

PATRIOT NATIONAL BANCORP INC
Form 10-K
March 31, 2016
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the Year Ended December 31, 2015

Commission file number 000-29599

PATRIOT NATIONAL BANCORP, INC.

(Exact name of registrant as specified in its charter)

Connecticut 06-1559137
(State of Incorporation) (I.R.S. Employer Identification Number)

900 Bedford Street, Stamford, Connecticut 06901

(Address of principal executive offices)

(203) 324-7500

(Registrant's telephone number, including area code)

Securities registered under Section 12(b) of the Exchange Act: Common Stock, par value \$0.01 per share

Securities registered under Section 12(g) of the Exchange Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes No

Check whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days:

Yes No

Check if disclosure of delinquent filers in response to Item 405 of Regulation S-K is not contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10K or any amendment to this Form 10K

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company in Rule 12b-2 of the Exchange Act:

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act):

Yes No

Aggregate market value of the voting stock held by non-affiliates of the registrant as of June 30, 2015 based on the last sale price as reported on the NASDAQ Global Market:\$7.5 million

Number of shares of the registrant's Common stock, \$0.01 par value per share, 4,067,642 shares outstanding as of February 29, 2016.

Document Incorporated by Reference

Proxy or Information Statement for 2015 Annual Meeting of Shareholders. (A definitive proxy or Information statement will be filed with the Securities and Exchange Commission within 120 days after the close of the Fiscal year covered by this form 10-K.)

Incorporated into part III of this Form 10-K.

PATRIOT NATIONAL BANCORP, INC.

2015 FORM 10-K ANNUAL REPORT

TABLE OF CONTENTS

| | |
|--|----|
| PART I | 2 |
| ITEM 1. Business | 2 |
| ITEM 1A. Risk Factors | 8 |
| ITEM 1B. Unresolved Staff Comments | 15 |
| ITEM 2. Properties | 15 |
| ITEM 3. Legal Proceedings | 15 |
| ITEM 4. Mine Safety Disclosures | 15 |
| PART II | 16 |
| ITEM 5. Market for Registrant’s Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities | 16 |
| ITEM 6. Selected Financial Data | 18 |
| ITEM 7. Management’s Discussion and Analysis of Financial Condition and Results of Operation | 19 |
| ITEM 7A. Quantitative and Qualitative Disclosures about Market Risk | 40 |
| ITEM 8. Financial Statements and Supplementary Data | 42 |
| ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure | 44 |
| ITEM 9A. Controls and Procedures | 44 |
| ITEM 9B. Other Information | 45 |
| PART III | 45 |
| ITEM 10. Directors, Executive Officers and Corporate Governance | 45 |
| ITEM 11. Executive Compensation | 45 |
| ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters | 46 |
| ITEM 13. Certain Relationships and Related Transactions, and Director Independence | 46 |
| ITEM 14. Principal Accountant Fees and Services | 46 |
| Part IV | 47 |
| ITEM 15. Exhibits and Financial Statement Schedules | 47 |

“Safe Harbor” Statement Under Private Securities Litigation Reform Act of 1995

"SAFE HARBOR" STATEMENT UNDER PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

Certain statements contained in the Company’s public statements, including this one, and in particular in “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” may be forward looking and subject to a variety of risks and uncertainties. These factors include, but are not limited to: (1) changes in prevailing interest rates which would affect the interest earned on the Company’s interest earning assets and the interest paid on its interest bearing liabilities; (2) the timing of repricing of the Company’s interest earning assets and interest bearing liabilities; (3) the effect of changes in governmental monetary policy; (4) the effect of changes in regulations applicable to the Company and the Bank and the conduct of its business; (5) changes in competition among financial service companies, including possible further encroachment of non-banks on services traditionally provided by banks; (6) the ability of competitors that are larger than the Company to provide products and services which it is impracticable for the Company to provide; (7) the state of the economy and real estate values in the Company’s market areas, and the consequent effect on the quality of the Company’s loans; (8) recent governmental initiatives that are expected to have a profound effect on the financial services industry and could dramatically change the competitive environment of the Company; (9) other legislative or regulatory changes, including those related to residential mortgages, changes in accounting standards, and Federal Deposit Insurance Corporation (“FDIC”) premiums that may adversely affect the Company; (10) the application of generally accepted accounting principles, consistently applied; (11) the fact that one period of reported results may not be indicative of future periods; (12) the state of the economy in the greater New York metropolitan area and its particular effect on the Company's customers, vendors and communities and other such factors, including risk factors, as may be described in the Company’s other filings with the Securities and Exchange Commission (the “SEC”).

Although the Company believes that it offers competitive loan and deposit products and has the resources needed for continued success, future revenues and interest spreads and yields cannot be reliably predicted. These trends may cause the Company to adjust its operations in the future. Because of the foregoing and other factors, recent trends should not be considered reliable indicators of future financial results or stock prices.

PART I

ITEM 1. Business

General

Patriot National Bancorp, Inc. (“The Company” or “Company”), a Connecticut corporation, is a one-bank holding company for Patriot Bank, N.A, a national banking association headquartered in Stamford, Fairfield County, Connecticut (the “Bank”). The Bank received its charter and commenced operations as a national bank on August 31, 1994. The Bank currently has eight branch offices in Connecticut. The Bank also has branch offices in Bedford and Scarsdale, both located in Westchester County, New York.

On March 11, 2003, The Company formed Patriot National Statutory Trust I (the “Trust”) for the sole purpose of issuing trust preferred securities and investing the proceeds in subordinated debentures issued by the Company. The Company primarily invested the funds from the issuance of the debt in the Bank. The Bank in turn used the proceeds to fund general operations.

On April 1, 2008, the Bank acquired a 20% interest in a de novo insurance agency. The impact on the Bank’s operations in 2011, 2012 and 2013 had been minimal. During the fourth quarter of 2013, the Bank sold its interest in the de novo insurance agency.

On October 15, 2010, pursuant to a Securities Purchase Agreement (the “Securities Purchase Agreement”), the Company issued and sold to PNBK Holdings LLC (“Holdings”), an investment limited liability company controlled by Michael Carrazza, 3.36 million shares of its common stock at a purchase price of \$15.00 per share (adjusted for a 1-for-10 reverse stock split discussed below) for an aggregate purchase price of \$50.4 million. The shares sold to Holdings represented 87.6% of the Company’s then issued and outstanding common stock. The par value of the common stock was changed to \$0.01 per share. Also in connection with that sale, certain directors and officers of both the Company and the Bank resigned and were replaced with nominees of Holdings and Michael Carrazza became Chairman of the Board of the Company.

As of the date hereof, the only business of the Company is its ownership of all of the issued and outstanding capital stock of the Bank and the Trust. Except as specifically noted otherwise herein, the balance of the description of the Company’s business is a description of the Bank’s business.

On February 26, 2013, the Company announced the appointment of Kenneth T. Neilson as President and Chief Executive Officer of both the Company and the Bank effective March 18, 2013. This was following the departure of Christopher Maher, who resigned as President, CEO and director of the Company and the Bank for personal reasons. Mr. Neilson had served as a director of the Company since 2010.

On March 4, 2015, the Company affected a 1-for-10 reverse stock split. All common stock and per share data included in 2014 and 2013 financial statements have been restated to give effect to the reverse stock split.

During 2015, Mr. Michael Carrazza sold 325,000 shares of PNBK Holding LLC, to third party where the third party has sole voting rights and dispositive power for sold shares. Following this transaction it makes Mr. Carrazza's holdings in PNBK Holding LLC to 75.65% at December 31, 2015.

On September 28, 2015, the Bank changed its name from Patriot National Bank to Patriot Bank, N.A., and the strategic approach to the way it provides value to its customers, community, and the market place. The name change came after the Bank has reported eight consecutive quarters of increased earnings.

Business Operations

The Bank conducts business at its main office located in Stamford, Connecticut and at other Connecticut branch offices located in Darien, Fairfield, Greenwich, Milford, Norwalk, Trumbull, and Westport. In New York State, the Bank conducts business at branch offices located in Bedford and Scarsdale. The Bank also operates a loan origination office at 900 Bedford Street, Stamford, Connecticut.

The Bank offers commercial real estate loans, commercial business loans, and a variety of consumer loans with an emphasis on serving the needs of individuals, small and medium-sized businesses and professionals. The Bank previously had offered loans on residential real estate, but discontinued doing so during 2013. The Bank's lending activities are conducted principally in Fairfield and New Haven Counties in Connecticut and Westchester County in New York, although the Bank's loan business is not necessarily limited to these areas.

Consumer and commercial deposit accounts offered include: checking, interest-bearing negotiable order of withdrawal "NOW", money market, time certificates of deposit, savings, Certificate of Deposit Account Registry Service CDARS, Individual Retirement Accounts ("IRAs") and Health Savings Accounts ("HSAs"). Other services offered by the Bank include include Automated Clearing House ("ACH") transfers, lockbox, internet banking, bill paying, remote deposit capture, debit cards, money orders, traveler's checks and automatic teller machines ("ATMs"). In addition, the Bank may in the future offer other financial services.

The Bank's employees perform most routine day-to-day banking transactions. The Bank has entered into a number of arrangements with third parties for banking services such as correspondent banking, check clearing, data processing services, credit card processing and armored car carrier service.

In the normal course of business and subject to applicable government regulations, the Bank invests a portion of its assets in investment securities, which may include government securities. An objective of the Bank's investment policy is to maintain a balance of high quality diversified investments to minimize risk while maintaining adequate levels of liquidity and limiting its exposure to interest rate movements and credit risk. Government agency issues currently comprise the majority of the Bank's investment portfolio.

Employees

As of December 31, 2015, the Company had 95 full-time employees and 6 part-time employees. None of the employees of the Company are covered by a collective bargaining agreement.

Competition

The Bank competes with a variety of financial institutions for loans and deposits in its market area. These include larger financial institutions with greater financial resources, larger branch systems and higher lending limits as well as the ability to conduct larger advertising campaigns to attract business. The larger institutions may also offer additional services such as trust and international banking which the Bank is not equipped to offer directly. When the need arises, arrangements are made with correspondent institutions to provide such services. To attract business in this competitive environment, the Bank relies on local promotional activities, personal contact by officers and directors, customer referrals and on its ability to distinguish itself by offering personalized and responsive banking service.

The customer base of the Bank generally is meant to be diversified so that there is not a concentration of either loans or deposits within a single industry, a group of industries, a single person or groups of people. The Bank is not dependent on one or a few major customers for its lending or deposit activities, the loss of any one of which would have a material adverse effect on the business of the Bank.

The Bank's loan customers extend beyond the towns and cities in which the Bank has branch offices, including nearby towns in Fairfield and New Haven Counties in Connecticut, and Westchester County and the five boroughs of New York City in New York, although the Bank's loan business is not necessarily limited to these areas. While the Bank does not currently hold or intend to attract significant deposit or loan business from major corporations with headquarters in its market area, the Bank believes that small manufacturers, distributors and wholesalers along with service industries, professionals and related businesses which have been attracted to this area, as well as the individuals that reside in this area, represent current and potential customers of the Bank.

In recent years, intense market demands, economic pressures and significant legislative and regulatory actions have eroded banking industry classifications which were once clearly defined and have increased competition among banks, as well as other financial institutions including non-bank competitors. This increase in competition has caused banks and other financial service institutions to diversify their services and become more cost effective. The impact on banks and other financial institutions of market dynamics and legislative and regulatory changes has increased customer awareness of product and service differences among competitors and increased merger activity among banks and other financial institutions.

Supervision and Regulation

As a bank holding company, the Company's operations are subject to regulation, supervision and examination by the Board of Governors of the Federal Reserve Board (the "Federal Reserve Board"). The Federal Reserve Board has established capital adequacy guidelines for bank holding companies that are similar of the Office of the Comptroller of the Currency ("OCC") capital guidelines applicable to the Bank. The Bank Holding Company Act of 1956, as amended (the "BHC Act"), limits the types of companies that a bank holding company may acquire or organize and the activities in which it or they may engage. In general, bank holding companies and their subsidiaries are only permitted to engage in, or acquire direct control of, any company engaged in banking or in a business so closely related to banking as to be a proper incident thereto. Federal legislation enacted in 1999 authorizes certain entities to register as financial holding companies. Registered financial holding companies are permitted to engage in businesses, including securities and investment banking businesses, which are prohibited to bank holding companies. The creation of financial holding companies has had no significant impact on the Company.

Under the BHC Act, the Company is required to file quarterly with the Federal Reserve Board a report of its operations. The Company, the Bank and any other subsidiaries are subject to examination by the Federal Reserve Board. In addition, the Company will be required to obtain the prior approval of the Federal Reserve Board to acquire, with certain exceptions, more than 5% of the outstanding voting stock of any bank or bank holding company, to acquire all or substantially all of the assets of a bank or to merge or consolidate with another bank holding company. Moreover, the Company, the Bank and any other subsidiaries are prohibited from engaging in certain tying arrangements in connection with any extension of credit or provision of any property or services. The Bank is also subject to certain restrictions imposed by the Federal Reserve Act on issuing any extension of credit to the Company or any of its subsidiaries or making any investments in the stock or other securities thereof and on the taking of such stock or securities as collateral for loans to any borrower. If the Company wants to engage in businesses permitted to financial holding companies but not to bank holding companies, it would need to register with the Federal Reserve Board as a financial holding company.

The Federal Reserve Board has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses its view that a bank holding company should pay cash dividends only to the extent that the bank holding company's net income for the past year is sufficient to cover both the cash dividend and a rate of earnings retention that is consistent with the bank holding company's capital needs, asset quality and overall financial condition. The Federal Reserve Board has also indicated that it would be inappropriate for a company experiencing

serious financial problems to borrow funds to pay dividends. Furthermore, under the prompt corrective action regulations adopted by the Federal Reserve Board, the Federal Reserve Board may prohibit a bank holding company from paying any dividends if its bank subsidiary is classified as “undercapitalized.”

A bank holding company is required to give the Federal Reserve Board prior written notice of any purchase or redemption of its outstanding equity securities if the gross consideration for the purchase or redemption, when combined with the net consideration paid for all such purchases or redemptions during the preceding 12 months, is equal to 10% or more of its consolidated retained earnings. The Federal Reserve Board may disapprove such a purchase or redemption if it determines that the proposal would constitute an unsafe or unsound practice or would violate any law, regulation, Federal Reserve Board order, or any condition imposed by, or written agreement with, the Federal Reserve Board.

The Company is subject to capital adequacy rules and guidelines issued by the Federal Reserve Board and the Federal Deposit Insurance Corporation (“*FDIC*”), and the Bank is subject to capital adequacy rules and guidelines issued by the OCC. These substantially identical rules and guidelines require the Company to maintain certain minimum ratios of capital to adjusted total assets and/or risk-weighted assets. Under the provisions of the Federal Deposit Insurance Corporation Improvements Act of 1991, the Federal regulatory agencies are required to implement and enforce these rules in a stringent manner. The Company is also subject to applicable provisions of Connecticut law insofar as they do not conflict with, or are not otherwise preempted by, Federal banking law.

The Company is subject to the reporting requirements of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and, in accordance with the Exchange Act, files periodic reports, proxy statements and other information with the SEC. The Bank’s operations are subject to regulation, supervision and examination by the OCC and the FDIC.

Federal and state banking regulations govern, among other things, the scope of the business of a bank, a bank holding company or a financial holding company, the investments a bank may make, deposit reserves a bank must maintain, the establishment of branches and the activities of a bank with respect to mergers and acquisitions. The Bank is a member of the Federal Reserve System and as such, is subject to applicable provisions of the Federal Reserve Act and regulations there-under. The Bank is subject to the federal regulations promulgated pursuant to the Financial Institutions Supervisory Act to prevent banks from engaging in unsafe and unsound practices, as well as various other federal and state laws and consumer protection laws. The Bank is also subject to the comprehensive provisions of the National Bank Act.

The OCC regulates the number and locations of branch offices of a national bank. The OCC may only permit a national bank to maintain branches in locations and under the conditions imposed by state law upon state banks. At this time, applicable Connecticut banking laws do not impose any material restrictions on the establishment of branches by Connecticut banks throughout Connecticut. New York State law is similar; however, the Bank cannot establish a branch in a town with a population of less than 50,000 if another bank is headquartered in the town.

The earnings and growth of the Company, the Bank and the banking industry are affected by the monetary and fiscal policies of the United States Government and its agencies, particularly the Federal Reserve Board. The Open Market

Committee of the Federal Reserve Board implements national monetary policy to curb inflation and combat recession. The Federal Reserve Board uses its power to adjust interest rates in United States Government securities, the Discount Rate and deposit reserve retention rates. The actions of the Federal Reserve Board influence the growth of bank loans, investments and deposits. They also affect interest rates charged on loans and paid on deposits. The nature and impact of any future changes in monetary policies cannot be predicted.

In addition to other laws and regulations, the Company and the Bank are subject to the Community Reinvestment Act (“CRA”), which requires the federal bank regulatory agencies, when considering certain applications involving the Company or the Bank, to consider the Company’s and the Bank’s record of helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods. The CRA was originally enacted because of concern over unfair treatment of prospective borrowers by banks and over unwarranted geographic differences in lending patterns. Existing banks have sought to comply with CRA in various ways; some banks have made use of more flexible lending criteria for certain types of loans and borrowers (consistent with the requirement to conduct safe and sound operations), while other banks have increased their efforts to make loans to help meet identified credit needs within the consumer community, such as those for home mortgages, home improvements and small business loans. Compliance may also include participation in various government insured lending programs, such as Federal Housing Administration insured or Veterans Administration guaranteed mortgage loans, Small Business Administration loans, and participation in other types of lending programs such as high loan-to-value ratio conventional mortgage loans with private mortgage insurance. To date, the market area from which the Bank draws much of its business is in the towns and cities in which the Bank has branch offices, which are characterized by a very diverse ethnic, economic and racial cross-section of the population. As the Bank expands further, the market areas served by the Bank will continue to evolve. The Company and the Bank have not and will not adopt any policies or practices, which discourage credit applications from, or unlawfully discriminate against, individuals or segments of the communities served by the Bank.

On October 26, 2001, the United and Strengthening America by Providing Tools Required to Intercept and Obstruct Terrorism Act of 2001, or the *USA Patriot Act*, was enacted to further strengthen domestic security following the September 11, 2001 attacks. This Act amended various federal banking laws, particularly the Bank Secrecy Act, with the intent to curtail money laundering and other activities that might be undertaken to finance terrorist actions. The Act also requires that financial institutions in the United States enhance already established anti-money laundering policies, procedures and audit functions and ensure that controls are reasonably designed to detect instances of money laundering through certain correspondent or private banking accounts. Verification of customer identification, maintenance of said verification records and cross checking names of new customers against government lists of known or suspected terrorists is also required. The Patriot Act was reauthorized and modified with the enactment of The USA Patriot Act Improvement and Reauthorization Act of 2005.

On July 20, 2002, the Sarbanes-Oxley Act of 2002 was enacted, the primary purpose of which is to protect investors through improved corporate governance and responsibilities of, and disclosures by, public companies. The Act contains provisions for the limitations of services that external auditors may provide as well as requirements for the credentials of Audit Committee members. In addition, the principal executive and principal financial officers are required to certify in quarterly and annual reports that they have reviewed the report; and based on the officers’ knowledge, the reports accurately present the financial condition and results of operations of the Company and contain no untrue statement or omission of material fact. The officers also certify their responsibility for establishing and maintaining a system of internal controls, which insure that all material information is made known to the officers; this certification also includes the evaluation of the effectiveness of disclosure controls and procedures and their impact upon financial reporting. Section 404 of the Act, entitled Management Assessment of Internal Controls, requires that each annual report include an internal control report which states that it is the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting, as well as an assessment by management of the effectiveness of the internal control structure and procedures for financial reporting. This section further requires that the external auditors attest to, and report on, the

Company's internal controls over financial reporting. The Dodd-Frank Wall Street Reform and Consumer Protection Act enacted an exemption to the attestation and the reporting on the Company's internal controls over financial reporting by the external auditors for non-accelerated filers, those with public float of less than \$75 million.

Recent Legislative Developments

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Act”) was signed into law on July 21, 2010 and has had a major impact on the financial services industry, including the organization, financial condition and operations of banks and bank holding companies. Many of the provisions of the Act are aimed at financial institutions that are significantly larger than the Company and the Bank. Notwithstanding this, there are many other provisions that the Company and the Bank are subject to and have to comply with, including any applicable rules promulgated by the Bureau of Consumer Financial Protection. As rules and regulations are promulgated by the agencies responsible for implementing and enforcing the Act, the Company and the Bank will have to address each to ensure compliance with applicable provisions of the Act and compliance costs are expected to increase.

The Dodd-Frank Act broadened the base for Federal Deposit Insurance Corporation insurance assessments. Under rules issued by the FDIC in February 2011, the base for insurance assessments changed from domestic deposits to consolidated assets less tangible equity. Assessment rates are calculated using formulas that take into account the risks of the institution being assessed. The rule was effective beginning April 1, 2011. This did not have a material impact on the Company.

On June 28, 2011, the Federal Reserve Board approved a final debit-card interchange rule. This primarily impacts larger banks and did not have a material impact on the Company.

It is difficult to predict at this time what specific impact yet to be implemented Dodd-Frank Act rules and regulations will have on the Company. Financial reform legislation and any implementing rules that are ultimately issued could have adverse implications on the financial industry, the competitive environment, and the Bank’s ability to conduct business. Management will have to apply resources to ensure compliance with all applicable provisions of the Dodd-Frank Act and any implementing rules, which may increase its costs of operations and adversely impact its earnings.

In July 2013, the FRB, the OCC and the FDIC approved final rules (the “New Capital Rules”) establishing a new comprehensive capital framework for U.S. Banking organizations. The New Capital Rules generally implement the Basel Committee on Banking Supervision’s (the “Basel Committee”) December 2010 final capital framework referred to as “Basel III” for strengthening international capital standards. The New Capital Rules substantially revise the risk-based capital requirements applicable to bank holding companies and their depository institution subsidiaries, including the Company and the Bank, as compared to the current U.S. general risk-based capital rules. The New Capital Rules revise the definitions and the components of regulatory capital, as well as address other issues affecting the numerator in banking institutions’ regulatory capital ratios. The New Capital Rules also address asset risk weights and other matters affecting the denominator in banking institutions’ regulatory capital ratios and replace the existing general risk-weighting approach with a more risk-sensitive approach based, in part, on the “standardized approach” in

the Basel Committee's 2004 capital accords. In addition, the New Capital Rules implement certain provisions of the Dodd-Frank Act. The New Capital Rules became effective for the Company on January 1, 2015. The Company has not experienced any difficulties in complying with these new regulations.

Recent Developments with Regulators

In September 2014, the Bank's formal written agreement (the "Agreement") with the Office of the Comptroller of the Currency which had been entered into in February 2009 was terminated. The Agreement required the Bank to review, adopt and implement a number of policies and programs related to credit and operational issues.

Available Information

The Company's website address is <https://www.bankpatriot.com>; however, information found on, or that can be accessed through, the website is not incorporated by reference into this Form 10-K. The Company makes available free of charge on its website (under the links entitled "For Investors", then "SEC filings" and then "Documents"), its annual report on Form 10-K, its quarterly reports on Form 10-Q, current reports on Form 8-K, information statements on Schedule 14C, and amendments to those reports filed or furnished pursuant to Section 13(a) of the Securities Exchange Act of 1934 as soon as practicable after we electronically file such reports with or furnish these to the SEC. Because the Company is an electronic filer, such reports are filed with the SEC and are also available on their website (<http://www.sec.gov>). The public may also read and copy any materials filed with the SEC at the SEC's Public Reference Room, 100 F Street, NE, Washington, DC 20549. Information about the Public Reference Room can be obtained by calling 1-800-SEC-0330.

ITEM 1A. Risk Factors

The Bank's financial condition and results of operation are subject to various risks inherent to its business, including those noted below.

The risks involved in the Company's commercial real estate loan portfolio are material.

The Company's commercial real estate loan portfolio constitutes a material portion of the Bank's assets and generally have different risks than residential mortgage loans. Commercial real estate loans often involve larger loan balances concentrated with single borrowers or groups of related borrowers as compared to single-family residential loans.

Because the repayment of commercial real estate loans depends on the successful management and operation of the borrower's properties or related businesses, repayments of such loans can be affected by adverse conditions in the real estate market or local economy. A downturn in the real estate market within the Company's market area may adversely impact the value of properties securing these loans. These risks are partially offset by shorter terms, reduced loan-to-value ratios and guarantors.

Real estate lending in the Company's core market involves risks related to a decline in value of commercial and residential real estate.

The market value of real estate can fluctuate significantly in a relatively short period of time as a result of market conditions in the geographic area in which the real estate is located. A significant portion of the Company's total loan portfolio is secured by real estate located in Fairfield County, Connecticut and Westchester County, New York, areas historically of high affluence that had been materially impacted by the financial troubles experienced by large financial service companies on Wall Street and other companies during the financial crisis. Since then, credit markets have become tighter and underwriting standards more stringent and the inability of purchasers of real estate to obtain financing will continue to impact the real estate market. Therefore, these loans may be subject to changes in grade, classification, accrual status, foreclosure, or loss which could have an effect on the adequacy of the allowance for loan losses.

The Company's business is subject to various lending and other economic risks that could adversely impact the Company's results of operations and financial condition.

Changes in economic conditions, particularly a continued economic slowdown in Fairfield County, Connecticut and the New York metropolitan area, could result in the following consequences, any of which may hurt the business of the Company materially:

loan delinquencies may increase

problem assets and foreclosures may increase

demand for the Bank's products and services may decline; and

Assets and collateral associated with the Bank's loans, especially real estate, may decline in value, thereby reducing a customer's borrowing power.

During the years 2007 through 2009, the general economic conditions and specific business conditions in the United States, including Fairfield County, Connecticut and the New York metropolitan area, deteriorated, resulting in increases in loan delinquencies, problem assets and foreclosures and declines in the value and collateral associated with the Bank's loans. During 2010 through 2015 however, the economic climate improved gradually, contributing to decreases in the Bank's non-performing assets.

The Company's allowance for loan losses may not be adequate to cover actual losses.

Like all financial institutions, the Bank maintains an allowance for loan losses to provide for loan defaults and non-performance. The allowance for loan losses is based on an evaluation of the risks associated with the Bank's loans receivable as well as the Bank's prior loss experience. Deterioration in general economic conditions and unforeseen risks affecting customers could have an adverse effect on borrowers' capacity to timely repay their obligations before risk grades could reflect those changing conditions. Maintaining the adequacy of the Bank's allowance for loan losses may require that the Bank make significant and unanticipated increases in the provision for loan losses, which would materially affect the results of operations and capital adequacy. The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates that may be beyond the Bank's control and these losses may exceed current estimates. Although the current economic environment has improved, conditions remain uncertain which may result in additional risk of loan losses.

Federal regulatory agencies, as an integral part of their examination process, review the Bank's loans and assess the adequacy of the allowance for loan losses. The regulatory agencies may require us to change classifications or grades on loans, increase the allowance for loan losses with additional provisions for loan losses and to recognize further loan charge-offs based upon their judgments, which may differ from the Bank's. Any increase in the allowance for loan losses required by these regulatory agencies could have a negative effect on the Bank's results of operations and financial condition. While management believes that the allowance for loan losses is currently adequate to cover inherent losses, further loan deterioration could occur and therefore management cannot assure shareholders that there will not be a need to increase the allowance for loan losses or that the regulators will not require management to increase this allowance. Either of these occurrences could materially and adversely affect the Company's earnings and profitability.

The Company is subject to certain risks with respect to liquidity.

"Liquidity" refers to the Company's ability to generate sufficient cash flows to support its operations and to fulfill its obligations, including commitments to originate loans, to repay its wholesale borrowings and other liabilities, and to satisfy the withdrawal of deposits by its customers.

The Company's primary sources of liquidity are the deposits it acquires organically through its branch network, borrowed funds, primarily in the form of wholesale borrowings, and the cash flows generated through the repayment of loans and securities. In addition, depending on current market conditions, the Company may have the ability to access the capital markets.

Deposit flows, calls of investment securities and wholesale borrowings, and prepayments of loans and mortgage-related securities are strongly influenced by such external factors as the direction of interest rates, whether actual or perceived; local and national economic conditions; and competition for deposits and loans in the markets it serve. Furthermore, changes to the underwriting guidelines for wholesale borrowings or lending policies may limit or restrict the Company's ability to borrow, and could therefore have a significant adverse impact on its liquidity. A decline in available funding could adversely impact the Company's ability to originate loans, invest in securities, and meet its expenses, or to fulfill such obligations as repaying its borrowings or meeting deposit withdrawal demands.

The Company's business is subject to interest rate risk and variations in interest rates may negatively affect the Company's financial performance.

The Company is unable to predict with certainty, fluctuations of market interest rates, which are affected by many factors including inflation, recession, a rise in unemployment, a tightening money supply, domestic and international disorder and instability in domestic and foreign financial markets. Changes in the interest rate environment may reduce the Company's profits. The Company realizes income from the differential or "spread" between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits, borrowings and other interest-bearing liabilities. Net interest spreads are affected by the difference between the maturities and repricing characteristics of interest-earning assets and interest-bearing liabilities. In addition, an increase in the general level of interest rates may adversely affect the ability of some borrowers to pay the interest on and principal of their obligations. Although the Company has implemented strategies which are designed to reduce the potential effects of changes in interest rates on operations, these strategies may not always be successful. Accordingly, changes in levels of market interest rates could materially and adversely affect the Company's net interest spread, asset quality, levels of prepayments and cash flow as well as the market value of its securities portfolio and overall profitability.

The Company's investment portfolio includes securities which are sensitive to interest rates and variations in interest rates may adversely impact the Company's profitability.

The Company's security portfolio is classified as available-for-sale, and is comprised primarily of debt and mortgage-backed securities, which are insured or guaranteed by U.S. government agencies, and corporate bonds. These securities are sensitive to interest rate fluctuations. Unrealized gains or losses in the available-for-sale portfolio for securities are reported as a separate component of shareholders' equity. As a result, future interest rate fluctuations may impact shareholders' equity, causing material fluctuations from quarter to quarter. The inability to hold its securities until maturity, or until payments are received on mortgage-backed securities, or until market conditions are favorable for a sale, could adversely affect the Company's earnings and profitability.

The Company is dependent on its management team and the loss of its senior executive officers or other key employees could impair its relationship with its customers and adversely affect its business and financial results.

The Company's success is dependent upon the continued services and skills of its management team. The unexpected loss of services of one or more of these key personnel, because of their skills, knowledge of the Company's market, years of industry experience and the difficulty of promptly finding qualified replacement personnel could have an adverse impact on the Company's business.

The Company's success also depends, in part, on its continued ability to attract and retain experienced commercial lenders and retail bankers, as well as other management personnel. The loss of the services of several of such key personnel could adversely affect the Company's growth and prospects to the extent it is unable to quickly replace such personnel. Competition for commercial lenders and retail bankers is strong, and the Company may not be successful in retaining or attracting such personnel.

A breach of information security could negatively affect the Company's earnings.

The Company increasingly depends upon data processing, communications and information exchange on a variety of computing platforms and networks, and the internet to conduct its business. The Company cannot be certain that all of its systems are entirely free from vulnerability to attack, despite safeguards it has instituted. In addition, the Company relies on the services of a variety of vendors to meet its data processing and communication needs. If information security is breached, information can be lost or misappropriated and could result in financial loss or costs to the Company or damages to others. These costs or losses could materially exceed the amount of insurance coverage, if any, which would have an adverse effect on the Company's results of operations and financial condition. In addition, the Bank's reputation could be harmed, which also could materially affect the Company's financial condition and results of operations.

The Bank is subject to environmental liability risk associated with its lending activities.

A significant portion of the Bank's loan portfolio is secured by real property. During the ordinary course of business, the Bank may foreclose on, and take title to, properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on these properties, which may make the Bank liable for remediation costs, as well as for personal injury and property damage. In addition, the Bank owns and operates certain properties that may be subject to similar environmental liability risks.

Environmental laws may require the Bank to incur substantial expense and may materially reduce the affected property's value, or limit the Bank's ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase the Bank's exposure to environmental liability. Although the Company has policies and procedures requiring the performance of an environmental site assessment before loan approval or initiating any foreclosure action on real property, these assessments may not be sufficient to detect all potential environmental hazards. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on its financial condition and results of operations.

The Company relies on the dividends it receives from its subsidiary.

The Company is a separate and distinct legal entity from the Bank, and all of the revenues the Company receives consist of dividends from the Bank. These dividends are the primary funding source for the interest and principal payments on its debt. Various federal and state laws and regulations limit the amount of dividends that a bank may pay to its parent company. In addition, the Company's right to participate in a distribution of assets upon the liquidation or reorganization of a subsidiary may be subject to the prior claims of the subsidiary's creditors. If the Bank is unable to pay dividends to the Company, it may not be able to pay its obligations. The inability to receive dividends from the Bank could therefore have a material adverse effect on its business, its financial condition, and its results of operations, as well as its ability to pay cash dividends to its shareholders.

The price of the Company's common stock may fluctuate.

The market price of the Company's common stock could be subject to significant fluctuations due to changes in sentiment in the market regarding the Company's operations or business prospects. Among other factors, the Company's stock price may be affected by:

operating results that vary from the expectations of management or of securities analysts and investors;
developments in the business or in the financial services sector generally;
regulatory or legislative changes affecting the industry generally or the business and operations;
operating and securities price performance of companies that investors consider to be comparable to the Company;
changes in estimates or recommendations by securities analysts or rating agencies;
announcements of strategic developments, acquisitions, dispositions, financings, and other material events by the Company or the Company's competitors; and
changes or volatility in global financial markets and economies, general market conditions, interest or foreign exchange rates, stock, commodity, credit, or asset valuations.

Difficult market conditions have adversely affected the Company's industry.

The Company is exposed to downturns in the U.S. economy, and particularly the local markets in which it operates in Connecticut and New York. During the financial crisis, declines in the housing market with falling home prices and increasing foreclosures, unemployment and under-employment, had negatively impacted the credit performance of mortgage and construction loans and resulted in significant write-downs of asset values by financial institutions, including government-sponsored enterprises as well as major commercial and investment banks. These write-downs caused many financial institutions to seek additional capital, to merge with larger and stronger institutions and, in some cases, to fail. Many lenders and institutional investors reduced or ceased providing funding to borrowers, including other financial institutions. This market turmoil and the tightening of credit led to an increased level of commercial and consumer delinquencies, lack of consumer confidence, increased market volatility and generally widespread reductions in business activity. The resulting economic pressure on consumers and lack of confidence in the financial markets have adversely affected The Company's business, financial condition and results of operations. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market conditions on the Company and other financial institutions. In particular:

Economic conditions may continue to affect market confidence levels and may cause adverse changes in payment patterns, causing increases in delinquencies, which could affect the Bank's charge-offs and provision for loan losses.

The ability to assess the creditworthiness of the Bank's customers or to estimate the values of collateral for loans may be impaired if the models and approaches the Bank uses becomes less predictive of future behaviors, valuations, assumptions or estimates due to the unpredictable economic climate.

Increasing consolidation of financial services companies as a result of current market conditions could have unexpected adverse effects upon the Bank's ability to compete effectively.

The Bank may be required to pay significantly higher FDIC premiums, special assessments, or taxes that could adversely affect its earnings.

Market developments have significantly impacted the insurance fund of the FDIC. As a result, the Bank may be required to pay higher premiums or additional special assessments that could adversely affect its earnings. The Bank is generally unable to control the amount of premiums that it is required to pay for FDIC insurance. If there are additional banks or financial institution failures, the Bank may be required to pay higher FDIC premiums than are currently assessed. These increases and any future increases or required prepayments in FDIC insurance premiums may materially adversely affect the results of operations.

The Company is subject to risks associated with taxation.

The amount of income taxes the Company is required to pay on its earnings is based on federal and state legislation and regulations. The Company provides for current and deferred taxes in its financial statements, based on the results of operations, business activity, legal structure, interpretation of tax statutes, assessment of risk of adjustment upon audit, and application of financial accounting standards. The Company may take tax return filing positions for which the final determination of tax is uncertain. The Company's net income and earnings per share may be reduced if a federal, state, or local authority assesses additional taxes that have not been provided for in the consolidated financial statements. There can be no assurance that the Company will achieve its anticipated effective tax rate either due to a change in a tax law, a change in regulatory or judicial guidance, or an audit assessment which denies previously recognized tax benefits.

Risks associated with changes in technology.

Financial products and services have become increasingly technology-driven. The Bank's ability to meet the needs of its customers competitively, and in a cost-efficient manner, is dependent on its ability to keep pace with technological advances and to invest in new technology as it becomes available. Many of the Bank's competitors have greater resources to invest in technology than the Bank does and may be better equipped to market new technology-driven products and services. The ability to keep pace with technological change is important, and the failure to do so on the part of the Bank could have a material adverse impact on its business and therefore on the financial condition and results of operations.

Strong competition within the Company's market area may limit the growth and profitability of the Company.

Competition in the banking and financial services industry is intense. The Fairfield County, Connecticut and the New York City metropolitan areas have a high concentration of financial institutions including large money center and regional banks, community banks and credit unions. Some of the Company's competitors offer products and services that the Bank currently does not offer, such as private banking and trust services. Many of these competitors have substantially greater resources and lending limits than the Company and may offer certain services that the Company does not or cannot provide. Price competition for loans and deposits might result in the Bank earning less on its loans and paying more for deposits, which would reduce net interest income. The Company expects competition to increase in the future as a result of legislative, regulatory and technological changes. The Company's profitability depends upon its continued ability to successfully compete in its market area.

Government regulation may have an adverse effect on the Company's profitability and growth.

The Company is subject to extensive regulation, supervision and examination by the Office of the Comptroller of the Currency as the Bank's chartering authority, by the FDIC, as insurer of its deposits, and by the Federal Reserve Board as regulator of the Company. Changes in state and federal banking laws and regulations or in federal monetary policies could adversely affect the Bank's ability to maintain profitability and continue to grow and, in light of recent economic conditions, such changes are expected but cannot be predicted. For example, new legislation or regulation could limit the manner in which the Company may conduct its business, including the Bank's ability to obtain financing, attract deposits, make loans and achieve satisfactory interest spreads. The laws, regulations, interpretations and enforcement policies that apply to the Company have been subject to significant, and sometimes retroactively applied, changes in recent years, and are likely to change significantly in the future.

Legislation proposing significant structural reforms to the financial services industry considered in the U.S. Congress has, among other things, created the Consumer Financial Protection Bureau, which gives broad authority to regulate

financial service providers and financial products. In addition, the Federal Reserve Bank has passed guidance on incentive compensation at the banking organizations it regulates and the United States Department of the Treasury and the federal banking regulators have issued statements calling for higher capital and liquidity requirements for banking organization. Complying with any new legislative or regulatory requirements, and any programs established thereunder by federal and state governments could have an adverse impact on the results of operations and the ability to fill positions with the most qualified candidates available.

Changing regulation of corporate governance and public disclosure.

The Company is subject to Laws, regulations and standards relating to corporate governance and public disclosure, SEC regulations and NASDAQ rules. These laws, regulations and standards are subject to varying interpretations, and as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies, which could make compliance more difficult and result in higher costs. The Company is committed to maintaining high standards of corporate governance and public disclosure. As a result, the Company's efforts to comply with evolving laws, regulations and standards have resulted in, and are likely to continue to result in, increased general and administrative expenses and a diversion of management's time and attention from revenue-generating activities to compliance activities. The Company's reputation may be harmed if it does not continue to comply with these laws, regulations and standards.

The earnings of financial institutions are significantly affected by general business and economic conditions.

As a financial institution, the Company's operations and profitability are impacted by general business and economic conditions in the United States and abroad. These conditions include short-term and long-term interest rates, inflation, money supply, political issues, legislative and regulatory changes and the strength of the U.S. economy and the local economies in which it operates, all of which are beyond the Company's control. In recent years, the banking world has experienced unprecedented upheaval, including the failure of some of the leading financial institutions in the world. Further deterioration in economic conditions could result in an increase in loan delinquencies and non-performing assets, decreases in loan collateral values and a decrease in demand for the Bank's products and services, among other things, any of which could have a material adverse impact on the Company's results of operations and financial condition and for which the Company cannot currently predict or implement plans to combat.

The Company is a "controlled company" within the meaning of the NASDAQ rules and, as a result, the Company qualifies for, and relies on, exemptions from certain corporate governance requirements.

PNBK Holdings LLC controls a majority of the Company's voting common stock. As a result, the Company is a "controlled company" within the meaning of NASDAQ corporate governance standards. Under the NASDAQ rules, a company of which more than 50% of the voting power is held by an individual, group or another company is considered a "controlled company" which may utilize exemptions relating to certain NASDAQ corporate governance requirements, including:

The requirement that the Company have a Nominating and Governance Committee that is composed entirely of independent directors;

The requirement that the Company have a Compensation Committee that is composed entirely of independent directors; and

The requirement for an annual performance evaluation of the Nominating and Governance and Compensation Committees.

As a result of these exemptions, the Company's Nominating and Governance Committee and Compensation Committee do not consist entirely of independent directors and the Company is not required to have an annual performance evaluation of the Nominating and Governance and Compensation Committees. Accordingly, a holder of its common stock will not have the same protections afforded to stockholders of companies that are subject to all of the NASDAQ corporate governance requirements.

ITEM 1B. Unresolved Staff Comments

None.

ITEM 2. Properties

The Company's corporate headquarters and main branch banking office is located at 900 Bedford Street in Stamford, Connecticut. The Bank purchased a building at 999 Bedford Street, Stamford, CT in November 2014, and intends to move the main branch banking office to this location by December 2016. The Bank purchased the current Stamford and Greenwich branch buildings in 2013. During 2014, the Bank purchased the Milford branch building and new locations for the Darien and Westport branches. During 2015, the Bank moved its corporate offices to 900 Bedford Street in Stamford, Connecticut, leaving some operational departments at the old leased location. The Bank also moved its Darien Branch to newly renovated location. The Bank intends to move from its existing branch in Westport upon completion of the new facility. At December 31, 2015, five branches were owned, another two owned buildings were in the process of becoming branch facilities, and the Bank's seven other branch banking offices and a small administrative office space was leased. The Bank also leases space at its main office for additional parking. Lease commencement dates for office locations range from January 2006 to July 2015 and lease expiration dates fall between March 2016 and July 2017. Most of the leases contain rent escalation provisions, as well as renewal options for one or more periods.

The Bank has leased excess space in two of its locations to four independent parties. For additional information regarding the Bank's lease obligations, see Note 8 to the Consolidated Financial Statements.

All leased properties are in good condition.

ITEM 3. Legal Proceedings

Neither the Company nor the Bank has any pending legal proceedings, other than ordinary routine litigation incidental to its business, to which the Company or the Bank is a party or any of its property is subject.

ITEM 4. Mine Safety Disclosures

Not applicable.

15

PART II**ITEM 5. Market for Registrant’s Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities**Market Information

The Company’s Common Stock is traded on the NASDAQ Global Market under the Symbol “PNBK.” On December 31, 2015, the last sale price for the Company’s Common Stock was \$16.40.

The following table sets forth the high and low sales prices of the Company’s Common Stock for the last two fiscal years of each quarter adjusted for a 1-for-10 reverse stock split. No cash dividends were declared during this time.

| Quarter Ended | 2015 | | Cash Dividends Declared | 2014 | | Cash Dividends Declared |
|---------------|---------|---------|-------------------------------|---------|--------|-------------------------------|
| | High | Low | | High | Low | |
| March 31 | \$15.60 | \$15.00 | \$ - | \$14.00 | \$9.60 | \$ - |
| June 30 | \$16.05 | \$13.60 | - | 17.40 | 12.00 | - |
| September 30 | \$18.68 | \$15.15 | - | 23.80 | 13.40 | - |
| December 31 | \$17.49 | \$14.55 | - | 19.40 | 15.80 | - |

 Holders

There were approximately 182 shareholders of record of the Company’s Common Stock as of December 31, 2015. This number does not reflect the number of persons or entities holding stock in nominee name through banks, brokerage firms or other nominees.

Dividends

The Company's ability to pay dividends is dependent on the Bank's ability to pay dividends to the Company. The Bank can pay dividends to the Company pursuant to a dividend policy requiring compliance with the Bank's OCC-approved capital program, in compliance with applicable law and with the prior written determination of no supervisory objection by the Assistant Deputy Comptroller. In addition to the capital program, certain other restrictions exist regarding the ability of the Bank to transfer funds to the Company in the form of cash dividends, loans or advances. The approval of the OCC is required to pay dividends in excess of the Bank's earnings retained in the current year plus retained net earnings for the preceding two years. The Company is also prohibited from paying dividends that would reduce its capital ratios below minimum regulatory requirements. The Federal Reserve Bank has also imposed dividend restrictions on the Company.

OCC regulations impose limitations upon all capital distributions by commercial institutions, like the Bank, such as dividends and payments to repurchase or otherwise acquire shares. The Company may not declare or pay cash dividends on or repurchase any of its shares of common stock if the effect thereof would cause stockholders' equity to be reduced below applicable regulatory capital maintenance requirements, or if such declaration and payments would otherwise violate regulatory requirements.

Recent Sales of Unregistered Securities

During the fourth quarter of 2015, the Company did not have any sales of unregistered securities.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

None.

Performance Graph

The performance graph compares the yearly percentage change in the Company's cumulative total shareholder return on its common stock over the last five fiscal years to the cumulative total return of the S&P 500 Index and the NASDAQ Bank Index. Total shareholder return is measured by dividing the sum of the cumulative amount of dividends for the measurement period (assuming dividend reinvestment) and the difference between the Company's share price at the end and the beginning of the measurement period, by the share price at the beginning of the measurement period.

| Index | Period Ending | | | | |
|-------|-----------------------|------------|------------|------------|------------|
| | 12/31/2010 | 12/31/2011 | 12/31/2012 | 12/31/2013 | 12/12/2014 |

| | | | | | | |
|---------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Patriot National Bancorp | 100.0 | 112.9 | 80.6 | 67.1 | 105.8 | 93.9 |
| Nasdaq Bank Index | 100.0 | 98.0 | 113.5 | 157.6 | 162.1 | 172.8 |
| S&P 500 | 100.0 | 112.8 | 127.9 | 165.8 | 184.6 | 183.3 |

ITEM 6. Selected Financial Data**At or for the year ended December 31,**

| | 2015 | 2014 | 2013 | 2012 | 2011 |
|--|----------|----------|----------|----------|----------|
| <i>(Dollars in thousands, except per share data)</i> | | | | | |
| Balance Sheet Data: | | | | | |
| Cash and due from banks | \$85,400 | \$73,258 | \$34,866 | \$70,303 | \$54,716 |
| Federal funds sold | - | - | - | - | - |
| Short-term investments | - | - | - | 711 | 710 |
| Investment securities | 42,472 | 46,818 | 47,738 | 51,293 | 76,185 |
| Loans, net | 479,127 | 471,984 | 418,148 | 458,794 | 501,227 |
| Total assets (2) | 653,531 | 632,624 | 541,248 | 617,855 | 665,816 |
| Total deposits (1) | 447,047 | 443,033 | 430,204 | 497,283 | 544,909 |
| Total borrowings | 142,187 | 128,248 | 65,248 | 65,248 | 65,248 |
| Total shareholders' equity | 61,464 | 58,735 | 41,841 | 49,568 | 50,550 |

Operating Data:

| | | | | | |
|--------------------------------------|----------|-----------|----------|----------|-----------|
| Interest and dividend income | \$23,741 | \$20,368 | \$21,654 | \$25,216 | \$28,332 |
| Interest expense | 2,690 | 2,970 | 4,854 | 7,419 | 8,510 |
| Net interest income | 21,051 | 17,398 | 16,800 | 17,797 | 19,822 |
| Provision for loan losses | 250 | - | 970 | (2,379) | 7,464 |
| Non-interest income | 1,551 | 1,832 | 2,426 | 3,274 | 3,411 |
| Non-interest expense | 18,851 | 18,271 | 28,554 | 23,986 | 31,228 |
| Provision (benefit) for income taxes | 1,358 | (14,750) | (339) | - | - |
| Net income (loss) | 2,143 | 15,709 | (7,289) | (536) | (15,459) |

Per Share Data:

| | | | | | |
|-------------------------------------|------|------|---------|---------|---------|
| Basic income (loss) per share (3) | 0.55 | 4.08 | (1.90) | (0.14) | (4.00) |
| Diluted income (loss) per share (3) | 0.55 | 4.05 | (1.90) | (0.14) | (4.00) |

Key Performance Ratios:

| | | | | | | | | | | |
|----------------------------------|------|---|-------|---|----------|----------|----------|---|------|---|
| Return on average assets | 0.34 | % | 2.81 | % | (1.28%) | (0.08%) | (2.29%) | | | |
| Return on average equity | 3.55 | % | 32.94 | % | (16.43%) | (1.05%) | (27.64%) | | | |
| Dividend payout ratio | N/A | | N/A | | N/A | N/A | N/A | | | |
| Average equity to average assets | 9.65 | % | 8.53 | % | 7.80 | % | 7.96 | % | 8.28 | % |

(1) Includes \$24.7 million of deposits held for sale at December 31, 2012.

(2) Includes \$88,000 of branch assets held for sale at December 31, 2012.

(3) All common stock and per share data have been restated to give effect to a reverse stock split of 1-for-10 effective March 4, 2015.

ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operation

Critical Accounting Policies

The preparation of consolidated financial statements in accordance with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and to disclose contingent assets and liabilities. Actual results could differ from those estimates. Management has identified accounting for the allowance for loan losses, the analysis and valuation of its investment securities and the valuation of deferred tax assets, as the Company's most critical accounting policies and estimates in that they are important to the portrayal of the Company's financial condition and results. They require management's most subjective and complex judgment as a result of the need to make estimates about the effect of matters that are inherently uncertain.

The Company's significant accounting policies are described in Note 1 to the Consolidated Financial Statements included in this 2015 Annual Report on Form 10-K.

The Company has adopted various accounting policies that govern the application of accounting principles generally accepted in the United States of America (U.S. GAAP) and that are consistent with general practices within the banking industry in the preparation of its financial statements. Certain accounting policies involve significant judgments and assumptions by the Company that have a material impact on the carrying value of certain assets and liabilities. The Company considers these accounting policies to be critical accounting policies. The judgment and assumptions used are based on historical experience and other factors, which are believed to be reasonable under the circumstances. Because of the nature of the judgments and assumptions management makes, actual results could differ from these judgments and estimates, which could have a material impact on the carrying values of the Company's assets and liabilities and results of operations.

Allowance for Loan Losses. The Company maintains an allowance for loan losses at a level management believes is sufficient to absorb estimated credit losses incurred as of the report date. Management's determination of the adequacy of the allowance is based on periodic evaluations of the loan portfolio and other relevant factors. However, this evaluation is inherently subjective as it requires significant estimates by management. Consideration is given to a variety of factors in establishing these estimates including historical losses, peer and industry data, current economic conditions, the size and composition of the loan portfolio, delinquency statistics, criticized and classified assets and impaired loans, results of internal loan reviews, borrowers' perceived financial and management strengths, the adequacy of underlying collateral, the dependence on collateral, or the strength of the present value of future cash flows and other relevant factors. These factors may be susceptible to significant change. To the extent actual outcomes differ from management estimates, additional provisions for loan losses may be required which may adversely affect the Company's results of operations in the future. Subsequent to acquisition of purchased-credit-impaired loans, estimates of cash flows expected to be collected are updated each reporting period based on updated assumptions

regarding default rates, loss severities, and other factors that are reflective of current market conditions. Subsequent decreases in expected cash flows will generally result in a provision for loan losses. Subsequent increases in expected cash flows result in a reversal of the provision for loan losses to the extent of prior charges.

Unrealized Gains and Losses on Securities Available for Sale. The Company receives estimated fair values of debt securities from independent valuation services and brokers. In developing these fair values, the valuation services and brokers use estimates of cash flows based on historical performance of similar instruments in similar rate environments. Debt securities available for sale consist primarily of mortgage-backed securities issued by U.S. government-sponsored agencies. The Company uses various indicators in determining whether a security is other-than-temporarily impaired including, for debt securities, when it is probable that the contractual interest and principal will not be collected, or for equity securities, whether the market value is below its cost for an extended period of time with low expectation of recovery. The debt securities are monitored for changes in credit ratings because adverse changes in credit ratings could indicate a change in the estimated cash flows of the underlying collateral or issuer. For marketable equity securities, The Company considers the issuer's financial condition, capital strength and near term prospects to determine whether an impairment is temporary or other-than-temporary. The Company also considers the volatility of a security's price in comparison to the market as a whole and any recoveries or declines in fair value subsequent to the balance sheet date. If management determines that the impairment is other-than-temporary, the entire amount of the impairment as of the balance sheet date is recognized in earnings even if the decision to sell the security has not been made. The fair value of the security becomes the new amortized cost basis of the investment and is not adjusted for subsequent recoveries in fair value. The unrealized losses associated with available-for-sale debt securities were not considered to be other-than-temporarily impaired as of December 31, 2015 and 2014 because the unrealized losses were related to changes in interest rates and did not affect the expected cash flows of the underlying collateral or issuer. The unrealized losses associated with the equity investments were also not considered other-than-temporarily impaired as of December 31, 2015 and 2014. Management concluded that the decline in fair value was temporary and would recover by way of increases in market price or positive changes in foreign currency exchange rates.

Deferred Income Taxes. The Company provides for deferred income taxes on the liability method whereby tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities in the financial statements and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Summary

During 2015, the Company achieved net income, second consecutive year since 2007, primarily as a result of balance sheet and operational restructuring initiatives implemented during 2013, 2014 and 2015 by new executive management.

The following were among the Company's notable achievements in 2015:

Net interest margin (NIM) of 3.60%

The amount of classified assets outstanding continues to decline and the overall risk rating for the portfolio has improved

Average non-interest bearing deposits increased \$13.0 million.

As compared to December 31, 2014

o Total cash and cash equivalents growth of \$12.1 million or 16.6%

o Improved Tier 1 to average assets capital ratios

o Increase in total interest and dividend income of \$3.4 million or 16.6%

o Increase in income before taxes of \$2.5 million or 265.0%

FINANCIAL CONDITION

Assets

The Company's total assets increased \$20.9 million, or 3.3%, from \$632.6 million at December 31, 2014 to \$653.5 million at December 31, 2015 as generation of income and increased in the Bank's borrowings.

Cash and cash equivalents increased \$12.1 million primarily due to the Bank's efforts to increase liquidity.

Net loans increased \$7.1 million as originations exceeded payments of loan principal.

Premises and equipment net increased by \$7.1 million. The increase was primarily due to the purchase of \$6.0 million in owned premises, including the purchase of a branch property previously leased and the construction of a new branch in a town where the Company has leased space historically. Equipment increased by \$1.0 million, net of depreciation and dispositions, as the Company invested in its network infrastructure, its website and communications-related technology.

Deferred tax assets of \$13.8 million were reported at December 31, 2015.

Investments

The following table is a summary of the Company's investment portfolio at fair value at December 31 for the years shown.

| <i>(in thousands)</i> | 2015 | 2014 | 2013 |
|--|-------------|-------------|-------------|
| U.S. Government Agency bonds | \$4,954 | \$7,409 | \$7,079 |
| U.S. Government Agency mortgage- backed securities | 13,413 | 17,337 | 21,752 |
| Corporate bonds | 9,010 | 8,936 | 8,870 |
| Subordinate bonds | 2,000 | - | - |
| Federal Reserve Bank stock | 2,075 | 2,058 | 1,444 |
| Federal Home Loan Bank stock | 6,570 | 6,628 | 4,143 |