**55,282**	**2,646**	**46**	**57,882**
State and municipal	**41,508**	**1,209**	**268**	**42,449**
Corporate bonds	**11,004**	**205**	**49**	**11,160**
CRA mutual fund	**1,044**	**4**		**1,048**
Stock in other banks	**627**	**228**		**855**
	$ 130,592	**$ 4,934**	**$ 363**	**$ 135,163**
DECEMBER 31, 2012				
U.S. Government and agencies	$ 23,225	$ 1,016	$	$ 24,241
Mortgage-backed securities, residential	75,816	4,767		80,583
State and municipal	49,568	2,246	10	51,804
Corporate bonds	7,008	286	8	7,286
CRA mutual fund	1,044	52		1,096
Stock in other banks	627	153		780
	$ 157,288	$ 8,520	$ 18	$ 165,790
SECURITIES HELD TO MATURITY				
SEPTEMBER 30, 2013				
U.S. Government and agencies	**$ 37,539**	**$ 221**	**$ 742**	**$ 37,018**
Mortgage-backed securities, residential	**58,716**	**71**	**1,138**	**57,649**
	$ 96,255	**$ 292**	**$ 1,880**	**$ 94,667**
DECEMBER 31, 2012				
U.S. Government and agencies	$ 30,115	$ 536	$ 6	$ 30,645
Mortgage-backed securities, residential	20,044	298	7	20,335
	$ 50,159	$ 834	$ 13	$ 50,980

The following table shows the Corporation s investments gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at September 30, 2013, and December 31, 2012:

	Less than 12 Months		12 Months or More		Total	
In thousands	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
SECURITIES AVAILABLE FOR SALE						
SEPTEMBER 30, 2013						
Mortgage-backed securities, residential	**$ 5,466**	**$ 46**	**$**	**$**	**$ 5,466**	**$ 46**
State and municipal	**11,350**	**268**			**11,350**	**268**
Corporate bonds	**4,951**	**49**			**4,951**	**49**
	$ 21,767	**$ 363**	**$**	**$**	**$ 21,767**	**$ 363**
DECEMBER 31, 2012						
State and municipal	$ 1,975	$ 10	$	$	$ 1,975	$ 10
Corporate bond	992	8			992	8
	$ 2,967	$ 18	$	$	$ 2,967	$ 18
SECURITIES HELD TO MATURITY						
SEPTEMBER 30, 2013						
U.S. Government and agencies	**$ 23,830**	**$ 699**	**$ 1,957**	**$ 43**	**$ 25,787**	**$ 742**
Mortgage-backed securities, residential	**44,094**	**1,138**			**44,094**	**1,138**
	$ 67,924	**$ 1,837**	**$ 1,957**	**$ 43**	**$ 69,881**	**$ 1,880**
DECEMBER 31, 2012						
U.S. Government and agencies	$ 2,994	$ 6	$	$	$ 2,994	$ 6
Mortgage-backed security, residential	2,046	7			2,046	7
	$ 5,040	$ 13	$	$	$ 5,040	$ 13

All mortgage-backed security investments are government sponsored enterprise (GSE) pass-through instruments issued by the Federal National Mortgage Association (FNMA), Government National Mortgage Association (GNMA) or Federal Home Loan Mortgage Corporation (FHLMC), which guarantee the timely payment of principal on these investments.

At September 30, 2013, five available for sale residential mortgage-backed securities had unrealized losses that individually did not exceed 3% of amortized cost. These securities have not been in a continuous loss position for 12 months or more. These unrealized losses relate principally to changes in interest rates subsequent to the acquisition of the specific securities.

At September 30, 2013, twenty-four available for sale state and municipal bonds had unrealized losses that individually did not exceed 6% of amortized cost. These securities have not been in a continuous loss position for 12 months or more. These unrealized losses relate principally to changes in interest rates subsequent to the acquisition of the specific securities.

At September 30, 2013, one available for sale corporate bond had an unrealized loss that did not exceed 1% of amortized cost. This security has not been in a continuous loss position for 12 months or more. This unrealized loss relates principally to changes in interest rates subsequent to the acquisition of the specific security.

At September 30, 2013, seventeen held to maturity U.S. Government and agency securities had unrealized losses that individually did not exceed 6% of amortized cost. One of these securities has been in a continuous loss position for 12 months or more. These unrealized losses relate principally to changes in interest rates subsequent to the acquisition of the specific securities.

At September 30, 2013, twenty-eight held to maturity residential mortgage-backed securities had unrealized losses that individually did not exceed 6% of amortized cost. These securities have not been in a continuous loss position for 12 months or more. These unrealized losses relate principally to changes in interest rates subsequent to the acquisition of the specific securities.

In analyzing the issuer s financial condition, management considers industry analysts reports, financial performance, and projected target prices of investment analysts within a one-year time frame. Based on the above information, management has determined that none of these investments are other-than-temporarily impaired.

The fair values of securities available for sale (carried at fair value) and held to maturity (carried at amortized cost) are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or matrix pricing (Level 2), which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific securities but rather by relying on the security s relationship to other benchmark quoted prices. The Corporation uses independent service providers to provide matrix pricing.

Management routinely sells securities from its available for sale portfolio in an effort to manage and allocate the portfolio. At September 30, 2013, management had not identified any securities with an unrealized loss that it intends or will be required to sell. In estimating other-than-temporary impairment losses on debt securities, management considers (1) whether management intends to sell the security, or (2) if it is more likely than not that management will be required to sell the security before recovery, or (3) if management does not expect to recover the entire amortized cost basis. In assessing potential other-than-temporary impairment for equity securities, consideration is given to management s intention and ability to hold the securities until recovery of unrealized losses.

Amortized cost and fair value at September 30, 2013, by contractual maturity, where applicable, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay with or without penalties.

	Available for Sale		Held to Maturity	
In thousands	**Amortized Cost**	**Fair Value**	**Amortized Cost**	**Fair Value**
1 year or less	**$ 4,129**	**$ 4,190**	**$ 10,009**	**$ 10,229**
Over 1 year through 5 years	**35,039**	**36,402**	**14,067**	**13,875**
Over 5 years through 10 years	**30,813**	**31,021**	**13,463**	**12,914**
Over 10 years	**3,658**	**3,765**		
Mortgage-backed securities, residential	**55,282**	**57,882**	**58,716**	**57,649**
CRA mutual fund	**1,044**	**1,048**		
Stock in other banks	**627**	**855**		
	$ 130,592	**$ 135,163**	**$ 96,255**	**$ 94,667**

The Corporation did not realize any gross gains or losses on sales or calls of securities available for sale during the third quarter of 2013 or 2012. For the nine month period ended September 30, 2013, the Corporation did not realize any gross gains or losses on sales or calls of securities available for sale. For the nine month period ended September 30, 2012, the Corporation realized gross gains of $7,000 and $0 in gross losses on sales or calls of securities available for sale.

At September 30, 2013, and December 31, 2012, securities with a carrying value of $154,575,000 and $147,923,000, respectively, were pledged as collateral as required by law on public and trust deposits, repurchase agreements, and for other purposes.

8. **Loans**

The Corporation grants commercial, residential, and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans throughout southcentral Pennsylvania and northern Maryland. The ability of the Corporation s debtors to honor their contracts is dependent upon the real estate values and general economic conditions in this area.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off generally are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

The loans receivable portfolio is segmented into commercial, residential mortgage, home equity lines of credit, and consumer loans. Commercial loans consist of the following classes: commercial and industrial, commercial real estate, and commercial real estate construction.

The accrual of interest on residential mortgage and commercial loans is discontinued at the time the loan is 90 days past due unless the credit is well-secured and in process of collection. Consumer loans (consisting of home equity lines of credit and consumer loan classes) are typically charged off no later than 120 days past due. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

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

Allowance for Credit Losses

The allowance for credit losses consists of the allowance for loan losses and the reserve for unfunded lending commitments. The allowance for loan losses (the allowance) is established as losses are estimated to occur through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. The reserve for unfunded lending commitments represents management s estimate of losses inherent in its unfunded loan commitments and is recorded in other liabilities on the consolidated statement of condition. The amount of the reserve for unfunded lending commitments is not material to the consolidated financial statements.

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

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as either doubtful, substandard, or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers pools of loans by loan class including commercial loans not considered impaired, as well as smaller balance homogeneous loans, such as residential real estate, home equity, and other consumer loans. These pools of loans are evaluated for loss exposure based upon historical loss rates for the previous twelve quarters for each of these categories of loans, adjusted for qualitative risk factors. These qualitative risk factors include:

- lending policies and procedures, including underwriting standards and collection, charge-off and recovery practices;

- national, regional and local economic and business conditions, as well as the condition of various market segments, including the impact on the value of underlying collateral for collateral dependent loans;

- the nature and volume of the portfolio and terms of loans;

- the experience, ability and depth of lending management and staff;

- the volume and severity of past due, classified and nonaccrual loans, as well as other loan modifications; and,

- the existence and effect of any concentrations of credit and changes in the level of such concentrations.

Each factor is assigned a value to reflect improving, stable or declining conditions based on management s best judgment using relevant information available at the time of the evaluation. Adjustments to the factors are supported through documentation of changes in conditions in a narrative accompanying the allowance for loan loss calculation.

The unallocated component of the allowance is maintained to cover uncertainties that could affect management s estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. It covers risks that are inherently difficult to quantify including, but not limited to, collateral risk, information risk, and historical charge-off risk.

A loan is considered impaired when, based on current information and events, it is probable that the Corporation will be unable to collect the scheduled payments of principal and/or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and/or interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower s prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial and commercial construction loans by either the present value of expected future cash flows discounted at the loan s effective interest rate, the loan s obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

A specific allocation within the allowance for loan losses is established for an impaired loan if its carrying value exceeds its estimated fair value. The estimated fair values of the Corporation s impaired loans are measured based on the estimated fair value of the loan s collateral or the discounted cash flows method.

It is the policy of the Corporation to order an updated valuation on all real estate secured loans when the loan becomes 90 days past due and there has not been an updated valuation completed within the previous 12 months. In addition, the Corporation orders third party valuations on all impaired real estate collateralized loans within 30 days of the loan being classified as impaired. Until the valuations are completed, the Corporation utilizes the most recent independent third party real estate valuation to estimate the need for a specific allocation to be assigned to the loan. These existing valuations are discounted downward to account for such things as the age of the existing collateral valuation, a change in the condition of the real estate, change in local market and economic conditions, and other specific factors involving the collateral. Once the updated valuation is completed, the collateral value is updated accordingly.

For commercial and industrial loans secured by non-real estate collateral, such as accounts receivable, inventory and equipment, estimated fair values are determined based on the borrower s financial statements, inventory reports, accounts receivable aging reports, equipment appraisals, or invoices. Indications of value from these sources are generally discounted based on the age of the financial information or the quality of the assets.

The Corporation actively monitors the values of collateral as well as the age of the valuation of impaired loans. Management believes that the Corporation s market area is not as volatile as other areas throughout the United States, therefore valuations are ordered at least every 18 months, or more frequently if management believes that there is an indication that the fair value has declined.

For impaired loans secured by collateral other than real estate, the Corporation considers the net book value of the asset, as provided by the most recent financial statements of the borrower, and discounts downward accordingly based on determinations made by management.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Corporation does not separately identify individual consumer and residential loans for impairment disclosures, unless such loans are the subject of a troubled debt restructure.

Loans whose terms are modified are classified as troubled debt restructured loans if the Corporation grants such borrowers concessions that it would not otherwise consider and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring generally involve a temporary reduction in interest rate, a below market interest rate given the risk associated with the loan, or an extension of a loan s stated maturity date. Nonaccrual troubled debt restructurings may be restored to accrual status if principal and interest payments, under the modified terms, are current for a sustained period of time and, based on a well-documented credit evaluation of the borrower s financial condition, there is reasonable assurance of repayment. Loans classified as troubled debt restructurings are generally designated as impaired.

The allowance calculation methodology includes further segregation of loan classes into credit quality rating categories. The borrower s overall financial condition, repayment sources, guarantors, and value of collateral, if appropriate, are generally evaluated annually for commercial loans or when credit deficiencies arise, such as delinquent loan payments.

Credit quality risk ratings include regulatory classifications of special mention, substandard, doubtful, and loss. Loans classified special mention have potential weaknesses that deserve management s close attention. If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. Loans classified substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They include loans that are inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified doubtful have all the weaknesses inherent in loans classified substandard with the added characteristic that collection or liquidation in full, on the basis of current conditions and facts, is highly improbable. Loans classified as a loss are considered uncollectible and are charged to the allowance for loan losses. Loans not classified are rated pass.

In addition, federal and state regulatory agencies, as an integral part of their examination process, periodically review the Corporation s allowance for loan losses and may require the Corporation to recognize additions to the allowance based on their judgments about information available to them at the time of their examination, which may not be currently available to management. Based on management s comprehensive analysis of the loan portfolio and economic conditions, management believes the current level of the allowance for loan losses is adequate.

Commercial and Industrial Lending The Corporation originates commercial and industrial loans primarily to businesses located in its primary market area and surrounding areas. These loans are used for various business purposes which include short-term loans and lines of credit to finance machinery and equipment purchases, inventory, and accounts receivable. Generally, the maximum term for loans extended on machinery and equipment is based on the projected useful life of such machinery and equipment. Most business lines of credit are written on demand and may be renewed annually.

Commercial and industrial loans are generally secured with short-term assets; however, in many cases, additional collateral such as real estate is provided as additional security for the loan. Loan-to-value maximum values have been established by the Corporation and are specific to the type of collateral. Collateral values may be determined using invoices, inventory reports, accounts receivable aging reports, collateral appraisals, etc.

In underwriting commercial and industrial loans, an analysis is performed to evaluate the borrower s character and capacity to repay the loan, the adequacy of the borrower s capital and collateral, as well as the conditions affecting the borrower. Evaluation of the borrower s past, present and future cash flows is also an important aspect of the Corporation s analysis.

Commercial loans generally present a higher level of risk than other types of loans due primarily to the effect of general economic conditions.

Commercial Real Estate Lending The Corporation engages in commercial real estate lending in its primary market area and surrounding areas. The Corporation s commercial loan portfolio is secured primarily by commercial retail space, office buildings, and hotels. Generally, commercial real estate loans have terms that do not exceed 20 years, have loan-to-value ratios of up to 80% of the appraised value of the property, and are typically secured by personal guarantees of the borrowers.

In underwriting these loans, the Corporation performs a thorough analysis of the financial condition of the borrower, the borrower s credit history, and the reliability and predictability of the cash flow generated by the property securing the loan. Appraisals on properties securing commercial real estate loans originated by the Corporation are performed by independent appraisers.

Commercial real estate loans generally present a higher level of risk than other types of loans due primarily to the effect of general economic conditions and the complexities involved in valuing the underlying collateral.

Commercial Real Estate Construction Lending The Corporation engages in commercial real estate construction lending in its primary market area and surrounding areas. The Corporation s commercial real estate construction lending consists of commercial and residential site development loans, as well as commercial building construction and residential housing construction loans.

The Corporation s commercial real estate construction loans are generally secured with the subject property. Terms of construction loans depend on the specifics of the project, such as estimated absorption rates, estimated time to complete, etc.

In underwriting commercial real estate construction loans, the Corporation performs a thorough analysis of the financial condition of the borrower, the borrower s credit history, and the reliability and predictability of the cash flow generated by the project using feasibility studies, market data, etc. Appraisals on properties securing commercial real estate construction loans originated by the Corporation are performed by independent appraisers.

Commercial real estate construction loans generally present a higher level of risk than other types of loans due primarily to the effect of general economic conditions and the uncertainties surrounding total construction costs.

Residential Mortgage Lending One-to-four family residential mortgage loan originations, including home equity closed-end loans, are generated by the Corporation s marketing efforts, its present customers, walk-in customers, and referrals. These loans originate primarily within the Corporation s market area or with customers primarily from the market area.

The Corporation offers fixed-rate and adjustable-rate mortgage loans with terms up to a maximum of 30 years for both permanent structures and those under construction. The Corporation s one-to-four family residential mortgage originations are secured primarily by properties located in its primary market area and surrounding areas. The majority of the Corporation s residential mortgage loans originate with a loan-to-value of 80% or less. Loans in excess of 80% are required to have private mortgage insurance.

In underwriting one-to-four family residential real estate loans, the Corporation evaluates both the borrower s ability to make monthly payments and the value of the property securing the loan. Properties securing real estate loans made by the Corporation are appraised by independent appraisers. The Corporation generally requires borrowers to obtain an attorney s title opinion or title insurance, as well as fire and property insurance (including flood insurance, if necessary) in an amount not less than the amount of the loan. The Corporation has not engaged in subprime residential mortgage originations.

Residential mortgage loans present a moderate level of risk due primarily to general economic conditions, as well as a continued weak housing market.

Home Equity Lines of Credit Lending The Corporation originates home equity lines of credit primarily within the Corporation s market area or with customers primarily from the market area. Home equity lines of credit are generated by the Corporation s marketing efforts, its present customers, walk-in customers, and referrals.

Home equity lines of credit are secured by the borrower s primary residence with a maximum loan-to-value of 90% and a maximum term of 20 years. In underwriting home equity lines of credit, a thorough analysis of the borrower s financial ability to repay the loan as agreed is performed. The ability to repay is determined by the borrower s employment history, current financial condition, and credit background.

Home equity lines of credit generally present a moderate level of risk due primarily to general economic conditions, as well as a continued weak housing market.

Junior liens inherently have more credit risk by virtue of the fact that another financial institution may have a higher security position in the case of foreclosure liquidation of collateral to extinguish the debt. Generally, foreclosure actions could become more prevalent if the real estate market continues to be weak and property values deteriorate.

Consumer Lending The Corporation offers a variety of unsecured and secured consumer loans, including those for vehicles and mobile homes and those secured by savings deposits. These loans originate primarily within the Corporation s market area or with customers primarily from the market area.

Consumer loan terms vary according to the type and value of collateral and the creditworthiness of the borrower. In underwriting consumer loans, a thorough analysis of the borrower s financial ability to repay the loan as agreed is performed. The ability to repay is determined by the borrower s employment history, current financial condition, and credit background.

Consumer loans may entail greater credit risk than residential mortgage loans or home equity lines of credit, particularly in the case of consumer loans which are unsecured or are secured by rapidly depreciable assets such as automobiles or recreational equipment. In such cases, any repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation. In addition, consumer loan collections are dependent on the borrower s continuing financial stability, and thus are more likely to be affected by adverse personal circumstances. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount which can be recovered on such loans.

The following table presents the classes of the loan portfolio summarized by the aggregate pass rating and the classified ratings of special mention, substandard, and doubtful within the Corporation s internal risk rating system as of September 30, 2013, and December 31, 2012:

In thousands	Pass	Special Mention	Substandard	Doubtful	Total
SEPTEMBER 30, 2013					
Commercial and industrial	**$ 49,823**	**$ 2,088**	**$ 2,939**	**$**	**$ 54,850**
Commercial real estate	**200,074**	**22,099**	**17,153**		**239,326**
Commercial real estate construction	**5,372**	**1,833**	**5,478**		**12,683**
Residential mortgage	**337,407**	**2,306**	**3,675**		**343,388**
Home equity lines of credit	**52,499**	**587**	**376**		**53,462**
Consumer	**14,339**				**14,339**
	$ 659,514	**$ 28,913**	**$ 29,621**	**$**	**$ 718,048**
DECEMBER 31, 2012					
Commercial and industrial	$ 44,072	$ 2,491	$ 2,441	$	$ 49,004
Commercial real estate	205,449	20,379	17,191		243,019
Commercial real estate construction	7,354	9,820	1,980		19,154
Residential mortgage	321,986	4,502	2,348		328,836
Home equity lines of credit	51,096	1,776	258		53,130
Consumer	14,993				14,993
	$ 644,950	$ 38,968	$ 24,218	$	$ 708,136

The following table summarizes information relative to impaired loans by loan portfolio class as of September 30, 2013, and December 31, 2012:

In thousands	Impaired Loans with Allowance: Recorded Investment	Impaired Loans with Allowance: Unpaid Principal Balance	Impaired Loans with Allowance: Related Allowance	Impaired Loans with No Allowance: Recorded Investment	Impaired Loans with No Allowance: Unpaid Principal Balance
SEPTEMBER 30, 2013					
Commercial and industrial	**$**	**$**	**$**	**$ 179**	**$ 1,294**
Commercial real estate	**455**	**699**	**455**	**11,407**	**11,607**
Commercial real estate construction	**3,811**	**3,811**	**906**	**788**	**1,062**
Residential mortgage	**1,050**	**1,050**	**404**	**1,164**	**1,526**
	$ 5,316	**$ 5,560**	**$ 1,765**	**$ 13,538**	**$ 15,489**
DECEMBER 31, 2012					
Commercial and industrial	$ 146	$ 146	$ 29	$ 195	$ 1,310
Commercial real estate	237	276	7	8,772	9,216
Commercial real estate construction				854	1,128
Residential mortgage				938	1,263
	$ 383	$ 422	$ 36	$ 10,759	$ 12,917

The following table summarizes information in regards to average of impaired loans and related interest income by loan portfolio class for the three months ended September 30, 2013 and 2012:

In thousands	Impaired Loans with Allowance: Average Recorded Investment	Impaired Loans with Allowance: Interest Income	Impaired Loans with No Allowance: Average Recorded Investment	Impaired Loans with No Allowance: Interest Income
SEPTEMBER 30, 2013				
Commercial and industrial	**$**	**$**	**$ 183**	**$**
Commercial real estate	**228**		**11,997**	**107**
Commercial real estate construction	**4,168**	**34**	**788**	
Residential mortgage	**1,170**		**999**	**2**
	$ 5,566	**$ 34**	**$ 13,967**	**$ 109**
SEPTEMBER 30, 2012				
Commercial and industrial	$	$	$ 215	$
Commercial real estate	1,092		8,676	
Commercial real estate construction			899	
Residential mortgage			1,495	
	$ 1,092	$	$ 11,285	$

The following table summarizes information in regards to average of impaired loans and related interest income by loan portfolio class for the nine months ended September 30, 2013 and 2012:

	Impaired Loans with Allowance		Impaired Loans with No Allowance	
In thousands	**Average Recorded Investment**	**Interest Income**	**Average Recorded Investment**	**Interest Income**
SEPTEMBER 30, 2013				
Commercial and industrial	**$ 73**	**$**	**$ 189**	**$**
Commercial real estate	**232**		**11,133**	**466**
Commercial real estate construction	**3,430**	**169**	**821**	
Residential mortgage	**935**		**967**	**8**
	$ 4,670	**$ 169**	**$ 13,110**	**$ 474**
SEPTEMBER 30, 2012				
Commercial and industrial	$ 503	$	$ 229	$
Commercial real estate	804		8,049	
Commercial real estate construction	420		1,339	
Residential mortgage	22		1,504	
	$ 1,749	$	$ 11,121	$

No additional funds are committed to be advanced in connection with impaired loans.

The following table presents nonaccrual loans by loan portfolio class as of September 30, 2013, and December 31, 2012:

In thousands	**September 30, 2013**	**December 31, 2012**
Commercial and industrial	**$ 179**	$ 341
Commercial real estate	**4,893**	4,515
Commercial real estate construction	**788**	854
Residential mortgage	**1,905**	617
	$ 7,765	$ 6,327

The following table summarizes information relative to troubled debt restructurings by loan portfolio class as of September 30, 2013, and December 31, 2012:

In thousands	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Recorded Investment at Period End
SEPTEMBER 30, 2013			
Nonaccruing troubled debt restructurings:			
Commercial and industrial	**$ 490**	**$ 485**	**$ 170**
Commercial real estate	**1,021**	**1,021**	**656**
Commercial real estate construction	**1,548**	**1,541**	**694**
Total nonaccruing troubled debt restructurings	**3,059**	**3,047**	**1,520**
Accruing troubled debt restructurings:			
Commercial real estate	**7,118**	**7,170**	**6,969**
Residential mortgage	**336**	**336**	**309**
Total accruing troubled debt restructurings	**7,454**	**7,506**	**7,278**
Total troubled debt restructurings	**$ 10,513**	**$ 10,553**	**$ 8,798**
DECEMBER 31, 2012			
Nonaccruing troubled debt restructurings:			
Commercial and industrial	$ 490	$ 485	$ 187
Commercial real estate	1,304	1,304	953
Commercial real estate construction	1,548	1,541	760
Total nonaccruing troubled debt restructurings	3,342	3,330	1,900
Accruing troubled debt restructurings:			
Commercial real estate	4,577	4,577	4,494
Residential mortgage	336	336	321
Total accruing troubled debt restructurings	4,913	4,913	4,815
Total troubled debt restructurings	$ 8,255	$ 8,243	$ 6,715

All of the Corporation s troubled debt restructured loans are also impaired loans, of which some have resulted in a specific allocation and, subsequently, a charge-off as appropriate. During the nine months ended September 30, 2013, one troubled debt restructured loan defaulted in the amount of $237,000 and was transferred to foreclosed assets held for resale. All other troubled debt restructured loans were current with respect to their associated terms, except for one loan which has had periodic late payments. There were no defaults of troubled debt restructured loans during the three months ended September 30, 2013. During the three and nine months ended September 30, 2012, there were no defaulted troubled debt restructurings. One loan was determined to be a troubled debt restructured loan during 2009 and modified during 2011, two were determined to be troubled debt restructured loans during 2010, three were determined to be troubled debt restructured loans during 2012, and one was determined to be a troubled debt restructured loan during 2013.

There are forbearance agreements on all loans currently classified as troubled debt restructurings, except for two loans in which the forbearance agreement has expired and one loan in which a modification took place, all of which remain classified as troubled debt restructured loans. All of these troubled debt restructured loans have resulted in additional principal repayment. The terms of these troubled debt restructured loans vary whereby principal payments have been decreased, interest rates have been reduced, and/or the loan will be repaid as collateral is sold.

The following table summarizes loans whose terms have been modified resulting in troubled debt restructurings during the three and nine months ended September 30, 2013 and 2012:

Dollars in thousands	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Recorded Investment at Period End
THREE MONTHS ENDED SEPTEMBER 30, 2013				
Troubled debt restructurings:		**$**	**$**	**$**
NINE MONTHS ENDED SEPTEMBER 30, 2013				
Troubled debt restructurings:				
Commercial real estate	**1**	**$ 2,541**	**$ 2,593**	**$ 2,559**
THREE MONTHS ENDED SEPTEMBER 30, 2012				
Troubled debt restructurings:				
Commercial real estate	2	$ 5,225	$ 5,225	$ 5,142
Residential mortgage	1	$ 336	$ 336	$ 324
NINE MONTHS ENDED SEPTEMBER 30, 2012				
Troubled debt restructurings:				
Commercial real estate	2	$ 5,225	$ 5,225	$ 5,142
Residential mortgage	1	$ 336	$ 336	$ 324

The performance and credit quality of the loan portfolio is also monitored by analyzing the age of the loans receivable as determined by the length of time a recorded payment is past due.

The following table presents the classes of the loan portfolio summarized by the past due status as of September 30, 2013, and December 31, 2012:

In thousands	30-59 Days Past Due	60-89 Days Past Due	>90 Days Past Due	Total Past Due	Current	Total Loans Receivable	Loans Receivable >90 Days and Accruing
SEPTEMBER 30, 2013							
Commercial and industrial	**$ 24**	**$ 11**	**$ 191**	**$ 226**	**$ 54,624**	**$ 54,850**	**$ 12**
Commercial real estate	**878**	**894**	**2,184**	**3,956**	**235,370**	**239,326**	**44**
Commercial real estate construction			**788**	**788**	**11,895**	**12,683**	
Residential mortgage	**261**	**1,494**	**3,371**	**5,126**	**338,262**	**343,388**	**1,635**
Home equity lines of credit	**292**			**292**	**53,170**	**53,462**	
Consumer	**12**	**13**	**5**	**30**	**14,309**	**14,339**	**5**
	$ 1,467	**$ 2,412**	**$ 6,539**	**$ 10,418**	**$ 707,630**	**$ 718,048**	**$ 1,696**
DECEMBER 31, 2012							
Commercial and industrial	$ 128	$	$ 342	$ 470	$ 48,534	$ 49,004	$ 1
Commercial real estate	757	1,569	1,502	3,828	239,191	243,019	6

Commercial real estate construction			854	854	18,300	19,154	
Residential mortgage	4,197	2,425	1,339	7,961	320,875	328,836	721
Home equity lines of credit	353	10	43	406	52,724	53,130	43
Consumer	8	4		12	14,981	14,993	
	$ 5,443	$ 4,008	$ 4,080	$ 13,531	$ 694,605	$ 708,136	$ 771

The following tables summarize the allowance for loan losses and recorded investment in loans receivable:

In thousands	Commercial and Industrial	Commercial Real Estate	Commercial Real Estate Construction	Residential Mortgage	Home Equity Lines of Credit	Consumer	Unallocated	Total
AS OF AND FOR THE PERIODS ENDED SEPTEMBER 30, 2013								
Allowance for Loan Losses								
Beginning balance - July 1, 2013	**$ 1,470**	**$ 5,852**	**$ 1,542**	**$ 4,149**	**$ 531**	**$ 826**	**$ 2,869**	**$ 17,239**
Charge-offs	**(41)**	**(396)**		**(133)**		**(29)**		**(599)**
Recoveries	**5**			**1**		**1**		**7**
Provisions	**346**	**934**	**(462)**	**87**	**7**	**85**	**(847)**	**150**
Ending balance - September 30, 2013	**$ 1,780**	**$ 6,390**	**$ 1,080**	**$ 4,104**	**$ 538**	**$ 883**	**$ 2,022**	**$ 16,797**
Beginning balance - January 1, 2013	**$ 1,507**	**$ 6,576**	**$ 518**	**$ 3,721**	**$ 517**	**$ 633**	**$ 3,353**	**$ 16,825**
Charge-offs	**(133)**	**(540)**		**(729)**		**(158)**		**(1,560)**
Recoveries	**226**			**2**		**4**		**232**
Provisions	**180**	**354**	**562**	**1,110**	**21**	**404**	**(1,331)**	**1,300**
Ending balance - September 30, 2013	**$ 1,780**	**$ 6,390**	**$ 1,080**	**$ 4,104**	**$ 538**	**$ 883**	**$ 2,022**	**$ 16,797**
Ending balance: individually evaluated for impairment	**$**	**$ 455**	**$ 906**	**$ 404**	**$**	**$**	**$**	**$ 1,765**
Ending balance: collectively evaluated for impairment	**$ 1,780**	**$ 5,935**	**$ 174**	**$ 3,700**	**$ 538**	**$ 883**	**$ 2,022**	**$ 15,032**
Loans Receivable								
Ending balance	**$ 54,850**	**$ 239,326**	**$ 12,683**	**$ 343,388**	**$ 53,462**	**$ 14,339**	**$**	**$ 718,048**
Ending balance: individually evaluated for impairment	**$ 179**	**$ 11,862**	**$ 4,599**	**$ 2,214**	**$**	**$**	**$**	**$ 18,854**
Ending balance: collectively evaluated for impairment	**$ 54,671**	**$ 227,464**	**$ 8,084**	**$ 341,174**	**$ 53,462**	**$ 14,339**	**$**	**$ 699,194**
AS OF AND FOR THE PERIODS ENDED SEPTEMBER 30, 2012								
Allowance for Loan Losses								
Beginning Balance - July 1, 2012	$ 1,515	$ 6,369	$ 537	$ 3,633	$ 522	$ 505	$ 2,241	$ 15,322
Charge-offs	(49)	(244)	(158)	(9)		(3)		(463)
Recoveries	7		1			1		9
Provisions	87	264	148	83	6	21	516	1,125
Ending balance - September 30, 2012	$ 1,560	$ 6,389	$ 528	$ 3,707	$ 528	$ 524	$ 2,757	$ 15,993
Beginning Balance - January 1, 2012	$ 2,582	$ 6,007	$ 548	$ 3,624	$ 507	$ 419	$ 1,795	$ 15,482
Charge-offs	(2,136)	(283)	(538)	(218)	(51)	(54)		(3,280)
Recoveries	15	250	149			2		416
Provisions	1,099	415	369	301	72	157	962	3,375
	$ 1,560	$ 6,389	$ 528	$ 3,707	$ 528	$ 524	$ 2,757	$ 15,993

Ending balance - September 30, 2012								
Ending balance: individually evaluated for impairment	$	$ 15	$	$	$	$	$	$ 15
Ending balance: collectively evaluated for impairment	$ 1,560	$ 6,374	$ 528	$ 3,707	$ 528	$ 524	$ 2,757	$ 15,978
Loans Receivable								
Ending balance	$ 53,201	$ 239,397	$ 19,211	$ 321,987	$ 52,830	$ 15,449	$	$ 702,075
Ending balance: individually evaluated for impairment	$ 209	$ 9,572	$ 877	$ 1,492	$	$	$	$ 12,150
Ending balance: collectively evaluated for impairment	$ 52,992	$ 229,825	$ 18,334	$ 320,495	$ 52,830	$ 15,449	$	$ 689,925

AS OF DECEMBER 31, 2012								
Ending balance	$ 1,507	$ 6,576	$ 518	$ 3,721	$ 517	$ 633	$ 3,353	$ 16,825
Ending balance: collectively evaluated for impairment	$ 1,478	$ 6,569	$ 518	$ 3,721	$ 517	$ 633	$ 3,353	$ 16,789
Loans Receivable								
Ending balance: individually evaluated for impairment	$ 341	$ 9,009	$ 854	$ 938	$	$	$	$ 11,142

9. **Fair Value Measurements**

Management uses its best judgment in estimating the fair value of the Corporation s financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Corporation could have realized in a sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective reporting dates and have not been reevaluated or updated for purposes of these consolidated financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each period end.

Fair value measurement and disclosure guidance defines fair value as the price that would be received to sell the asset or transfer the liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions.

Fair value measurement and disclosure guidance provides a list of factors that a reporting entity should evaluate to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability. When the reporting entity concludes there has been a significant decrease in the volume and level of activity for the asset or liability, further analysis of the information from that market is needed and significant adjustments to the related prices may be necessary to estimate fair value in accordance with fair value measurement and disclosure guidance.

This guidance further clarifies that when there has been a significant decrease in the volume and level of activity for the asset or liability, some transactions may not be orderly. In those situations, the entity must evaluate the weight of the evidence to determine whether the transaction is orderly. The guidance provides a list of circumstances that may indicate that a transaction is not orderly. A transaction price that is not associated with an orderly transaction is given little, if any, weight when estimating fair value.

Fair value measurement and disclosure guidance establishes a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level

1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2: Quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability.

Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported with little or no market activity).

An asset or liability s level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

For assets measured at fair value, the fair value measurements by level within the fair value hierarchy, and the basis of measurement used, at September 30, 2013, and December 31, 2012, are as follows:

		September 30, 2013			
In thousands	**Basis**	**Total**	**Level 1**	**Level 2**	**Level 3**
U.S. Government and agencies		**$ 21,769**	**$**	**$ 21,769**	**$**
Mortgage-backed securities, residential		**57,882**		**57,882**	
State and municipal		**42,449**		**42,449**	
Corporate bonds		**11,160**		**11,160**	
CRA mutual fund		**1,048**	**1,048**		
Stock in other banks		**855**	**855**		
Total securities available for sale	**Recurring**	**$ 135,163**	**$ 1,903**	**$ 133,260**	**$**
Impaired loans	**Nonrecurring**	**$ 9,803**	**$**	**$**	**$ 9,803**
Foreclosed assets held for resale	**Nonrecurring**	**$ 632**	**$**	**$**	**$ 632**

		December 31, 2012			
In thousands	**Basis**	**Total**	**Level 1**	**Level 2**	**Level 3**
U.S. Government and agencies		$ 24,241	$	$ 24,241	$
Mortgage-backed securities, residential		80,583		80,583	
State and municipal		51,804		51,804	
Corporate bonds		7,286		7,286	
CRA mutual fund		1,096	1,096		
Stock in other banks		780	780		
Total securities available for sale	Recurring	$ 165,790	$ 1,876	$ 163,914	$
Impaired loans	Nonrecurring	$ 2,415	$	$	$ 2,415
Foreclosed assets held for resale	Nonrecurring	$ 2,338	$	$	$ 2,338

The following information should not be interpreted as an estimate of the fair value of the entire Corporation since a fair value calculation is only provided for a limited portion of the Corporation s assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Corporation s disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Corporation s financial instruments at September 30, 2013, and December 31, 2012:

Cash and Cash Equivalents (Carried at Cost)

The carrying amounts reported in the consolidated statement of condition for cash and short-term instruments approximate those assets fair value. U.S. currency is Level 1 and cash equivalents are Level 2.

Securities

The fair values of securities available for sale (carried at fair value) and held to maturity (carried at amortized cost) are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or by matrix pricing (Level 2) which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific security but rather by relying on the security s relationship to other benchmark quoted prices. The Corporation uses an independent service provider to provide matrix pricing, and uses the valuation of another provider to compare for reasonableness.

Loans Held for Sale (Carried at Lower of Cost or Fair Value)

The fair values of mortgage loans held for sale are determined based on amounts to be received at settlement by establishing the respective buyer requirement or market interest rates.

Loans (Carried at Cost)

The fair values of loans are estimated using discounted cash flow analyses, as well as using market rates at the balance sheet date that reflect the credit and interest rate risk inherent in the loans. Projected future cash flows are calculated based upon contractual maturity or call dates, projected repayments, and prepayments of principal. Generally, for variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values.

Impaired Loans (Generally Carried at Fair Value)

Loans for which the Corporation has measured impairment are generally based on the fair value of the loan s collateral. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements. The fair value consists of the loan balances less the valuation allowance and/or charge-offs.

Foreclosed Assets Held for Resale

The fair value of real estate acquired through foreclosure is based on independent third-party appraisals of the properties. These assets are included as Level 3 fair values, based upon appraisals that consider the sales prices of similar properties in the proximate vicinity.

It is the policy of the Corporation to have the initial market value of a foreclosed asset held for resale determined by an independent third party valuation. If the Corporation already has a valid appraisal on file for the property and that appraisal has been completed within the previous 12 months, another appraisal shall not be required when the Corporation acquires ownership of that real estate. Further, the Corporation shall update the market value of each foreclosed asset with an independent third party valuation at least every 18 months, or more frequently if management believes that there is an indication that the fair value has declined. These valuations may be adjusted downward to account for specialized use of the property, change in the condition of the real estate, change in local market and economic conditions, and other specific factors involving the collateral.

Restricted Investment in Bank Stock (Carried at Cost)

The carrying amount of required and restricted investment in correspondent bank stock approximates fair value, and considers the limited marketability of such securities.

Accrued Interest Receivable and Payable (Carried at Cost)

The carrying amounts of accrued interest receivable and accrued interest payable approximate their fair value.

Deposits (Carried at Cost)

The fair values disclosed for demand deposits (e.g., interest and non-interest checking, savings, and money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (e.g., their carrying amounts). Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates currently being offered in the market on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Short-Term Borrowings (Carried at Cost)

The carrying amounts of short-term borrowings approximate their fair values.

Long-Term Borrowings (Carried at Cost)

The fair values of Federal Home Loan Bank (FHLB) advances are estimated using discounted cash flow analysis, based on quoted prices for new FHLB advances with similar credit risk characteristics, terms, and remaining maturity. The prices obtained from this active market represent a market value that is deemed to represent the transfer price if the liability were assumed by a third party.

Off-Balance Sheet Credit-Related Instruments

The fair values for the Corporation s off-balance sheet financial instruments (lending commitments and letters of credit) are based on fees currently charged in the market to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties credit standing.

The following presents the carrying amount, fair value, and placement in the fair value hierarchy of the Corporation s financial instruments as of September 30, 2013, and December 31, 2012:

	September 30, 2013				
In thousands	**Carrying Amount**	**Fair Value**	**Level 1**	**Level 2**	**Level 3**
Financial assets:					
Cash and due from banks	**$ 16,371**	**$ 16,371**	**$ 10,747**	**$ 5,624**	**$**
Interest-bearing deposits in banks	**2,856**	**2,856**	**2,856**		
Investment securities available for sale	**135,163**	**135,163**	**1,903**	**133,260**	
Investment securities held to maturity	**96,255**	**94,667**		**94,667**	
Loans held for sale	**603**	**603**		**603**	
Loans, less allowance for loan losses	**701,251**	**719,953**			**719,953**
Accrued interest receivable	**3,134**	**3,134**		**3,134**	
Restricted investment in bank stocks	**4,189**	**4,189**		**4,189**	
Financial liabilities:					
Deposits	**819,231**	**819,469**		**819,469**	
Short-term borrowings	**57,418**	**57,418**		**57,418**	
Long-term borrowings	**47,767**	**49,461**		**49,461**	
Accrued interest payable	**695**	**695**		**695**	
Off-balance sheet financial instruments					

	December 31, 2012				
In thousands	**Carrying Amount**	**Fair Value**	**Level 1**	**Level 2**	**Level 3**
Financial assets:					
Cash and due from banks	$ 19,078	$ 19,078	$ 5,832	$ 13,246	$
Interest-bearing deposits in banks	32,307	32,307	32,307		
Investment securities available for sale	165,790	165,790	1,876	163,914	
Investment securities held to maturity	50,159	50,980		50,980	
Loans held for sale	6,687	6,687		6,687	
Loans, less allowance for loan losses	691,311	724,982			724,982
Accrued interest receivable	3,360	3,360		3,360	
Restricted investment in bank stocks	5,318	5,318		5,318	
Financial liabilities:					
Deposits	834,176	835,640		835,640	
Short-term borrowings	47,303	47,303		47,303	
Long-term borrowings	59,954	62,296		62,296	
Accrued interest payable	1,114	1,114		1,114	

Off-balance sheet financial instruments

The following table presents additional quantitative information about assets measured at fair value on a nonrecurring basis for which the Corporation has utilized Level 3 inputs to determine fair value:

		Quantitative Information about Level 3 Fair Value Measurements			
Dollars in thousands	**Fair Value Estimate**	**Valuation Technique**	**Unobservable Input**	**Range**	**Weighted Average**
September 30, 2013					
Impaired loans	**$ 9,803**	**Appraisal of collateral (1)**	**Appraisal adjustments (2)**	**(10) - (50)%**	**(17)%**
Foreclosed assets held for resale	**$ 632**	**Appraisal of collateral (1) (3)**	**Appraisal adjustments (2)**	**(10) - (50)%**	**(35)%**
December 31, 2012					
Impaired loans	$ 2,415	Appraisal of collateral (1)	Appraisal adjustments (2)	(10) - (50)%	(16)%
Foreclosed assets held for resale	$ 2,338	Appraisal of collateral (1) (3)	Appraisal adjustments (2)	(10) - (50)%	(40)%

(1) Fair value is generally determined through independent third-party appraisals of the underlying collateral, which generally includes various Level 3 inputs which are not observable.

(2) Appraisals may be adjusted downwards by management for qualitative factors such as economic conditions and estimated liquidation expenses. The range of liquidation expenses and other appraisal adjustments are presented as a percentage of the appraisal. Higher downward adjustments are caused by negative changes to the collateral or conditions in the real estate market, actual offers or sales contracts received, or age of the appraisal.

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

10. **Securities Sold Under Agreements to Repurchase (Repurchase Agreements)**

The Corporation enters into agreements under which it sells securities subject to an obligation to repurchase the same or similar securities. Under these arrangements, the Corporation may transfer legal control over the assets but still retain effective control through an agreement that both entitles and obligates the Corporation to repurchase the assets.

As a result, these repurchase agreements are accounted for as collateralized financing agreements (i.e., secured borrowings) and not as a sale and subsequent repurchase of securities. The obligation to repurchase the securities is reflected as a liability in the Corporation s consolidated statements of condition, while the securities underlying the repurchase agreements remain in the respective investment securities asset accounts. In other words, there is no offsetting or netting of the investment securities assets with the repurchase agreement liabilities. In addition, as the Corporation does not enter into reverse repurchase agreements, there is no such offsetting to be done with the repurchase agreements.

The right of setoff for a repurchase agreement resembles a secured borrowing, whereby the collateral would be used to settle the fair value of the repurchase agreement should the Corporation be in default (e.g., fails to make an interest payment to the counterparty). For private institution repurchase agreements, if the private institution counterparty were to default (e.g., declare bankruptcy), the Corporation could cancel the repurchase agreement (i.e., cease payment of principal and interest), and attempt collection on the amount of collateral value in excess of the repurchase agreement fair value. The collateral is held by a third-party financial institution in the counterparty s custodial account. The counterparty has the right to sell or repledge the investment securities. For government entity repurchase agreements, the collateral is held by the Corporation in a segregated custodial account under a tri-party agreement.

The following table presents the liabilities subject to an enforceable master netting arrangement or repurchase agreements as of September 30, 2013 and December 31, 2012:

					Gross Amounts Not Offset in the Statements of Condition		
Dollars in thousands	**Gross Amounts of Recognized Liabilities**	**Gross Amounts Offset in the Statements of Condition**	**Net Amounts of Liabilities Presented in the Statements of Condition**	**Financial Instruments**	**Cash Collateral Pledged**	**Net Amount**
September 30, 2013						
Repurchase agreements						
Commercial customers and government entities	**(a) $ 55,618**	**$**	**$ 55,618**	**$ (55,618)**	**$**	**$**
December 31, 2012						
Repurchase agreements						
Commercial customers and government entities	(a) $ 47,303	$	$ 47,303	$ (47,303)	$	$

(a) As of September 30, 2013, and December 31, 2012, the fair value of securities pledged in connection with repurchase agreements was $74,765 and $56,392, respectively.

11. **New Accounting Pronouncements**

There were no new accounting pronouncements affecting the Corporation during the reporting period that were not already adopted.

ACNB CORPORATION

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

INTRODUCTION AND FORWARD-LOOKING STATEMENTS

Introduction

The following is management s discussion and analysis of the significant changes in the financial condition, results of operations, comprehensive income, capital resources, and liquidity presented in its accompanying consolidated financial statements for ACNB Corporation (the Corporation or ACNB), a financial holding company. Please read this discussion in conjunction with the consolidated financial statements and disclosures included herein. Current performance does not guarantee, assure or indicate similar performance in the future.

Forward-Looking Statements

In addition to historical information, this Form 10-Q contains forward-looking statements. Examples of forward-looking statements include, but are not limited to, (a) projections or statements regarding future earnings, expenses, net interest income, other income, earnings or loss per share, asset mix and quality, growth prospects, capital structure, and other financial terms, (b) statements of plans and objectives of management or the Board of Directors, and (c) statements of assumptions, such as economic conditions in the Corporation s market areas. Such forward-looking statements can be identified by the use of forward-looking terminology such as believes , expects , may , intends , will , should , anticipates negative of any of the foregoing or other variations thereon or comparable terminology, or by discussion of strategy. Forward-looking statements are subject to certain risks and uncertainties such as local economic conditions, competitive factors, and regulatory limitations. Actual results may differ materially from those projected in the forward-looking statements. Such risks, uncertainties and other factors that could cause actual results and experience to differ from those projected include, but are not limited to, the following: the effects of new laws and regulations, specifically the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act; impacts of the new capital and liquidity requirements of the Basel III standards and other regulatory pronouncements, regulations and rules; ineffectiveness of the business strategy due to changes in current or future market conditions; future actions or inactions of the United States government, including a failure to increase the government debt limit or a prolonged shutdown of the federal government; the effects of economic deterioration and the prolonged economic malaise on current customers, specifically the effect of the economy on loan customers ability to repay loans; the effects of competition, and of changes in laws and regulations on competition, including industry consolidation and development of competing financial products and services; interest rate movements; difficulties in integrating and operating distinct business operations, including information technology difficulties; challenges in establishing and maintaining operations in new markets; volatilities in the securities markets; and, slow economic conditions. We caution readers not to place undue reliance on these forward-looking statements. They only reflect management s analysis as of this date. The Corporation does not revise or update these forward-looking statements to reflect events or changed circumstances. Please carefully review the risk factors described in other documents the Corporation files from time to time with the Securities and Exchange Commission, including the Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, and any Current Reports on Form 8-K.

CRITICAL ACCOUNTING POLICIES

The accounting policies that the Corporation s management deems to be most important to the portrayal of its financial condition and results of operations, and that require management s most difficult, subjective or complex judgment, often result in the need to make estimates about the

effect of such matters which are inherently uncertain. The following policies are deemed to be critical accounting policies by management:

The allowance for loan losses represents management s estimate of probable losses inherent in the loan portfolio. Management makes numerous assumptions, estimates and adjustments in determining an adequate allowance. The Corporation assesses the level of potential loss associated with its loan portfolio and provides for that exposure through an allowance for loan losses. The allowance is established through a provision for loan losses charged to earnings. The allowance is an estimate of the losses inherent in the loan portfolio as of the end of each reporting period. The Corporation assesses the adequacy of its allowance on a quarterly basis. The specific methodologies applied on a consistent basis are discussed in greater detail under the caption, *Allowance for Loan Losses*, in a subsequent section of this Management s Discussion and Analysis of Financial Condition and Results of Operations.

The evaluation of securities for other-than-temporary impairment requires a significant amount of judgment. In estimating other-than-temporary impairment losses, management considers various factors including the length of time the fair value has been below cost, the financial condition of the issuer, and the Corporation s intent to sell, or requirement to sell, the security before recovery of its value. Declines in fair value that are determined to be other than temporary are charged against earnings.

Accounting Standard Codification (ASC) Topic 350, *Intangibles Goodwill and Other*, requires that goodwill is not amortized to expense, but rather that it be assessed or tested for impairment at least annually. Impairment write-downs are charged to results of operations in the period in which the impairment is determined. The Corporation did not identify any impairment on its outstanding goodwill from its most recent testing, which was performed as of October 1, 2012. If certain events occur which might indicate goodwill has been impaired, the goodwill is tested for impairment when such events occur. The Corporation has not identified any such events and, accordingly, has not tested goodwill for impairment during the nine months ended September 30, 2013. During the quarter ended June 30, 2012, the Corporation changed its method of applying ASC Topic 350 such that the annual goodwill impairment testing date was changed from December 31 to October 1. This new testing date is preferable under the circumstances, because it allows the Corporation more time to accurately complete its impairment testing process in order to incorporate the results in the annual consolidated financial statements. Other acquired intangible assets with finite lives, such as customer lists, are required to be amortized over the estimated lives. These intangibles are generally amortized using the straight line method over estimated useful lives of ten years.

The Corporation recognizes deferred tax assets and liabilities for the future effects of temporary differences and tax credits. Enacted tax rates are applied to cumulative temporary differences based on expected taxable income in the periods in which the deferred tax asset or liability is anticipated to be realized. Future tax rate changes could occur that would require the recognition of income or expense in the consolidated statements of income in the period in which they are enacted. Deferred tax assets must be reduced by a valuation allowance if in management s judgment it is more likely than not that some portion of the asset will not be realized. Management may need to modify their judgments in this regard from one period to another should a material change occur in the business environment, tax legislation, or in any other business factor that could impair the Corporation s ability to benefit from the asset in the future.

RESULTS OF OPERATIONS

Quarter ended September 30, 2013, compared to quarter ended September 30, 2012

Executive Summary

Net income for the three months ended September 30, 2013, was $2,308,000, compared to $2,304,000 for the same quarter in 2012, an increase of $4,000 or less than 1.0%. Earnings per share was $0.39 in 2013 and 2012. Net interest income decreased $257,000, or 3.0%, as decreases in interest income were not totally matched by decreases in interest expense. Provision for loan losses decreased $975,000, or 86.7%, based on the adequacy analysis of the allowance for loan losses at the end of each period. Other income decreased $125,000, or 4.2%, due primarily to lower revenue from the insurance subsidiary and lower fees from mortgage sales. Other expenses increased $554,000, or 7.4%, due primarily to higher costs on foreclosed real estate.

Net Interest Income

Net interest income totaled $8,284,000 for the quarter ended September 30, 2013, compared to $8,541,000 for the same period in 2012, a decrease of $257,000 or 3.0%. Net interest income decreased due to a decrease in interest income to a greater degree than the decrease in interest expense, both resulting from reductions in market rates associated with the continued low interest rates maintained by the Federal Reserve Bank and the general interest rate environment. Interest income decreased $847,000, or 8.4%, due to declines in the Federal Funds Target Rate and other market driver rates. These driver rates affect new loan originations and are indexed to a portion of the loan portfolio in that a decrease in the driver rates decreases the yield on new loans and on existing loans at subsequent interest rate reset dates. In this manner, interest income will continue to decrease as new loans replace paydowns on existing loans and variable rate loans reset to new lower rates. In addition, interest income was lower as a result of investment securities paydowns that were reinvested at much lower market rates that were prevailing at the time of reinvestment due to uneven domestic and international economic conditions, compounded by Federal Reserve Bank buying activities referred to as Quantitative Easing. A portion of earning assets was left in short-term money market type accounts during the third quarter of 2013, because of the interest rate risk and liquidity tolerances set for the current mix of deposit funding sources. As to funding costs, interest rates on alternative funding sources, such as the Federal Home Loan Bank (FHLB), and other market driver rates are factors in rates the Corporation and the local market pay for deposits. However, during the third quarter of 2013, several of the core deposit rates continued at practical floors after the Federal Open Market Committee decreased the Federal Funds Target Rate by 400 basis points during 2008 and has maintained it at 0% to 0.25% since that time. Interest expense decreased $590,000, or 38.7%. For more information about interest rate risk, please refer to Item 7A - Quantitative and Qualitative Disclosures about Market Risk in the Annual Report on Form 10-K for the fiscal year ended December 31, 2012, and filed with the SEC on March 15, 2013. Over the longer term, the Corporation continues its strategic direction to increase asset yield and interest income by means of loan growth and rebalancing the composition of earning assets.

The net interest spread for the third quarter of 2013 was 3.34% compared to 3.38% during the same period in 2012. Also comparing the third quarter of 2013 to 2012, the yield on interest earning assets decreased by 0.30% and the cost of interest bearing liabilities decreased by 0.26%. The net interest margin was 3.42% for the third quarter of 2013 and 3.49% for the third quarter of 2012. The net interest margin decline was mainly a result of the rate of decline in the yield on assets decreasing to a greater degree than the decline in funding rates due to funding rates approaching practical floors on deposits as described above.

Average earning assets were $962,610,000 during the third quarter of 2013, an increase of $11,126,000 from the average for the third quarter of 2012. Average interest bearing liabilities were $795,176,000 in the third quarter of 2013, a decrease of $29,628,000 from the same quarter in 2012.

Provision for Loan Losses

The provision for loan losses was $150,000 in the third quarter of 2013 compared to $1,125,000 in the third quarter of 2012, a decrease of $975,000 or 86.7%. The decrease was a result of analysis of the adequacy of the allowance for loan losses. More specifically, even though net charge-offs increased, provision expense decreased due to the scaling back of the unallocated portion of the allowance in proportion to substandard loans in accordance with management s belief that adequate collateralization exists for substandard loans in accordance with GAAP. Each quarter, the Corporation measures risk in the loan portfolio compared with the balance in the allowance for loan losses and the current evaluation factors. For more information, please refer to *Allowance for Loan Losses* in the following Financial Condition section of this Management s Discussion and Analysis of Financial Condition and Results of Operations. ACNB charges confirmed loan losses to the allowance and credits the allowance for recoveries of previous loan charge-offs. For the third quarter of 2013, the Corporation had net charge-offs of $592,000, as compared to net charge-offs of $454,000 for the third quarter of 2012.

Other Income

Total other income was $2,847,000 for the three months ended September 30, 2013, down $125,000, or 4.2%, from the third quarter of 2012. Fees from deposit accounts decreased by $52,000, or 8.0%, due to decreased volume. Various specific government regulations effectively limit fee assessments related to deposit accounts, making future revenue levels uncertain. Revenue from ATM and debit card transactions increased 16.4% to $376,000 due to higher volume. The current increase resulted from consumer desire to use more electronic delivery channels; however, regulations or legal challenges for large financial institutions may impact industry pricing for such transactions and fees in connection therewith in future periods, the effect of which cannot be currently quantified. Income from fiduciary activities, which include both institutional and personal trust and investment management services, totaled $333,000 for the three months ended September 30, 2013, as compared to $288,000 during the third quarter of 2012, a 15.6% increase as a result of more estate fee income, which is inherently sporadic in nature, in the third quarter of 2013 and higher amounts of assets under management. Earnings on bank-owned life insurance decreased by $9,000, or 3.5%, as a result of lowered crediting rates. In addition, a gain on life insurance proceeds was recognized in the third quarter of 2012, and no such gain was recognized in third quarter 2013. At the Corporation s wholly-owned insurance subsidiary, Russell Insurance Group, Inc. (RIG), revenue was down by $54,000, or 4.8%, to $1,079,000, due to the non-renewal of a large commercial account and actions by insurance carriers to reduce commissions paid to agencies such as RIG. Contingent or extra commission payments from insurance carriers are mostly received in March and April of each year, and the amount is at the discretion of the insurance carriers in accordance with applicable insurance regulations. Heightened pressure on commissions is expected to continue in this business line, and contingent commissions are not predictable. Other income in the quarter ended September 30, 2013, was down by $45,000, or 17.2%, to $217,000 due to decreased fees related to sales of residential mortgages as increases in market rates decreased refinancing activity.

Impairment Testing

RIG has certain long-lived assets, including purchased intangible assets subject to amortization, such as insurance books of business, and associated goodwill assets, which are reviewed for impairment annually or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the statement of condition and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

Goodwill, which has an indefinite useful life, is evaluated for impairment annually and is evaluated for impairment more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset s fair value. Recent changes to accounting rules permit an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. The goodwill impairment analysis currently used by the Corporation is a two-step test. The first step, used to identify potential impairment, involves comparing the reporting unit s estimated fair value to its carrying value including goodwill. If the estimated fair value of the reporting unit exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value exceeds the estimated fair value, there is an indication of potential impairment and the second step is performed to measure the amount of impairment. If required, the second step involves calculating an implied fair value of goodwill for the reporting unit for which the first step indicated potential impairment. The implied fair value of goodwill is determined in a manner similar to the amount of goodwill calculated in a business combination, by measuring the excess of the estimated fair value of the reporting unit to a group of likely buyers whose cash flow estimates could differ from those of the reporting entity, as determined in the first step, over the aggregate estimated fair values of the individual assets, liabilities and identifiable intangibles as if the reporting unit was being acquired in a business combination. If the implied fair value of goodwill exceeds the carrying value of goodwill assigned to the reporting unit, there is no impairment. If the carrying value of goodwill assigned to a reporting unit exceeds the implied fair value of the goodwill, an impairment charge is recorded for the excess. Subsequent reversal of goodwill impairment losses is not permitted. At the last test, commissions from insurance sales were up, although RIG s stand alone net income decreased because of startup costs of a new business line and earned incentive payments. The testing for potential impairment involves methods that include both current and projected income amounts, and the fair value remained above the carrying value as of the annual impairment test date. Therefore, the results of the annual evaluations to date have determined that there is no impairment of goodwill, including the most recent testing at October 1, 2012. However, future declines in RIG s net income or changes in external market factors, including likely buyers that are assumed in impairment testing, may require an impairment charge to goodwill.

Other Expenses

The largest component of other expenses is salaries and employee benefits, which increased by $19,000, or less than 1.0%, when comparing the third quarter of 2013 to the same quarter a year ago. Overall, the net increase in salaries and employee benefits was the result of:

- increases from normal promotion and production-based incentive/bonus compensation to employees;

- increased payroll taxes including higher unemployment tax assessments; and,

- health insurance, covering a substantial portion of employees, although stable is projected to increase;

- increased costs associated with benefit plans other than the qualified pension plan; partially offset by,

- decreased defined benefit pension expense, which was down by $15,000, or 12.9%, when comparing the three months ended September 30, 2013, to September 30, 2012, resulting from higher 2012 investment performance offsetting a significant decrease in the discount rate from market rates at historically low levels.

The Corporation s overall pension plan investment strategy is to achieve a mix of investments to meet the long-term rate of return assumption and near-term pension obligations with a diversification of asset types, fund strategies, and fund managers. The mix of investments is adjusted periodically by retaining an advisory firm to recommend appropriate allocations after reviewing the Corporation s risk tolerance on contribution levels, funded status, plan expense, as well as any applicable regulatory requirements. However, the determination of future benefit expense is also dependent on the fair value of assets and the discount rate on the year-end measurement date, which in recent years has experienced low discount rates and fair value volatility. The Corporation amended the defined benefit pension plan effective April 1, 2012, in that no employee hired after March 31, 2012, shall be eligible to participate in the plan and no inactive or former plan participant shall be eligible to again participate in the plan. In addition, a pension provision in a public law known as MAP-21, enacted in July 2012, had no effect on reducing the GAAP expense associated with the plan. The ACNB plan has maintained a well-funded status.

Net occupancy expense decreased by $24,000, or 4.9%, in part due to variations in weather-related costs and preventative maintenance programs. Equipment expense increased by $154,000, or 26.9%, as a result of conversion of a processing vendor and planned small item technology upgrades in 2013.

Professional services expense totaled $232,000 for the third quarter of 2013, as compared to $186,000 for the same period in 2012, an increase of $46,000 or 24.7%. The increase was due to higher expenses related to corporate governance, risk and compliance management engagements, and legal counsel matters for loans.

Marketing and corporate relations expenses were $14,000, or 20.9%, higher in the third quarter of 2013, as compared to the same period of 2012. Marketing expense varies with the timing and amount of advertising production and media expenditures, typically related to the promotion of certain in-market consumer loans.

Foreclosed assets held for resale consist of the fair value of real estate acquired through foreclosure on real estate loan collateral or the acceptance of ownership of real estate in lieu of the foreclosure process. Fair values are based on appraisals that consider the sales prices of similar properties in the proximate vicinity less estimated selling costs. Foreclosed real estate expenses were $503,000 and $116,000 for the quarters ended September 30, 2013 and 2012, respectively. The higher cost in the third quarter of 2013 was primarily due to an unanticipated final loss of $310,000 taken on a property that, during a recent building inspection, was discovered to have extensive hidden damage. Selling to a buyer in as-is condition was deemed to be in the best interest of ACNB. Otherwise, the expense varies based upon the number and mix of commercial and residential real estate properties, unpaid property taxes, and deferred maintenance required upon acquisition. In addition, some properties suffered decreases in value after acquisition, requiring write-downs to fair value during the prolonged marketing cycles for these distressed properties. Foreclosed assets held for resale expenses or recoveries will vary in the remainder of 2013 depending on the successful closing of sales agreements on some existing properties and the unknown expenses related to new properties acquired.

Other tax expenses decreased by $22,000, or 10.0%, due to a sales tax challenge refund that offset a state shareholders equity-based tax that has increased annually regardless of income. Supplies and postage decreased by 9.9% in part due to variation in placing periodic large envelope reorders. Other operating expenses decreased by $8,000, or 1.0%, in the third quarter of 2013, as compared to the third quarter of 2012. The decreases were a result of normal variations in a variety of categories.

Provision for Income Taxes

The Corporation recognized income taxes of $627,000, or 21.4% of pretax income, during the third quarter of 2013, as compared to $592,000, or 20.4% of pretax income, during the same period in 2012. The variances from the federal statutory rate of 34% in both periods are generally due to tax-exempt income (from investments in and loans to state and local units of government at below-market rates, an indirect form of taxation) and investments in low-income housing partnerships (which qualify for federal tax credits). Tax-exempt investments have been allowed to run off due to concerns of interest rate risk related to these investments. The income tax provision during the third quarters ended September 30, 2013 and 2012, included low-income housing tax credits of $170,000 and $139,000, respectively.

Nine months ended September 30, 2013, compared to nine months ended September 30, 2012

Executive Summary

Net income for the nine months ended September 30, 2013, was $7,048,000, compared to $6,668,000 for the same nine months in 2012, an increase of $380,000 or 5.7%. Earnings per share was $1.18 in 2013 and $1.12 in 2012, an increase of 5.4%. Net interest income decreased $593,000, or 2.3%, as decreases in interest income were not totally matched by decreases in interest expense. Provision for loan losses decreased $2,075,000, or 61.5%, based on the adequacy analysis of the allowance for loan losses at the end of each period. Other income increased $79,000, or less than 1.0%, due to additional revenue from higher fees from mortgage sales. Other expenses increased $947,000, or 4.1%, due to a variety of higher expenditures.

Net Interest Income

Net interest income totaled $25,156,000 for the nine months ended September 30, 2013, compared to $25,749,000 for the same period in 2012, a decrease of $593,000 or 2.3%. Net interest income decreased due to a decrease in interest income to a greater degree than the decrease in interest expense, both resulting from reductions in market rates associated with the continued low interest rates maintained by the Federal Reserve Bank and the general interest rate environment. The sharp spike in market rates at the end of June 2013 had little effect on the second and third quarter results, except to lower fair values on the security portfolio. Interest income decreased $2,259,000, or 7.4%, due to declines in the Federal Funds Target Rate and other market driver rates. These driver rates affect new originations and are indexed to a portion of the loan portfolio in that a decrease in the driver rates decreases the yield on new loans and on existing loans at subsequent interest rate reset dates. In this manner, interest income will continue to decrease as new loans replace paydowns on existing loans and variable rate loans reset to new lower rates. In addition, interest income was lower as a result of investment securities paydowns that were reinvested at much lower market rates that were prevailing at the time of reinvestment due to uneven domestic and international economic conditions, compounded by Federal Reserve Bank buying activities referred to as Quantitative Easing. A portion of earning assets was left in short-term money market type accounts because of the interest rate risk and liquidity tolerances set for the current mix of deposit funding sources. As to funding costs, interest rates on alternative funding sources, such as the Federal Home Loan Bank (FHLB), and other market driver rates are factors in rates the Corporation and the local market pay for deposits. However, during the third quarter of 2013, several of the core deposit rates continued at practical floors after the Federal Open Market Committee decreased the Federal Funds Target Rate by 400 basis points during 2008 and has maintained it at 0% to 0.25% since that time. Interest expense decreased $1,666,000, or 35.1%. For more information about interest rate risk, please refer to Item 7A - Quantitative and Qualitative Disclosures about Market Risk in the Annual Report on Form 10-K for the fiscal year ended December 31, 2012, and filed with the SEC on March 15, 2013. Over the longer term, the Corporation continues its strategic direction to increase asset yield and interest income by means of loan growth and rebalancing the composition of earning assets.

The net interest spread for the first nine months of 2013 was 3.41% compared to 3.49% during the same period in 2012. Also comparing the first nine months of 2013 to 2012, the yield on interest earning assets decreased by 0.34% and the cost of interest bearing liabilities decreased by 0.27%. The net interest margin was 3.50% for the first nine months of 2013 and 3.61% for the same period in 2012. The net interest margin decline was mainly a result of the rate of decline in the yield on assets decreasing to a greater degree than the decline in funding rates due to funding rates approaching practical floors on deposits as described above.

Average earning assets were $963,966,000 during the first nine months of 2013, an increase of $10,662,000 from the average for the first nine months of 2012. Average interest bearing liabilities were $800,886,000 in the first nine months of 2013, a decrease of $5,726,000 from the same nine months in 2012.

Provision for Loan Losses

The provision for loan losses was $1,300,000 in the first nine months of 2013 compared to $3,375,000 in the first nine months of 2012, a decrease of $2,075,000 or 61.5%. The decrease was a result of analysis of the adequacy of the allowance for loan losses. More specifically, even though impaired loans and substandard loans increased from September 30, 2012, provision expense decreased due to the scaling back of the unallocated portion of the allowance in proportion to substandard loans in accordance with management s belief that adequate collateralization exists for substandard loans in accordance with GAAP. Each quarter, the Corporation measures risk in the loan portfolio compared with the balance in the allowance for loan losses and the current evaluation factors. For more information, please refer to *Allowance for Loan Losses* in the following Financial Condition section of this Management s Discussion and Analysis of Financial Condition and Results of Operations. ACNB charges confirmed loan losses to the allowance and credits the allowance for recoveries of previous loan charge-offs. For the first nine months of 2013, the Corporation had net charge-offs of $1,328,000, as compared to net charge-offs of $2,864,000 for the first nine months of 2012.

Other Income

Total other income was $8,932,000 for the nine months ended September 30, 2013, up $79,000, or less than 1.0%, from the first nine months of 2012. Fees from deposit accounts decreased by $121,000, or 6.7%, due to varying volume. Various specific government regulations effectively limit fee assessments related to deposit accounts, making future revenue levels uncertain. Revenue from ATM and debit card transactions increased 10.1% to $1,051,000 due to higher volume. The current increase resulted from consumer desire to use more electronic delivery channels; however, regulations or legal challenges for large financial institutions may impact industry pricing for such transactions and fees in connection therewith in future periods, the effect of which cannot be currently quantified. Income from fiduciary activities, which include both institutional and personal trust and investment management services, totaled $976,000 for the nine months ended September 30, 2013, as compared to $932,000 during the first nine months of 2012, a 4.7% increase as a result of higher average asset market values under management offsetting lower estate fee income in 2013. Estate fee income is inherently sporadic in nature. Earnings on bank-owned life insurance increased by $6,000, or less than 1.0%, as a result of lower crediting rates being offset by more insurance in force. In addition, a gain on life insurance proceeds was recognized in the third quarter of 2012, and no such gain was recognized in the third quarter 2013. At the Corporation s wholly-owned insurance subsidiary, Russell Insurance Group, Inc. (RIG), revenue was down by $24,000, or less than 1.0%, to $3,609,000, with improved recurring revenue mostly offsetting lower contingent commissions. The contingent or extra commission payments from insurance carriers are mostly received in March and April of each year, and the amount is at the discretion of the insurance carriers in accordance with applicable insurance regulations. Pressure on RIG net income will continue in this business line as a large commercial account was recently lost that will lower future commissions, insurance companies are actively lowering commissions to agencies, and contingent commissions are not predictable. Other income in the nine months ended September 30, 2013, was up by $148,000, or 20.4%, to $873,000 due to increased fees related to sales of residential mortgages in the first half of 2013; however, with increases in market rates slowing refinance activity, this revenue source decreased in the third quarter of 2013.

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Other Expenses

The largest component of other expenses is salaries and employee benefits, which increased by $386,000, or 2.8%, when comparing the first nine months of 2013 to the same period a year ago. Overall, the net increase in salaries and employee benefits was the result of:

- increases from normal promotion and production-based incentive/bonus compensation to employees;
- increased payroll taxes including higher unemployment tax assessments; and,
- health insurance, covering a substantial portion of employees, although stable is projected to increase;
- increased costs associated with benefit plans other than the qualified pension plan; partially offset by,
- decreased defined benefit pension expense, which was down by $46,000, or 13.2%, when comparing the nine months ended September 30, 2013, to September 30, 2012, resulting from higher 2012 investment performance offsetting a significant decrease in the discount rate from market rates at historically low levels.

The Corporation s overall pension plan investment strategy is to achieve a mix of investments to meet the long-term rate of return assumption and near-term pension obligations with a diversification of asset types, fund strategies, and fund managers. The mix of investments is adjusted periodically by retaining an advisory firm to recommend appropriate allocations after reviewing the Corporation s risk tolerance on contribution levels, funded status, plan expense, as well as any applicable regulatory requirements. However, the determination of future benefit expense is also dependent on the fair value of assets and the discount rate on the year-end measurement date, which in recent years has experienced low discount rates and fair value volatility. The Corporation amended the defined benefit pension plan effective April 1, 2012, in that no employee hired after March 31, 2012, shall be eligible to participate in the plan and no inactive or former plan participant shall be eligible to again participate in the plan. In addition, a pension provision in a public law known as MAP-21, enacted in July 2012, had no effect on reducing the GAAP expense associated with the plan. The ACNB plan has maintained a well-funded status.

Net occupancy expense decreased by $6,000, or less than 1.0%, in part due to lower summer cooling costs offsetting higher winter season expenses in first quarter 2013. Equipment expense increased by $322,000, or 17.4%, as a result of the costs of converting to a new processing vendor and increased small item technology upgrades in 2013.

Professional services expense totaled $667,000 for the first nine months of 2013, as compared to $628,000 for the same period in 2012, an increase of $39,000 or 6.2%. The increase was due to higher expenses related to corporate governance, risk and compliance management engagements, and legal counsel matters for loans.

Marketing and corporate relations expenses were up $36,000, or 14.0%, in the first nine months of 2013, as compared to the same period of 2012. Marketing expense varies with the timing and amount of advertising production and media expenditures, typically to promote certain in-market consumer loans. In addition, production costs began in 2013 for the redesign of the web site for the banking subsidiary.

FDIC and regulatory expense for the first nine months of 2013 was $592,000, a decrease of $48,000, or 7.5%, from the same period in 2012.

Foreclosed assets held for resale consist of the fair value of real estate acquired through foreclosure on real estate loan collateral or the acceptance of ownership of real estate in lieu of the foreclosure process. Fair values are based on appraisals that consider the sales prices of similar properties in the proximate vicinity less estimated selling costs. Foreclosed real estate expenses were $410,000 and $346,000 for the nine months ended September 30, 2013 and 2012, respectively. The higher cost in 2013 was due to a third quarter unanticipated final loss of $310,000 taken on a property that, during a building inspection, was discovered to have extensive hidden damage. Selling to a buyer in as-is condition was deemed to be in the best interest of ACNB. Otherwise, costs vary due to the number and varying mix of commercial and residential real estate properties, unpaid property taxes, and deferred maintenance required upon acquisition. In addition, some properties suffer decreases in value after acquisition, requiring write-downs to fair value during the prolonged marketing cycles for these distressed properties. Besides the unanticipated loss in the third quarter of 2013, there was a second quarter net recovery of $241,000 from the benefit of an unrelated sale and expense recovery. Large gains and losses on foreclosed assets are not always predictable. Foreclosed assets held for resale expenses or recoveries will vary in the remainder of 2013, depending on the successful closing of sales agreements on some existing properties and the unknown expenses related to new properties acquired and deterioration of existing properties.

Other tax expenses increased by $55,000, or 9.0%, due to a state shareholders equity-based tax that increases annually regardless of income and differing results from recoveries in sales tax challenges. Supplies and postage declined by 5.3% in part due to more electronic information delivery. Other operating expenses increased by $124,000, or 5.3%, in the first nine months of 2013, as compared to the first nine months of 2012. The increases were centered in technology and corporate governance expenditures.

Provision for Income Taxes

The Corporation recognized income taxes of $1,921,000, or 21.4% of pretax income, during the first nine months of 2013, as compared to $1,687,000, or 20.2% of pretax income, during the same period in 2012. The variances from the federal statutory rate of 34% in both periods are generally due to tax-exempt income (from investments in and loans to state and local units of government at below-market rates, an indirect form of taxation) and investments in low-income housing partnerships (which qualify for federal tax credits). The income tax provision during the nine months ended September 30, 2013 and 2012, included low-income housing tax credits of $509,000 and $417,000, respectively.

FINANCIAL CONDITION

Assets totaled $1,035,000,000 at September 30, 2013, compared to $1,050,000,000 at December 31, 2012, and $1,063,000,000 at September 30, 2012. Average earning assets during the nine months ended September 30, 2013, increased to $964,000,000 from $953,000,000 during the same period in 2012. Average interest bearing liabilities decreased in 2013 to $801,000,000 from $807,000,000 in 2012, while average non-interest bearing deposits increased by $16,000,000.

Investment Securities

ACNB uses investment securities to generate interest and dividend income, manage interest rate risk, provide collateral for certain funding products, and provide liquidity. The increase in the securities portfolio in 2013 was mainly to deploy available funds into a more suitable allocation than Federal Reserve balances. Investing into investment security portfolio assets was made more challenging due to the Federal Reserve Bank s program called Quantitative Easing in which, by its open market purchases, the yields are maintained at a lower level than would otherwise be the case. The investment portfolio is comprised of U.S. Government agency, municipal, and corporate securities. These securities provide the appropriate characteristics with respect to credit quality, yield and maturity relative to the management of the overall balance sheet.

At September 30, 2013, the securities balance included a net unrealized gain of $3,019,000, net of taxes, on available for sale securities on $130,592,000 amortized cost versus a net unrealized gain of $5,614,000, net of taxes, on $157,288,000 amortized cost at December 31, 2012, and a net unrealized gain of $6,377,000, net of taxes, on $198,102,000 amortized cost at September 30, 2012. The decrease in fair value of securities during 2013 was the result of a lower amount of investments in the available for sale portfolio and changes in the U.S. Treasury yield curve and the spread from this yield curve required by investors on the types of investment securities that ACNB owns. More specifically, an increase in market rates after comments by Federal Reserve Chairman Bernanke in late second quarter caused a sharp spike in market rates which in turn lowered the value of most securities already owned at September 30, 2013. Previously, actions by the Federal Reserve to lower rates on the yield curve most conducive to stimulating the housing market and separate concerns about European sovereign debt offset the bond markets concern about the level of U.S. debt and inflation, leading to generally lower rates in the yield curve despite fair values being volatile on any given day in all periods presented.

At September 30, 2013, the securities balance included held to maturity securities with an amortized cost of $96,255,000 and a fair value of $94,667,000, compared to an amortized cost of $50,159,000 and a fair value of $50,980,000 at December 31, 2012, and an amortized cost of $48,016,000 and a fair value of $48,971,000 at September 30, 2012. The held to maturity securities are U.S. government agency debentures and pass through mortgage-backed securities in which the full payment of principal and interest is guaranteed; however, because of prevailing low interest rates at purchase, these securities are projected not to be practicable to sale for liquidity needs in future periods. These securities are generally used as required collateral for certain eligible government accounts or repurchase agreements. They are also held for possible pledging to access liquidity for banking subsidiary needs in the form of Federal Home Loan Bank borrowings.

The Corporation does not own investments consisting of pools of Alt-A or subprime mortgages, private label mortgage-backed securities, or trust preferred investments.

The fair values of securities available for sale (carried at fair value) are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or by matrix pricing (Level 2) which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific security but rather by relying on the security s relationship to other benchmark quoted prices. The Corporation uses independent service providers to provide matrix pricing. Please refer to Note 7 - *Securities* in the Notes to Consolidated Financial Statements for more information on the security portfolio and Note 9 - *Fair Value Measurements* in the Notes to Consolidated Financial Statements for more information about fair value.

Loans

Loans outstanding increased by $15,973,000, or 2.3%, from September 30, 2012, to September 30, 2013, and increased by $9,912,000, or 1.4%, from December 31, 2012, to September 30, 2013. The year-over-year increase in loan volume was the result of determined efforts to lend to creditworthy borrowers subject to the Corporation s disciplined standards, despite the continued uncertain economic conditions. The smaller increase in the first nine months of 2013 was caused by a number of large commercial loans paying off by refinancing elsewhere for better rates or more lenient terms. More payoffs are anticipated in the remainder of 2013 from the customers cash reserves or from refinancing at competing banks. During the first nine months of 2013, commercial purpose loans decreased, while local market portfolio residential mortgages increased despite customer preference for a 30-year fixed product, of which the majority is sold because of inherent interest rate risk. Commercial purpose segments decreased $4,318,000, or 1.4%, as compared to December 31, 2012. These loans are spread among diverse categories that include commercial real estate, commercial real estate construction, and commercial and industrial. Residential real estate mortgage lending, which includes smaller commercial purpose loans secured by the owner s home, increased by $14,552,000, or 4.4%, as compared to December 31, 2012. These loans are to local borrowers who preferred loan types that would not be sold into the secondary mortgage market. Of the $396,850,000 total, $83,800,000 were residential mortgage loans secured by junior liens or home equity loans, which are also in many cases junior liens. Junior liens inherently have more credit risk by virtue of the fact that another financial institution may have a senior security position in the case of foreclosure liquidation of collateral to extinguish the debt. Generally, foreclosure actions could become more prevalent if the real estate market weakens further and property values further deteriorate. Real estate construction loans included in commercial purpose segments declined in all periods, as a result of the weak demand in the residential real estate market and because of stricter underwriting on this loan type due to the category s credit attributes.

Most of the Corporation s lending activities are with customers located within southcentral Pennsylvania and in the northern Maryland area that is contiguous to its Pennsylvania retail banking offices. This region currently and historically has lower unemployment than the U.S. as a whole. Included in commercial real estate loans are loans made to lessors of non-residential dwellings that total $105,664,000, or 26.7% of total loans, at September 30, 2013. These borrowers are geographically dispersed throughout ACNB s marketplace and are leasing commercial properties to a varied group of tenants including medical offices, retail space, and other commercial purpose facilities. Because of the varied nature of the tenants, in aggregate, management believes that these loans do not present any greater risk than commercial loans in general. ACNB does not originate or hold Alt-A or subprime mortgages in its loan portfolio.

Allowance for Loan Losses

ACNB maintains the allowance for loan losses at a level believed adequate by management to absorb potential losses in the loan portfolio, and it is funded through a provision for loan losses charged to earnings. On a quarterly basis, ACNB utilizes a defined methodology in determining the adequacy of the allowance for loan losses, which considers specific credit reviews, past loan losses, historical experience, and qualitative factors. This methodology results in an allowance that is considered appropriate in light of the high degree of judgment required and that is

prudent and conservative, but not excessive.

Management assigns internal risk ratings for each commercial lending relationship. Utilizing historical loss experience, adjusted for changes in trends, conditions and other relevant factors, management derives estimated losses for non-rated and non-classified loans. When management identifies impaired loans with uncertain collectability of principal and interest, it evaluates a specific reserve on a quarterly basis in order to estimate potential losses. Management s analysis considers:

- adverse situations that may affect the borrower s ability to repay;

- the current estimated fair value of underlying collateral; and,

- prevailing market conditions.

If management determines a loan is not impaired, a specific reserve allocation is not required. Management then places the loan in a pool of loans with similar risk factors and assigns the general loss factor to determine the reserve. For homogeneous loan types, such as consumer and residential mortgage loans, management bases specific allocations on the average loss ratio for the previous twelve quarters for each specific loan pool. Additionally, management adjusts projected loss ratios for other factors, including the following:

- lending policies and procedures, including underwriting standards and collection, charge-off and recovery practices;

- national, regional and local economic and business conditions, as well as the condition of various market segments, including the impact on the value of underlying collateral for collateral dependent loans;

- the nature and volume of the portfolio and terms of loans;

- the experience, ability and depth of lending management and staff;

- the volume and severity of past due, classified and nonaccrual loans, as well as other loan modifications; and,

- the existence and effect of any concentrations of credit and changes in the level of such concentrations.

Management determines the unallocated portion of the allowance for loan losses, which represents the difference between the reported allowance for loan losses and the calculated allowance for loan losses, based on the following criteria:

- the risk of imprecision in the specific and general reserve allocations;

- the perceived level of consumer and small business loans with demonstrated weaknesses for which it is not practicable to develop specific allocations;

- other potential exposure in the loan portfolio;

- variances in management s assessment of national, regional and local economic conditions; and,

- other internal or external factors that management believes appropriate at that time.

The unallocated portion of the allowance is deemed to be appropriate as it reflects an uncertainty that remains in the loan portfolio, as well as a Corporation specific and industry-wide hesitancy to prematurely release reserves at this time given that additional losses are probable. The Corporation has determined that the amount of provision in 2013 and the resulting allowance at September 30, 2013, are appropriate given the continuing level of risk in the loan portfolio.

Management believes the above methodology accurately reflects losses inherent in the portfolio. Management charges actual loan losses to the allowance for loan losses. Management periodically updates the methodology and the assumptions discussed above.

Management bases the provision for loan losses on the overall analysis taking into account the methodology discussed above. The provision for the quarter ended September 30, 2013, was $975,000 less than the provision for the quarter ended September 30, 2012. More specifically, even though substandard loans increased, provision expense decreased because the increase in substandard loans was largely in credits that were, in the opinion of management, adequately collateralized. Management believes that the decrease in the provision reflects that potential losses inherent in the portfolio were reflected in previous period provision expense and included in the unallocated portion of allowance, as well as, is consistent with recent improving credit quality in the loan portfolio.

Federal and state regulatory agencies, as an integral part of their examination process, periodically review the Corporation s allowance for loan losses and may require the Corporation to recognize additions to the allowance based on their judgments about information available to them at the time of their examination, which may not be currently available to management.

Based on management s comprehensive analysis of the loan portfolio and economic conditions, management believes the current level of the allowance for loan losses is adequate.

The allowance for loan losses at September 30, 2013, was $16,797,000, or 2.34% of loans, as compared to $15,993,000, or 2.28% of loans, at September 30, 2012, and $16,825,000, or 2.38% of loans, at December 31, 2012.

Changes in the allowance for loan losses were as follows:

In thousands	Nine Months Ended September 30, 2013	Year Ended December 31, 2012	Nine Months Ended September 30, 2012
Beginning balance - January 1	**$ 16,825**	$ 15,482	$ 15,482
Provisions charged to operations	**1,300**	4,675	3,375
Recoveries on charged-off loans	**232**	425	416
Loans charged-off	**(1,560)**	(3,757)	(3,280)
Ending balance	**$ 16,797**	$ 16,825	$ 15,993

Loans past due 90 days and still accruing were $1,696,000 and nonaccrual loans were $7,765,000 as of September 30, 2013. $1,520,000 of the nonaccrual balance at September 30, 2013, were troubled debt restructured loans. $7,278,000 of the impaired loans were accruing troubled debt restructured loans. Loans past due 90 days and still accruing were $1,166,000 at September 30, 2012, while nonaccruals were $7,304,000. $1,952,000 of the nonaccrual balance at September 30, 2012, were troubled debt restructured loans. $4,846,000 of the impaired loans were accruing troubled debt restructured loans. Loans past due 90 days and still accruing were $771,000 at December 31, 2012, while nonaccruals were $6,327,000. $1,900,000 of the nonaccrual balance at December 31, 2012, were troubled debt restructured loans. $4,815,000 of the impaired loans were accruing troubled debt restructured loans. Total additional loans classified as substandard (potential problem loans) at September 30, 2013, September 30, 2012, and December 31, 2012, were approximately $10,767,000, $17,389,000 and $13,076,000, respectively.

A better understanding of the trends of the nonaccrual loans is obtained by a comparison back to previous periods. Information on nonaccrual loans at September 30, 2013, as compared to December 31, 2012 and 2011, is as follows:

Dollars in thousands	Number of Credit Relationships	Balance	Specific Loss Allocations	Current Year Charge-Offs	Location	Originated
September 30, 2013						
Residential real estate developments	**3**	**$ 1,188**	**$ 177**	**$ 37**	**In market**	**2006 - 2010**
Owner occupied commercial real estate	**14**	**4,349**		**109**	**In market**	**1995 - 2012**
Investment/rental commercial real estate	**6**	**2,049**	**682**	**101**	**In market**	**2003 - 2011**
Commercial and industrial	**1**	**179**		**22**	**In market**	**2006 - 2007**
Total	**24**	**$ 7,765**	**$ 859**	**$ 269**		
December 31, 2012						
Residential real estate developments	2	$ 854	$	$ 389	In market	2006 - 2010
Owner occupied commercial real estate	12	3,137	7	83	In market	1995 - 2010
Investment/rental commercial real estate	6	1,995		606	In market	2003 - 2011
Commercial and industrial	3	341	29	1,954	In market	2006 - 2010
Total	23	$ 6,327	$ 36	$ 3,032		
December 31, 2011						
Residential real estate developments	3	$ 2,614	$	$ 1,155	In market	2006 - 2010
Owner occupied commercial real estate	13	6,469	43	1,196	In market	1995 - 2010
Investment/rental commercial real estate	5	1,544	53	286	In market	2003 - 2010
Commercial and industrial	3	2,219	1,085	1,664	In market	2006 - 2008
Total	24	$ 12,846	$ 1,181	$ 4,301		

All nonaccrual impaired loans are to borrowers located within the market area served by the Corporation in southcentral Pennsylvania and nearby areas of northern Maryland. All nonaccrual impaired loans were originated by ACNB s banking subsidiary, except for one participation loan discussed below, between 1995 and 2012 for purposes listed in the classifications in the table above.

Included in residential real estate developments at September 30, 2013, the Corporation had one impaired loan totaling $694,000 to finance a residential real estate development project in the Corporation s primary trading area of southcentral Pennsylvania, which is in nonaccrual of interest status. The loan has standard terms and conditions, including repayment from the sales of the respective properties, and no interest reserves, and was originated during the first half of 2006. Foreclosure has been held in abeyance, while allowing the pursuit of a workout plan including providing additional collateral and more targeted marketing of the property. This loan was charged down by $274,000 in the first quarter of 2011 due to a decline in fair value, and subsequently additional paydowns were made by the borrower from sales of collateral in 2011. Because of the 2011 write-down and subsequent principal repayments, there was no specific valuation allowance at September 30, 2013. One smaller residential real estate development relationship, added in 2010, was reduced by collateral sales to $94,000, which is supported by the remaining collateral s current fair value. Another smaller residential real estate development relationship, added in 2013 after the borrower filed Chapter 13 bankruptcy, is not fully supported by the collateral s current fair value because of a dispute on a prior lien. This relationship totaled $400,000 and resulted in a specific allocation of $177,000 based on new appraisals received in the second quarter of 2013 and $37,000 in a charge-off on a confirmed loss in the third quarter of 2013. Legal action has commenced on resolving the issues on this credit.

Owner occupied commercial real estate at September 30, 2013, includes 14 unrelated loan relationships totaling $4,349,000, for which the real estate is collateral and is used in connection with a business enterprise that is suffering economic stress or is out of business. Of these 14 loan relationships, 13 have balances of less than $700,000 each, of which four relationships were added in 2013. The loans in this category are business loans impacted by the general economic downturn. Collection efforts will continue until it is deemed in the best interest to initiate foreclosure procedures. The larger relationship was added to nonaccrual in the second quarter of 2013 after the loan matured with no response from the borrowers, for which there is an outstanding balance of $925,000 on farm land that appears to be adequately secured by real estate collateral awaiting new appraisals. One prior loan in this category with a balance of $237,000 was moved to foreclosed assets held for sale after a charge-off of $109,000 in the second quarter of 2013. Another prior loan in the amount of $154,000 was paid off without loss in 2013.

Investment/rental commercial real estate at September 30, 2013, includes six unrelated loan relationships totaling $2,049,000, for which the real estate is collateral and the purpose of which is for speculation, rental, or other non-owner occupied use. The loans in this category were each affected by the lack of borrower cash flow to continue to service the debt and, in some cases, by increased real estate taxes levied by local government units. The plan is to enter foreclosure proceedings and subsequently market the real estate if ongoing workout efforts are not successful. One loan with a balance of $853,000 added in the first quarter of 2013 had a specific allocation of $219,000 based on a current appraisal less estimated costs to sell.

Included in impaired commercial and industrial loans at September 30, 2013, is a fully-disbursed line of credit, originated in the second quarter of 2007 for a start-up enterprise in the food industry in southcentral Pennsylvania, in the amount of $179,000, with no specific valuation allowance at September 30, 2013, which is net of a $1,000,000 charge-off taken in 2008 and an additional charge-off of $529,000 in 2011. Subsequently, in the third quarter of 2011, the borrower entered into an addendum to a prior delinquent forbearance agreement with all required principal forbearance payments made by the borrower. This loan, with standard terms and conditions including repayment from conversion of trade assets, continues in default and in nonaccrual status.

The Corporation utilizes a systematic review of its loan portfolio on a quarterly basis in order to determine the adequacy of the allowance for loan losses. In addition, ACNB engages the services of an outside loan review function and sets the timing and coverage of loan reviews during the year. The results of this independent loan review are included in the systematic review of the loan portfolio. The allowance for loan losses consists of a component for individual loan impairment, primarily based on the loan s collateral fair value and expected cash flow. A watch list of loans is identified for evaluation based on internal and external loan grading and reviews. Loans other than those determined to be impaired are grouped into pools of loans with similar credit risk characteristics. These loans are evaluated as groups with allocations made to the allowance based on historical loss experience adjusted for current trends in delinquencies, trends in underwriting and oversight, concentrations of credit, and general economic conditions within the Corporation s trading area. The provision expense was based on the loans discussed above, as well as current trends in the watch list and the local economy as a whole. The charge-offs discussed elsewhere in this Management s Discussion and Analysis create the recent loss history experience and result in the qualitative adjustment which, in turn, affects the calculation of losses inherent in the portfolio. The provision for loan losses for 2013 and 2012 was a result of the measurement of the adequacy of the allowance for loan losses at each period.

Foreclosed Assets Held for Resale

Foreclosed assets held for resale consists of the fair value of real estate acquired through foreclosure on real estate loan collateral or the acceptance of ownership of real estate in lieu of the foreclosure process. Fair values are based on appraisals that consider the sales prices of similar properties in the proximate vicinity less estimated selling costs. The carrying value of real estate acquired through foreclosure totaled $1,608,000 for 11 properties to unrelated borrowers at September 30, 2013, compared to $4,247,000 for 15 properties at December 31, 2012. The decrease in the carrying value was due to 12 unrelated commercial purpose parcels sold, while eight different and unrelated smaller value residential and small commercial real estate parcels were added in 2013. All remaining properties are actively being marketed. The Corporation expects to obtain and market additional foreclosed assets through the remainder of 2013; however, the total amount and timing is currently not certain.

Deposits

ACNB continues to rely on its market area deposits as a primary source of funds for lending activities with total deposits of $819,231,000 as of September 30, 2013. Deposits decreased by $12,120,000, or 1.5%, from September 30, 2012, to September 30, 2013, and decreased by $14,945,000, or 1.8%, from December 31, 2012, to September 30, 2013. Deposits vary between quarters mostly reflecting different levels held by local government and school districts during different times of the year. 2012 had an additional increase due to the deposit of $20,000,000 in bond proceeds from a major customer. The drawdown of these deposits has commenced. In addition, deposits decreased in the first nine months of 2013 in part due to declines in retail certificates of deposits (CDs). CDs written in prior periods at higher interest rates are currently maturing, and some customers are unwilling to accept the current lower rates. ACNB s deposit pricing function employs a disciplined pricing approach based upon alternative funding rates, but also strives to price deposits to be competitive with relevant local competition, including credit unions and larger regional banks. During the recession and subsequent slow recovery, deposit growth mix experienced a shift to transaction accounts as customers put more value in liquidity and FDIC insurance. Products, such as money market accounts and interest-bearing transaction accounts, that had suffered declines in past years, continued with recovered balances; however, a late third quarter 2013 decline could indicate a return to more normal, lower balances. With persistent low market interest rates in a slow economy, ACNB s ability to maintain and add to its deposit base may be further impacted by the reluctance of consumers to accept low rates and by competition willing to pay above market rates to attract market share. Alternatively, if rates rise rapidly and the equity markets improve, funds could leave the Corporation or be priced higher to maintain similar levels.

Borrowings

Short-term borrowings are comprised of securities sold under agreements to repurchase and short-term borrowings from the Federal Home Loan Bank (FHLB). As of September 30, 2013, short-term borrowings were $57,418,000, as compared to $47,303,000 at December 31, 2012, and $52,926,000 at September 30, 2012. Agreements to repurchase accounts are within the commercial customer base and have attributes similar to core deposits. Investment securities are pledged in sufficient amounts to collateralize these agreements. In comparison to year-end 2012, repurchase agreement balances were up due to changes in the cash flow position of ACNB s commercial and local government customer base. There were $1,800,000 in short-term FHLB borrowings at the end of the third quarter of 2013; before that, short-term borrowings were last used in the first quarter of 2012 to even out funding from seasonality in the deposit base. Short-term borrowings will be used again in such circumstances. Long-term borrowings consist primarily of longer-term advances from the FHLB that contribute to a more balanced net repricing position; in addition, they include a loan from a commercial bank to fund the purchase of RIG. Long-term borrowings totaled $47,767,000 at September 30, 2013, versus $59,954,000 at December 31, 2012, and $70,015,000 at September 30, 2012. The Corporation decreased long-term borrowings by paying off maturing FHLB advances from increased core deposits. An additional $10,000,000 in one- to five-year laddered FHLB fixed-rate term advances were taken in October 2013 to reduce net liability sensitivity, to take advantage of perhaps temporarily lowered rates, and to increase liquidity during a period of federal government-related uncertainty. Further borrowings will be used when necessary for a variety of risk management and funding purposes. Please refer to the *Liquidity* discussion for more information on the ability to borrow.

Capital

ACNB s capital management strategies have been developed to provide an appropriate rate of return to stockholders, while maintaining its well-capitalized position. Total stockholders equity was $103,020,000 at September 30, 2013, compared to $101,264,000 at December 31, 2012, and $101,677,000 at September 30, 2012. Stockholders equity increased in the first nine months of 2013 by $1,756,000 due to $3,644,000 in earnings retained in capital offsetting an increase in accumulated other comprehensive loss as a result of depreciation in the fair value of the investment portfolio, which offset an increase in pension plan assets and benefit obligations. Other comprehensive income or loss is mainly caused by fixed-rate investment securities gaining or losing value in different interest rate environments and changes in the net funded position of the defined benefit pension plan.

The primary source of additional capital to ACNB is earnings retention, which represents net income less dividends declared. During the first nine months of 2013, ACNB earned $7,048,000 and paid dividends of $3,404,000 for a dividend payout ratio of 48.3%. During the first nine months of 2012, ACNB earned $6,668,000 and paid dividends of $3,392,000 for a dividend payout ratio of 50.9%.

ACNB Corporation has a Dividend Reinvestment and Stock Purchase Plan that provides registered holders of ACNB Corporation common stock with a convenient way to purchase additional shares of common stock by permitting participants in the plan to automatically reinvest cash dividends on all or a portion of the shares owned and to make quarterly voluntary cash payments under the terms of the plan. Participation in the plan is voluntary, and there are eligibility requirements to participate in the plan. Year-to-date September 30, 2013, 21,293 shares were issued under this plan with proceeds in the amount of $364,000. Year-to-date September 30, 2012, 14,911 shares were issued under this plan with proceeds in the amount of $220,000. Proceeds are used for general corporate purposes.

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

Quantitative measures established by regulation to ensure capital adequacy require ACNB to maintain minimum amounts and ratios of total and Tier 1 capital to average assets. Management believes, as of September 30, 2013, and December 31, 2012, that ACNB s banking subsidiary met all minimum capital adequacy requirements to which it is subject and is categorized as well capitalized . There are no subsequent conditions or events that management believes have changed the banking subsidiary s category.

Regulatory Capital Changes

In July 2013, the federal banking agencies issued final rules to implement the Basel III regulatory capital reforms and changes required by the Dodd-Frank Act. The phase-in period for community banking organizations begins January 1, 2015, while larger institutions (generally those with assets of $250 billion or more) must begin compliance on January 1, 2014. The final rules call for the following capital requirements:

- A minimum ratio of common Tier 1 capital to risk-weighted assets of 4.5%;
- A minimum ratio of Tier 1 capital to risk-weighted assets of 6.0%;
- A minimum ratio of total capital to risk-weighted assets of 8.0%, which is no change from the current rule; and,
- A minimum leverage ratio of 4.0%.

In addition, the final rules establish a common equity Tier 1 capital conservation buffer of 2.5% of risk-weighted assets applicable to all banking organizations. If a banking organization fails to hold capital above the minimum capital ratios and the capital conservation buffer, it will be subject to certain restrictions on capital distributions and discretionary bonus payments. The phase-in period for the capital conservation and countercyclical capital buffers for all banking organizations will begin on January 1, 2016.

Under the proposed rules, accumulated other comprehensive income (AOCI) would have been included in a banking organization s common equity Tier 1 capital. The final rules allow community banks to make a one-time election not to include these additional components of AOCI in regulatory capital and instead use the existing treatment under the general risk-based capital rules that excludes most AOCI components from regulatory capital. The opt-out election must be made in the first call report or FR Y-9 series report that is filed after the financial institution becomes subject to the final rule.

The final rules permanently grandfather non-qualifying capital instruments (such as trust preferred securities and cumulative perpetual preferred stock) issued before May 19, 2010, for inclusion in the Tier 1 capital of banking organizations with total consolidated assets of less than $15 billion as of December 31, 2009, and banking organizations that were mutual holding companies as of May 19, 2010.

The proposed rules would have modified the risk-weight framework applicable to residential mortgage exposures to require banking organizations to divide residential mortgage exposures into two categories in order to determine the applicable risk weight. In response to commenter concerns about the burden of calculating the risk weights and the potential negative effect on credit availability, the final rules do not adopt the proposed risk weights but retain the current risk weights for mortgage exposures under the general risk-based capital rules.

Consistent with the Dodd-Frank Act, the new rules replace the ratings-based approach to securitization exposures, which is based on external credit ratings, with the simplified supervisory formula approach in order to determine the appropriate risk weights for these exposures. Alternatively, banking organizations may use the existing gross-up approach to assign securitization exposures to a risk weight category or choose to assign such exposures a 1,250 percent risk weight.

Under the new rules, mortgage servicing assets and certain deferred tax assets are subject to stricter limitations than those applicable under the current general risk-based capital rule. The new rules also increase the risk weights for past due loans, certain commercial real estate loans, and some equity exposures, and makes selected other changes in risk weights and credit conversion factors.

The Corporation is in the process of assessing the impact of these changes on the regulatory ratios of the Corporation and the banking subsidiary, as well as on the capital, operations, liquidity and earnings of the Corporation and the banking subsidiary.

Risk-Based Capital

The banking subsidiary s capital ratios are as follows:

	September 30, 2013	December 31, 2012	To Be Well Capitalized Under Prompt Corrective Action Regulations
Tier 1 leverage ratio (to average assets)	**8.67%**	8.14%	5.00%
Tier 1 risk-based capital ratio (to risk-weighted assets)	**13.09%**	12.80%	6.00%
Total risk-based capital ratio	**14.36%**	14.07%	10.00%

Liquidity

Effective liquidity management ensures the cash flow requirements of depositors and borrowers, as well as the operating cash needs of ACNB, are met.

ACNB s funds are available from a variety of sources, including assets that are readily convertible such as interest bearing deposits with banks, maturities and repayments from the securities portfolio, scheduled repayments of loans receivable, the core deposit base, and the ability to borrow from the FHLB. At September 30, 2013, ACNB s banking subsidiary had a borrowing capacity of approximately $405,780,000 from the FHLB, of which $357,980,000 was available. Because of various restrictions and requirements on utilizing the available balance, ACNB considers $256,000,000 to be the practicable additional borrowing capacity, which is considered to be sufficient for operational needs. The FHLB system is self-capitalizing, member-owned, and its member banks stock is not publicly traded. ACNB creates its borrowing capacity with the FHLB by granting a security interest in certain loan assets with requisite credit quality. ACNB has reviewed information on the FHLB system and the FHLB of Pittsburgh, and has concluded that they have the capacity and intent to continue to provide both operational and contingency liquidity. The FHLB of Pittsburgh instituted a requirement that a member s investment securities must be moved into a safekeeping account under FHLB control to be considered in the calculation of maximum borrowing capacity. The Corporation currently has securities in safekeeping at the FHLB of Pittsburgh; however, the safekeeping account is under the Corporation s control. As better contingent liquidity is maintained by keeping the securities under the Corporation s control, the Corporation has not moved the securities which, in effect, lowered the Corporation s maximum borrowing capacity. However, there is no practical reduction in borrowing capacity as the securities can be moved into the FHLB-controlled account promptly if they are needed for borrowing purposes.

Another source of liquidity is securities sold under repurchase agreements to customers of ACNB s banking subsidiary totaling approximately $55,618,000 and $47,303,000 at September 30, 2013, and December 31, 2012, respectively. These agreements vary in balance according to the cash flow needs of customers and competing accounts at other financial organizations.

The liquidity of the parent company also represents an important aspect of liquidity management. The parent company s cash outflows consist principally of dividends to stockholders and corporate expenses. The main source of funding for the parent company is the dividends it receives

from its banking subsidiary. Federal and state banking regulations place certain legal restrictions and other practicable safety and soundness restrictions on dividends paid to the parent company from the subsidiary bank.

ACNB manages liquidity by monitoring projected cash inflows and outflows on a daily basis, and believes it has sufficient funding sources to maintain sufficient liquidity under varying degrees of business conditions.

Off-Balance Sheet Arrangements

The Corporation is party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and, to a lesser extent, standby letters of credit. At September 30, 2013, the Corporation had unfunded outstanding commitments to extend credit of approximately $152,000,000 and outstanding standby letters of credit of approximately $4,285,000. Because these commitments generally have fixed expiration dates and many will expire without being drawn upon, the total commitment level does not necessarily represent future cash requirements.

Market Risks

Financial institutions can be exposed to several market risks that may impact the value or future earnings capacity of the organization. These risks involve interest rate risk, foreign currency exchange risk, commodity price risk, and equity market price risk. ACNB s primary market risk is interest rate risk. Interest rate risk is inherent because, as a financial institution, ACNB derives a significant amount of its operating revenue from purchasing funds (customer deposits and wholesale borrowings) at various terms and rates. These funds are then invested into earning assets (primarily loans and investments) at various terms and rates.

RECENT DEVELOPMENTS

JUMPSTART OUR BUSINESS STARTUPS (JOBS) ACT **-** In April 2012, President Obama signed the JOBS Act into law. The JOBS Act is aimed at facilitating capital raising by smaller companies and banks and bank holding companies by implementing the following changes:

- raising the threshold requiring registration under the Securities Exchange Act of 1934 (Exchange Act) for banks and bank holdings companies from 500 to 2,000 holders of record;

- raising the threshold for triggering deregistration under the Exchange Act for banks and bank holding companies from 300 to 1,200 holders of record;

- raising the limit for Regulation A offerings from $5 million to $50 million per year and exempting some Regulation A offerings from state blue sky laws;

- permitting advertising and general solicitation in Rule 506 and Rule 144A offerings;

- allowing private companies to use crowd funding to raise up to $1 million in any 12-month period, subject to certain conditions; and,

- creating a new category of issuer, called an Emerging Growth Company , for companies with less than $1 billion in annual gross revenue, which will benefit from certain changes that reduce the cost and burden of carrying out an equity initial public offering (IPO) and complying with public company reporting obligations for up to five years.

While the JOBS Act is not expected to have any immediate application to the Corporation, and since April 2012 has had no material impact, management will continue to monitor the implementation rules for potential effects which might benefit the Corporation.

DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT (DODD-FRANK) - In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act was signed into law. Dodd-Frank is intended to effect a fundamental restructuring of federal banking regulation. Among other things, Dodd-Frank created a new Financial Stability Oversight Council to identify systemic risks in the financial system and gives federal regulators new authority to take control of and liquidate financial firms. Dodd-Frank additionally created a new independent federal regulator to administer federal consumer protection laws. Dodd-Frank has had and will continue to have a significant impact on ACNB s business operations as its provisions take effect. It is expected that, as various implementing rules and regulations are released, they will increase ACNB s operating and compliance costs and could increase the banking subsidiary s interest expense. Among the provisions that are likely to affect ACNB are the following:

Holding Company Capital Requirements

Dodd-Frank requires the Federal Reserve to apply consolidated capital requirements to bank holding companies that are no less stringent than those currently applied to depository institutions. Under these standards, trust preferred securities are excluded from Tier 1 capital unless such securities were issued prior to May 19, 2010, by a bank holding company with less than $15 billion in assets. Dodd-Frank additionally requires that bank regulators issue countercyclical capital requirements so that the required amount of capital increases in times of economic expansion, consistent with safety and soundness.

Deposit Insurance

Dodd-Frank permanently increases the maximum deposit insurance amount for banks, savings institutions, and credit unions to $250,000 per depositor, and extended unlimited deposit insurance to non-interest bearing transaction accounts through December 31, 2012. Dodd-Frank also broadens the base for FDIC insurance assessments. Assessments are now based on the average consolidated total assets less tangible equity capital of a financial institution. Dodd-Frank requires the FDIC to increase the reserve ratio of the Deposit Insurance Fund from 1.15% to 1.35% of insured deposits by 2020 and eliminates the requirement that the FDIC pay dividends to insured depository institutions when the reserve ratio exceeds certain thresholds. Effective one year from the date of enactment, on July 21, 2011, Dodd-Frank eliminated the federal statutory prohibition against the payment of interest on business checking accounts.

Corporate Governance

Dodd-Frank requires publicly-traded companies to give stockholders a non-binding vote on executive compensation at least every three years, a non-binding vote regarding the frequency of the vote on executive compensation at least every six years, and a non-binding vote on golden parachute payments in connection with approvals of mergers and acquisitions unless previously voted on by the stockholders. The SEC has finalized the rules implementing these requirements which took effect on January 21, 2011. Additionally, Dodd-Frank directs the federal banking regulators to promulgate rules prohibiting excessive compensation paid to executives of depository institutions and their holding companies with assets in excess of $1.0 billion, regardless of whether the company is publicly traded. Dodd-Frank also gave the SEC authority to prohibit broker discretionary voting on elections of directors and executive compensation matters.

Prohibition Against Charter Conversions of Troubled Institutions

Effective one year after enactment, Dodd-Frank prohibits a depository institution from converting from a state to a federal charter, or vice versa, while it is the subject of a cease and desist order or other formal enforcement action or a memorandum of understanding with respect to a significant supervisory matter unless the appropriate federal banking agency gives notice of the conversion to the federal or state authority that issued the enforcement action and that agency does not object within 30 days. The notice must include a plan to address the significant supervisory matter. The converting institution must also file a copy of the conversion application with its current federal regulator, which must notify the resulting federal regulator of any ongoing supervisory or investigative proceedings that are likely to result in an enforcement action and provide access to all supervisory and investigative information relating thereto.

Interstate Branching

Dodd-Frank authorizes national and state banks to establish branches in other states to the same extent as a bank chartered by that state would be permitted. Previously, banks could only establish branches in other states if the host state expressly permitted out-of-state banks to establish branches in that state. Accordingly, banks are able to enter new markets more freely.

Limits on Interstate Acquisitions and Mergers

Dodd-Frank precludes a bank holding company from engaging in an interstate acquisition the acquisition of a bank outside its home state unless the bank holding company is both well capitalized and well managed. Furthermore, a bank may not engage in an interstate merger with another bank headquartered in another state unless the surviving institution will be well capitalized and well managed. The previous standard in both cases was adequately capitalized and adequately managed.

Limits on Interchange Fees

Dodd-Frank amends the Electronic Fund Transfer Act to, among other things, give the Federal Reserve the authority to establish rules regarding interchange fees charged for electronic debit transactions by payment card issuers having assets over $10 billion and to enforce a new statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer.

Consumer Financial Protection Bureau

Dodd-Frank creates a new, independent federal agency called the Consumer Financial Protection Bureau (CFPB), which is granted broad rulemaking, supervisory and enforcement powers under various federal consumer financial protection laws, including the Equal Credit Opportunity Act, Truth in Lending Act, Real Estate Settlement Procedures Act, Fair Credit Reporting Act, Fair Debt Collection Act, Consumer Financial Privacy provisions of the Gramm-Leach-Bliley Act, and certain other statutes. The CFPB has examination and primary enforcement authority with respect to depository institutions with $10 billion or more in assets. Smaller institutions are subject to rules promulgated by the CFPB, but continue to be examined and supervised by federal banking regulators for consumer compliance purposes. The CFPB has authority to prevent unfair, deceptive or abusive practices in connection with the offering of consumer financial products. Dodd-Frank authorizes the CFPB to establish certain minimum standards for the origination of residential mortgages including a determination of the borrower s ability to repay. In addition, Dodd-Frank allows borrowers to raise certain defenses to foreclosure if they receive any loan other than a qualified mortgage as defined by the CFPB. Dodd-Frank permits states to adopt consumer protection laws and standards that are more stringent than those adopted at the federal level and, in certain circumstances, permits state attorneys general to enforce compliance with both the state and federal laws and regulations.

ABILITY-TO-REPAY AND QUALIFIED MORTGAGE RULE Pursuant to Dodd-Frank as highlighted above, the CFPB issued a final rule on January 10, 2013 (effective on January 10, 2014), amending Regulation Z as implemented by the Truth in Lending Act, requiring mortgage lenders to make a reasonable and good faith determination based on verified and documented information that a consumer applying for a mortgage loan has a reasonable ability to repay the loan according to its terms. Mortgage lenders are required to determine the consumer s ability to repay in one of two ways. The first alternative requires the mortgage lender to consider the following eight underwriting factors when making the credit decision: (1) current or reasonably expected income or assets; (2) current employment status; (3) the monthly payment on the covered transaction; (4) the monthly payment on any simultaneous loan; (5) the monthly payment for mortgage-related obligations; (6) current debt obligations, alimony, and child support; (7) the monthly debt-to-income ratio or residual income; and, (8) credit history. Alternatively, the mortgage lender can originate qualified mortgages , which are entitled to a presumption that the creditor making the loan satisfied the ability-to-repay requirements. In general, a qualified mortgage is a mortgage loan without negative amortization, interest-only payments, balloon payments, or terms exceeding 30 years. In addition, to be a qualified mortgage, the points and fees paid by a consumer cannot exceed 3% of the total loan amount. Loans which meet these criteria will be considered qualified mortgages, and as a result generally protect lenders from fines or litigation in the event of foreclosure. Qualified mortgages that are higher-priced (e.g. subprime loans) garner a rebuttable presumption of compliance with the ability-to-repay rules, while qualified mortgages that are not higher-priced (e.g. prime loans) are given a safe harbor of compliance. The impact of the final rule, and the subsequent amendments thereto, on the Corporation s lending activities and the Corporation s statements of income or condition are uncertain at this time.

SUPERVISION AND REGULATION

Dividends

ACNB is a legal entity separate and distinct from its subsidiary bank. ACNB s revenues, on a parent company only basis, result primarily from dividends paid to the Corporation by its subsidiary bank. Federal and state laws regulate the payment of dividends by ACNB s subsidiary bank. For further information, please refer to *Regulation of Bank* below.

Regulation of Bank

The operations of the subsidiary bank are subject to statutes applicable to banks chartered under the banking laws of Pennsylvania, to state nonmember banks, and to banks whose deposits are insured by the FDIC. The subsidiary bank s operations are also subject to regulations of the Pennsylvania Department of Banking and Securities, Federal Reserve, and FDIC.

The Pennsylvania Department of Banking and Securities, which has primary supervisory authority over banks chartered in Pennsylvania, regularly examines banks in such areas as reserves, loans, investments, management practices, and other aspects of operations. These examinations are designed for the protection of the subsidiary bank s depositors rather than ACNB s stockholders. The subsidiary bank must file quarterly and annual reports to the Federal Financial Institutions Examination Council, or FFIEC.

Monetary and Fiscal Policy

ACNB and its subsidiary bank are affected by the monetary and fiscal policies of government agencies, including the Federal Reserve and FDIC. Through open market securities transactions and changes in its discount rate and reserve requirements, the Board of Governors of the Federal Reserve exerts considerable influence over the cost and availability of funds for lending and investment. The nature of monetary and fiscal policies on future business and earnings of ACNB cannot be predicted at this time. From time to time, various federal and state legislation is proposed that could result in additional regulation of, and restrictions on, the business of ACNB and the subsidiary bank, or otherwise change the business environment. Management cannot predict whether any of this legislation will have a material effect on the business of ACNB.

ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Management monitors and evaluates changes in market conditions on a regular basis. Based upon the most recent review, management has determined that there have been no material changes in market risks since year-end 2012. For further discussion of year-end information, please refer to the Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

ITEM 4 - CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

As of the end of the period covered by this report, the Corporation carried out an evaluation, under the supervision and with the participation of its management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of its disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Corporation s disclosure controls and procedures are effective in timely alerting them to material information relating to the Corporation (including its consolidated subsidiaries) required to be included in periodic SEC filings.

Disclosure controls and procedures are Corporation controls and other procedures that are designed to ensure that information required to be disclosed by the Corporation in the reports that it files or submits under the Securities Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms.

There were no changes in the Corporation s internal control over financial reporting during the quarterly period ended September 30, 2013, that have materially affected, or are reasonably likely to materially affect, the internal control over financial reporting.

PART II - OTHER INFORMATION

ACNB CORPORATION

ITEM 1 - LEGAL PROCEEDINGS

As of September 30, 2013, there were no material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which ACNB or its subsidiaries are a party or by which any of their property is the subject. In addition, no material proceedings are pending or are known to be threatened or contemplated against the Corporation or its subsidiaries by governmental authorities.

ITEM 1A - RISK FACTORS

Management has reviewed the risk factors that were previously disclosed in the Annual Report on Form 10-K for the fiscal year-ended December 31, 2012. There are no material changes from the risk factors as previously disclosed in the Form 10-K.

ITEM 2 - UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

On November 3, 2008, the Corporation announced a plan to purchase up to 120,000 shares of its outstanding common stock. There were no treasury shares purchased under this plan during the quarter ended September 30, 2013. The maximum number of shares that may yet be purchased under this stock repurchase plan is 57,400.

On May 5, 2009, stockholders approved and ratified the ACNB Corporation 2009 Restricted Stock Plan, effective as of February 24, 2009, in which awards shall not exceed, in the aggregate, 200,000 shares of common stock. As of September 30, 2013, there were no shares of common stock granted as restricted stock awards to either employees or directors. The Corporation s Registration Statement under the Securities Act of 1933 on Form S-8 for the ACNB Corporation 2009 Restricted Stock Plan was filed with the Securities and Exchange Commission on January 4, 2013.

On May 5, 2009, stockholders approved and adopted the amendment to the Articles of Incorporation of ACNB Corporation to authorize up to 20,000,000 shares of preferred stock, par value $2.50 per share. As of September 30, 2013, there were no issued or outstanding shares of preferred stock.

ITEM 3 - DEFAULTS UPON SENIOR SECURITIES - NOTHING TO REPORT.

ITEM 4 - MINE SAFETY DISCLOSURES - NOT APPLICABLE.

ITEM 5 - OTHER INFORMATION - NOTHING TO REPORT.

ITEM 6 - EXHIBITS

The following exhibits are included in this report:

Exhibit 3(i)	Articles of Incorporation of ACNB Corporation, as amended. (Incorporated by reference to Exhibit 3.1 of the Registrant s Current Report on Form 8-K, filed with the Commission on June 2, 2009.)
Exhibit 3(ii)	Bylaws of ACNB Corporation, as amended. (Incorporated by reference to Exhibit 3.2 of the Registrant s Current Report on Form 8-K, filed with the Commission on February 4, 2013.)
Exhibit 10.1	ACNB Corporation, ACNB Acquisition Subsidiary LLC, and Russell Insurance Group, Inc. Stock Purchase Agreement. (Incorporated by reference to Exhibit 10.2 of the Registrant s Annual Report on Form 10-K for the year ended December 31, 2004, filed with the Commission on March 15, 2005.)
Exhibit 10.2	Salary Continuation Agreement Applicable to Ronald L. Hankey. (Incorporated by reference to Exhibit 10.2 of the Registrant s Annual Report on Form 10-K for the year ended December 31, 2008, filed with the Commission on March 13, 2009.)
Exhibit 10.3	Executive Supplemental Life Insurance Plan Applicable to Ronald L. Hankey, Thomas A. Ritter, David W. Cathell and Lynda L. Glass. (Incorporated by reference to Exhibit 10.3 of the Registrant s Quarterly Report on Form 10-Q for the period ended September 30, 2008, filed with the Commission on November 7, 2008.)
Exhibit 10.4	Director Supplemental Life Insurance Plan Applicable to Frank Elsner III, Scott L. Kelley, James J. Lott, Robert W. Miller, Donna M. Newell, J. Emmett Patterson, Daniel W. Potts, Marian B. Schultz, David L. Sites, Alan J. Stock, Harry L. Wheeler and James E. Williams. (Incorporated by reference to Exhibit 10.5 of the Registrant s Annual Report on Form 10-K for the year ended December 31, 2004, filed with the Commission on March 15, 2005.)
Exhibit 10.5	Amended and Restated Director Deferred Fee Plan Applicable to Frank Elsner III, Scott L. Kelley, James J. Lott, Robert W. Miller, Donna M. Newell, J. Emmett Patterson, Marian B. Schultz, David L. Sites, Alan J. Stock, Harry L. Wheeler and James E. Williams. (Incorporated by reference to Exhibit 99.1 of the Registrant s Current Report on Form 8-K, filed with the Commission on January 6, 2012.)
Exhibit 10.6	ACNB Bank Salary Savings Plan. (Incorporated by reference to Exhibit 10.6 of the Registrant s Annual Report on Form 10-K for the year ended December 31, 2009, filed with the Commission on March 12, 2010.)
Exhibit 10.7	Group Pension Plan for Employees of ACNB Bank. (Incorporated by reference to Exhibit 10.7 of the Registrant s Quarterly Report on Form 10-Q for the quarter ended March 31, 2012, filed with the Commission on May 4, 2012.)
Exhibit 10.8	Complete Settlement Agreement and General Release made among ACNB Corporation, Adams County National Bank and John W. Krichten effective June 13, 2006. (Incorporated by reference to Exhibit 99.1 of the Registrant s Current Report on Form 8-K, filed with the Commission on June 15, 2006.)
Exhibit 10.9	Employment Agreement between ACNB Corporation, Adams County National Bank and Thomas A. Ritter dated as of December 31, 2008. (Incorporated by reference to Exhibit 10.9 of the Registrant s Annual Report on Form 10-K for the year ended December 31, 2008, filed with the Commission on March 13, 2009.)
Exhibit 10.10	Employment Agreement between ACNB Corporation, Adams County National Bank and Lynda L. Glass dated as of December 31, 2008. (Incorporated by reference to Exhibit 10.10 of the Registrant s Annual Report on Form 10-K for the year ended December 31, 2008, filed with the Commission on March 13, 2009.)

Exhibit 10.11	Employment Agreement between ACNB Corporation, Russell Insurance Group, Inc. and Frank C. Russell, Jr. dated as of January 13, 2011. (Incorporated by reference to Exhibit 99.1 of the Registrant s Current Report on Form 8-K, filed with the Commission on January 19, 2011.)
Exhibit 10.12	Employment Agreement between ACNB Corporation, Adams County National Bank and David W. Cathell dated as of April 17, 2009. (Incorporated by reference to Exhibit 99.1 of the Registrant s Current Report on Form 8-K, filed with the Commission on April 23, 2009.)
Exhibit 10.13	2009 Restricted Stock Plan. (Incorporated by reference to Appendix C of the Registrant s Proxy Statement on Schedule 14A, filed with the Commission on March 25, 2009.)
Exhibit 10.14	Salary Continuation Agreement by and between ACNB Bank and Thomas A. Ritter dated as of March 28, 2012. (Incorporated by reference to Exhibit 99.1 of the Registrant s Current Report on Form 8-K, filed with the Commission on April 3, 2012.)
Exhibit 10.15	Salary Continuation Agreement by and between ACNB Bank and Lynda L. Glass dated as of March 28, 2012. (Incorporated by reference to Exhibit 99.2 of the Registrant s Current Report on Form 8-K, filed with the Commission on April 3, 2012.)
Exhibit 10.16	Salary Continuation Agreement by and between ACNB Bank and David W. Cathell dated as of March 28, 2012. (Incorporated by reference to Exhibit 99.3 of the Registrant s Current Report on Form 8-K, filed with the Commission on April 3, 2012.)
Exhibit 10.17	Amended and Restated 2001 Salary Continuation Agreement by and between ACNB Bank and Thomas A. Ritter dated as of March 28, 2012. (Incorporated by reference to Exhibit 99.4 of the Registrant s Current Report on Form 8-K, filed with the Commission on April 3, 2012.)
Exhibit 10.18	Amended and Restated 1996 Salary Continuation Agreement by and between ACNB Bank and Lynda L. Glass dated as of March 28, 2012. (Incorporated by reference to Exhibit 99.5 of the Registrant s Current Report on Form 8-K, filed with the Commission on April 3, 2012.)
Exhibit 11	Statement re Computation of Earnings. (Incorporated by reference to page 7 of this Form 10-Q.)
Exhibit 14	Code of Ethics. (Incorporated by reference to Exhibit 14 of the Registrant s Annual Report on Form 10-K for the year ended December 31, 2012, filed with the Commission on March 15, 2013.)
Exhibit 18	Preferability Letter from ParenteBeard LLC dated as of August 3, 2012. (Incorporated by reference to Exhibit 18 of the Registrant s Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, filed with the Commission on August 3, 2012.)
Exhibit 31.1	Chief Executive Officer Certification of Quarterly Report on Form 10-Q.
Exhibit 31.2	Chief Financial Officer Certification of Quarterly Report on Form 10-Q.
Exhibit 32.1	Chief Executive Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
Exhibit 32.2	Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Exhibit 101.LAB	XBRL Taxonomy Extension Label Linkbase.
Exhibit 101.PRE	XBRL Taxonomy Extension Presentation Linkbase.
Exhibit 101.INS	XBRL Instance Document.
Exhibit 101.SCH	XBRL Taxonomy Extension Schema.
Exhibit 101.CAL	XBRL Taxonomy Extension Calculation Linkbase.
Exhibit 101.DEF	XBRL Taxonomy Extension Definition Linkbase.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ACNB CORPORATION (Registrant)

Date: November 1, 2013

/s/ Thomas A. Ritter
Thomas A. Ritter
President & Chief Executive Officer

/s/ David W. Cathell
David W. Cathell
Executive Vice President, Treasurer &
Chief Financial Officer (Principal Financial Officer)