



# TIMELESS VISION.

AMERICAN VALUES *at* WORK.



2013 ANNUAL REPORT

## Corporate Information

### Board of Directors

**Frank Banko III**

*President, Warren Distributing*

**Geoffrey F. Boyer, CFP**

*Owner & Principal, Boyer Financial Group*

**John P. Brew, Jr.**

*Co-Chairman, Seifried & Brew LLC*

*Independent Contractor, IPI*

*CEO, Jay Brew LLC*

**Robert P. Daday**

*Retired PPL Executive*

**John G. Engleson**

*President, zAxis Corporation*

*Executive V.P. & Secretary,*

*Integrity Business Services, LLC*

**Elmer D. Gates**

*Lead Director, Embassy Bancorp, Inc. and*

*Embassy Bank for the Lehigh Valley*

**M. Bernadette Holland, CFP**

*Senior Vice President,*

*Janney Montgomery Scott, LLC*

**Bernard M. Lesavoy, Esquire**

*Member/Partner, Lesavoy Butz & Seitz LLC*

**David M. Lobach, Jr.**

*Chairman of the Board, CEO & President*

*Embassy Bancorp, Inc. and*

*Embassy Bank for the Lehigh Valley*

**John C. Pittman**

*President & CEO*

*John C Pittman Sport Stars Inc.*

**John T. Yurconic**

*President, JTY, Inc.*

*President, Insurance Premium Financing, Inc.*

## Officers

### Executive Officers

**David M. Lobach, Jr.**

*Chairman of the Board, CEO & President*

**Judith A. Hunsicker**

*Sr. Executive Vice President, COO, CFO,*

*Secretary & Treasurer*

**James R. Bartholomew**

*Executive Vice President & SLO Commercial Lending*

### Senior Vice Presidents

**David C. Arner, Commercial Services**

**Tracy A. Barker, Deposit Operations & Human Resources**

**Desty A. Bonstein, Business Development**

**Mark A. Casciano, Branch Administration**

**Diane M. Cunningham, Consumer Lending**

**Lynne M. Neel, Controller, Finance, Loan Operations &**

**Assistant Secretary**

**Terry M. Stecker, Commercial Lending**

### Vice Presidents

**Michelle L. Barron, Deposit Operations**

**Scott A. Karwacki, Credit Analysis**

**Michael Lahanas, Business Development**

**Michael Macy, Commercial Lending**

**Tracy L. McCarthy, Loan Operations**

**Brian Sabol, Commercial Lending**

**Brandi L. Stefanov, Branch Administration**

**Jennifer A. Tropeano, Consumer Lending**

**Kristin A. Wannisky, Marketing**

**Timothy P. Woodbridge, Commercial Lending**

### Assistant Vice Presidents

**Kathryn I. Wyant, Assistant Controller-Finance**

**Bryan D. Lobach, Commercial Services**

**Cynthia L. Morley, Commercial Lending**

**Mary Beth Mulicka, Branch Administration**

**Christine L. Pierce, Branch Administration**

**Debra A. Young, Commercial Services**

**Heather Zoito, Branch Administration**

### Assistant Treasurers

**Antonio A. Dias, Finance**

**Gina Franco, Consumer Lending**

**Jessica L. Kalavoda, Branch Administration**

**Maria McGill, Deposit Operations & Human Resources**

**Jessica S. Moyer, Branch Administration**

**Maria P. Nace, Branch Administration**

**Taryn M. Pell, Consumer Lending**

**Krystal Salce, Credit Analysis**

**Katrina Zeigler, Loan Operations**

**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 fiscal year end December 31, 2013

or

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

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

Commission file number 000-1449794

**Embassy Bancorp, Inc.**

(Exact name of registrant as specified in its charter)

**Pennsylvania**  
(State of incorporation)

**26-3339011**  
(I.R.S. Employer Identification No.)

**One Hundred Gateway Drive, Suite 100**  
**Bethlehem, PA**  
(Address of principal executive offices)

**18017**  
(Zip Code)

**(610) 882-8800**  
(Issuer's Telephone Number)

Securities registered under Section 12(b) of the Exchange Act:

**None**  
(Title of each class)

**None**  
(Name of each exchange on which registered)

Securities registered under section 12(g) of the Exchange Act:

**Common Stock, Par Value \$1.00 per share**

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

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

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 filing requirements for the past 90 days. Yes [ **X** ] 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 [ **X** ] No [ ]

Indicate by check mark if disclosure of delinquent filers in response to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K [ **X** ].

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

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

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

The aggregate market value of the registrant's common stock held by non-affiliates at June 30, 2013, the registrant's most recently completed second fiscal quarter was \$**32,954,055**.

(APPLICABLE ONLY TO CORPORATE REGISTRANTS)

Indicate the number of shares outstanding of each of the registrant's classes of common equity, as of the latest practicable date:

**COMMON STOCK**

**Number of shares outstanding as of March 25, 2014**

**(\$1.00 Par Value)**

**7,333,764**

(Title Class)

(Outstanding Shares)

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement for the 2014 annual meeting of shareholders are incorporated by reference into Part III of this report.

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## **PART I**

### **Item 1. BUSINESS.**

#### **General**

Embassy Bancorp, Inc. (the “Company”) is a Pennsylvania corporation organized in 2008 and registered as a bank holding company pursuant to the Bank Holding Company Act of 1956, as amended (the “BHC Act”). The Company was formed for purposes of acquiring Embassy Bank For The Lehigh Valley (the “Bank”) in connection with the reorganization of the Bank into a bank holding company structure, which was consummated on November 11, 2008. Accordingly, the Company owns all of the capital stock of the Bank, giving the organization more flexibility in meeting its capital needs as the Company continues to grow.

The Bank, which is the Company’s principal operating subsidiary, was originally incorporated as a Pennsylvania bank on May 11, 2001 and opened its doors on November 6, 2001. It was formed by a group of local business persons and professionals with significant prior experience in community banking in the Lehigh Valley area of Pennsylvania, the Bank’s primary market area.

#### **Mission**

The Company provides a traditional range of financial products and services to meet the depository and credit needs of individual consumers, small and medium sized businesses and professionals in its market area. As a locally owned and operated community bank, there is a strong focus on service that is highly personalized, efficient and responsive to local needs. It is the intention of the Company to deliver its products and services with the care and professionalism expected of a community bank and with a special dedication to personalized service. To create this environment, the Company employs a well-trained, highly motivated staff, all with previous banking experience, and interested in building quality client relationships using state-of-the-art delivery systems and client service facilities. The Company’s senior management has extensive banking experience. The Company’s goal is to serve the financial needs of its clients and provide a profitable return to its investors, consistent with safe and sound banking practices. The Company focuses on establishing and retaining customer relationships by offering a broad range of financial services, competitively-priced and delivered in a responsive manner. Correspondent relationships are utilized where it is cost beneficial. The specific objectives of the Company are: 1) to provide individuals, professionals and local businesses with the highest standard of relationship banking in the local market; 2) to attract deposits and loans by offering state of the art products and services with competitive pricing; 3) to provide a reasonable return to shareholders on capital invested; and 4) to attract, train and retain a happy, motivated and team oriented group of banking professionals dedicated to meeting the Company’s objectives.

#### **Market “Niche”**

The Company provides the traditional array of commercial banking products and services emphasizing one-on-one delivery to consumers and businesses located in Lehigh and Northampton Counties in Pennsylvania. In the Company’s primary market area, which is dominated by offices of large statewide, regional and interstate banking institutions, banking services that are furnished in a friendly and courteous manner with a timely response to customer needs fill a “niche” that arises due to the loss of local institutions through merger and acquisitions.

#### **Deposits**

The Company offers small business cash management services to help local companies better manage their cash flow, in order for the Company to attract and retain stable deposit relationships. The expertise and experience of the Company’s management coupled with the latest technology accessed through third party providers enables the Company to maximize the growth of business-related deposits.

As for consumers, deposit growth is driven by a variety of factors including, but not limited to, population growth, bank and non-bank competition, increase in household income, interest rates, accessibility of location and the sales efforts of Company personnel. Time deposits can be attracted and/or increased by paying an interest rate higher than

that offered by competitors, but they are the most costly type of deposit. The most profitable type of deposits are non-interest bearing demand (checking) accounts which can be attracted by offering free checking. However, both high interest rates and free checking accounts generate certain expenses for a bank and the desire to increase deposits must be balanced with the need to be profitable. The deposit services of the Company are generally comprised of demand deposits, savings deposits, money market deposits, time deposits and Individual Retirement Accounts.

## **Loans**

The loan portfolio of the Company consists primarily of secured fixed-rate and variable-rate loans, with a significant concentration in commercial-purpose transactions and consumer residential mortgage and home equity loans. While most credit facilities are appropriately collateralized, major emphasis is placed upon the financial condition of the borrower and evaluating the borrower's cash flow versus debt service requirements. The Company has an experienced lending team. The Company believes that the familiarity of its experienced management team and members of the Company's Loan Committee with prospective local borrowers enables the Company to better evaluate the character, integrity and creditworthiness of the prospective borrowers.

Loan growth is driven by customer demand, which in turn is influenced by individual and business indebtedness and consumer demand for goods. The Company's loan officers call upon accountants, financial planners, attorneys, local realtors and others to generate loan referrals. A performing loan is a loan which is being repaid according to its original terms and is the most desirable type of loan that a bank seeks to make. Again, a balancing act is required for the Company inasmuch as loaning money will always entail some risk. Without loaning money, however, a bank cannot generate enough earnings to be profitable. The risk involved in each loan must, therefore, be carefully evaluated before the loan is made. The interest rate at which the loan is made should always reflect the risk factors involved, including the term of the loan, the value of collateral, if any, the reliability of the projected source of repayment and the amount of the loan requested. Credit quality will always be the Company's most important factor.

The Company has not been involved in any "sub-prime" mortgage lending and has not purchased or invested in any securities backed by or which include sub-prime loans.

## **Business Lending**

The Company is generally targeting businesses with annual revenues of less than \$10 million. These customers tend to be ignored by the larger institutions and have felt the most negative effects of the recent bank consolidations. The Company offers responsiveness, flexibility and local decision making for loan applications of small business owners thereby eliminating delays caused by non-local management. The Company participates in programs offered through local, state and federal programs and may participate in Small Business Administration (SBA) programs.

## **Consumer Lending**

The Company offers its retail customer base a product line of consumer loan services including mortgage loans, secured home equity loans, lines of credit, auto loans, and to a much lesser extent, unsecured personal loans.

## **Residential Mortgage Loans**

The Company offers a range of specialty home equity and mortgage products at competitive rates. The Company seeks to capitalize on its policy of closing loans in a time frame that will meet the needs of its borrowers.

## **Commercial Mortgage/Construction Loans**

The Company originates various types of loans secured by real estate, including, to a limited extent, construction loans. Construction loans are generally priced at floating rates tied to current market rates. Upon completion of construction, these loans may be converted into permanent commercial and residential loans. Construction lending is expected to constitute a minor portion of the Company's loan portfolio.

In some cases, the Company originates loans larger than its lending limit and enters into participation arrangements for those loans with other banks.

As an independent community bank, the Company serves the special needs of legal, medical, accounting, financial service providers and other professionals. Commercial mortgages, lines of credit, term loans and demand loans are tailored to meet the needs of the Company's customers in the professional community. In addition to the usual criteria for pricing credit-related products, the Company takes into consideration the overall customer relationship to establish credit pricing. Deposit relationships in demand, savings, money market, and certificate accounts are considered in loan pricing along with the credit worthiness of the borrower.

### **Other Services**

To further attract and retain customer relationships, the Company provides or will provide the standard array of financial services expected of a community bank, which include the following:

Treasurer Checks	Remote Deposit Capture
Certified Checks	Safe Deposit Boxes
Gift Cards	Night Depository Services
Wire Transfers	Bond Coupon Redemptions
Savings Bond Redemptions	Bank by Mail
Credit/Debit Card Merchant Processing	Automated Teller Machines
Direct Deposit/ACH Services	On-Line Banking and Bill Pay
Cash Management Services	Commercial Credit Cards
Escrow Management Services	ATM and Debit Cards

### **Fee Income**

Fee income is non-interest related. The Company earns fee income by charging customers for banking services, credit card and merchant processing, treasurer's checks, overdrafts, wire transfers, bond coupon redemptions, and check orders, as well as other deposit and loan related fees.

### **Community Reinvestment Act**

The Community Reinvestment Act of 1977 ("CRA") is designed to create a system for bank regulatory agencies to evaluate a depository institution's record in meeting the credit needs of its community. The Company had its last CRA examination in 2012 and received a "satisfactory" rating.

The Company's Directors and Officers are committed to reaching out to the community in which they live and work. The personal, business and community rewards for helping local residents and businesses are numerous. The Board is dedicated to recognizing an ongoing commitment and understanding of the Company's responsibility under the CRA. The Company is committed to providing access to credit and deposit products for all members of the communities that it serves.

### **Service Area**

The Company draws its primary deposits and business from areas immediately surrounding its principal office in Hanover Township, Pennsylvania and its branch offices in South Whitehall Township, Lower Macungie Township, the City of Bethlehem, Salisbury Township, Lower Saucon Township and Lower Nazareth Township, Pennsylvania, as well as the remainder of Lehigh and Northampton Counties in Pennsylvania.

## **Bank Premises**

The Company leases each of its bank operations premises, situated at the following locations:

1. Hanover Township, Northampton County
2. South Whitehall Township, Lehigh County
3. Salisbury Township, Lehigh County
4. Lower Macungie Township, Lehigh County
5. City of Bethlehem, Lehigh County
6. Lower Saucon Township, Northampton County
7. Lower Nazareth Township, Northampton County

The Company pays certain additional expenses of occupying these spaces including, but not necessarily limited to, real estate taxes, insurance, utilities and repairs. The Company is obligated under the leases to maintain the premises in good order, condition and repair.

## **Employees**

As of December 31, 2013, the Company had a total of 71 full-time equivalent employees.

## **Competition**

The banking business is highly competitive. The Company competes with local banks as well as numerous regionally based commercial banks, most of which have assets, capital and lending limits far larger than those of the Company. The Company also competes with savings banks, savings and loan associations, money market funds, insurance companies, stock brokerage firms, regulated small loan companies, credit unions and with the issuers of commercial paper and other securities. The industry competes primarily in the area of interest rates, products offered, customer service and convenience.

Among the advantages many of the Company's competitors have over the Company are larger asset and capital bases, the ability to finance wide-ranging advertising campaigns and to allocate their investment assets to regions of highest yield and demand. Larger companies have market presence in the form of more branch offices. The Company's growth in number of offices has improved its ability to compete in the market. The Company believes it is able to compete with the market in terms of interest rate and level of customer service, as reflected in growth in market share. Many competitors offer certain services such as trust services, investment services and international banking that are not offered directly by the Company and, by virtue of their greater capital, most competitors will have substantially higher lending limits than those of the Company.

## **Segments**

The Company acts as an independent community financial services provider and offers traditional banking and related financial services to individual, business and government customers. The Company offers a full array of commercial and retail financial services, including the taking of time, savings and demand deposits; the making of commercial, consumer, residential mortgage and home equity loans; and the providing of other financial services.

Management does not separately allocate expenses, including the cost of funding loan demand, between commercial and retail operations of the Company. As such, discrete financial information is not available and segment reporting would not be meaningful.

## **Seasonality**

Management does not feel that the deposits, loans, or the business of the Company are seasonal in nature. Deposit and loan generation may, however, vary with local and national economic and market conditions, but should not have a material effect on planning and policy making.

## **Supervision and Regulation**

The Company is subject to extensive regulation under federal and Pennsylvania banking laws, regulations and policies, including prescribed standards relating to capital, earnings, dividends, the repurchase or redemption of shares, loans or extensions of credit to affiliates and insiders, internal controls, information systems, internal audit systems, loan documentation, credit underwriting, asset growth, impaired assets and loan-to-value ratios. The bank regulatory framework is intended primarily for the protection of depositors, federal deposit insurance funds and the banking systems as a whole, and not for the protection of security holders.

The following summary sets forth certain of the material elements of the regulatory framework applicable to bank holding companies and their bank subsidiaries and provides certain specific information about the Company and the Bank. It does not describe all of the provisions of the statutes, regulations and policies that are identified. To the extent that the following information describes statutory and regulatory provisions, it is qualified in its entirety by express reference to each of the particular statutory and regulatory provisions. A change in applicable statutes, regulations or regulatory policy may have a material effect on the business of the Company.

### *Dodd-Frank Wall Street Reform and Consumer Protection Act*

As a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”), which became law on July 21, 2010, there is additional regulatory oversight and supervision of the Company and the Bank. The Dodd-Frank Act significantly changed the regulation of financial institutions and the financial services industry. The Dodd-Frank Act includes, and the regulations being developed thereunder will include, provisions affecting large and small financial institutions alike, including several provisions that affect the regulations of community banks and bank holding companies.

The Dodd-Frank Act, among other things, imposed new capital requirements on bank holding companies; changed the base for FDIC insurance assessments to a bank’s average consolidated total assets minus average tangible equity, rather than upon its deposit base; permanently raised the current standard deposit insurance limit to \$250,000; and expanded the FDIC’s authority to raise insurance premiums. The legislation also calls for the FDIC to raise its ratio of reserves to deposits from 1.15% to 1.35% for deposit insurance purposes by September 30, 2020 and to “offset the effect” of increased assessments on insured depository institutions with assets of less than \$10 billion.

The Dodd-Frank Act also includes provisions that affect corporate governance and executive compensation at all publicly-traded companies and allows financial institutions to pay interest on business checking accounts. The legislation also restricts proprietary trading, places restrictions on the owning or sponsoring of hedge and private equity funds, and regulates the derivatives activities of banks and their affiliates. The Dodd-Frank Act also establishes the Financial Stability Oversight Council to identify threats to the financial stability of the U.S., promote market discipline, and respond to emerging threats to the stability of the U.S. financial system.

### *Consumer Financial Protection Bureau*

The Dodd-Frank Act also establishes the Consumer Financial Protection Bureau (the “CFPB”) as an independent entity within the Board of Governors of the Federal Reserve System (the “Federal Reserve Board”). The CFPB has broad rulemaking, supervisory and enforcement authority over consumer financial products and services, including deposit products, residential mortgages, home-equity loans and credit cards. The CFPB’s rules contain provisions on mortgage-related matters such as steering incentives, and determinations as to a borrower’s ability to repay, loan servicing, and prepayment penalties.

On January 10, 2013, the CFPB issued a final regulation defining a “qualified mortgage” for purposes of the Dodd-Frank Act, and setting standards for mortgage lenders to determine whether a consumer has the ability to repay the mortgage. This regulation, which became effective on January 10, 2014, also affords safe harbor legal protections for lenders making qualified loans that are not “higher priced.” On January 17, 2013, the CFPB issued a final regulation containing new mortgage servicing rules applicable to our bank subsidiary, which took effect on January 10, 2014. The announced goal of the CFPB is to bring greater consumer protection to the mortgage servicing market. These changes affect notices to be given to consumers as to delinquency, foreclosure alternatives, modification applications,

interest rate adjustments and options for avoiding “force-placed” insurance. Servicers are prohibited from processing foreclosures when a loan modification is pending, and must wait until a loan is more than 120 days delinquent before initiating a foreclosure action.

The servicer must provide direct and ongoing access to its personnel, and provide prompt review of any loss mitigation application. Servicers must maintain accurate and accessible mortgage records for the life of a loan and until one year after the loan is paid off or transferred. We expect these new standards to add to the cost of conducting our mortgage servicing business.

### *Capital Adequacy*

The Federal banking regulators have adopted risk-based capital guidelines for bank holding companies. Currently, the required minimum ratio of total capital to risk-weighted assets (including off-balance sheet activities, such as standby letters of credit) is 8% (10% in order to be considered “well-capitalized”). At least 4% of the total capital (6% to be well-capitalized) is required to be Tier 1 capital, consisting principally of common shareholders’ equity, related surplus, retained earnings, qualifying perpetual preferred stock, and minority interests in the equity accounts of consolidated subsidiaries, less goodwill and certain other intangibles. The remainder (Tier 2 capital) may consist of a limited amount of subordinated debt, certain hybrid capital instruments and other debt securities, qualifying preferred stock and a limited amount of the general loan loss allowance.

In addition to the risk-based capital guidelines, the federal banking regulators established minimum leverage ratio (Tier 1 capital to total assets) guidelines for bank holding companies. These guidelines provide for a minimum leverage ratio of 3% for those bank holding companies which have the highest regulatory examination ratings and are not contemplating or experiencing significant growth or expansion. All other bank holding companies are required to maintain a leverage ratio of at least 4%.

At December 31, 2013, the Company qualified as “well-capitalized” under the foregoing regulatory capital standards. See Note 16 of the Notes to Consolidated Financial Statements included in Item 8 of this Report.

### *New Capital Rules*

In July 2013, the Federal Deposit Insurance Corporation and the other federal bank regulatory agencies issued a final rule that will revise their leverage and risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision and certain provisions of the Dodd-Frank Act. Among other things, the rule establishes a new common equity Tier 1 minimum capital requirement (4.5% of risk-weighted assets), increases the minimum Tier 1 capital to risk-weighted assets requirement (from 4.0% to 6.0% of risk-weighted assets) and generally assigns a higher risk weight (150%) to exposures that are more than 90 days past due or are on nonaccrual status and to certain commercial real estate facilities that finance the acquisition, development or construction of real property. The final rule also requires unrealized gains and losses on certain “available-for-sale” securities holdings to be included for purposes of calculating regulatory capital unless a one-time opt-out is exercised. Additional constraints will also be imposed on the inclusion in regulatory capital of mortgage-servicing assets, defined tax assets and minority interest. The rule limits a banking organization’s capital distributions and certain discretionary bonus payments if the banking organization does not hold a “capital conservation buffer” consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets in addition to the amount necessary to meet its minimum risk-based capital requirements. The final rule becomes effective for the Bank and the Company on January 1, 2015. The capital conservation buffer requirement will be phased in beginning January 1, 2016 and ending January 1, 2019, when the full capital conservation buffer requirement will be effective.

The capital ratios to be considered “well capitalized” under the new capital rules are: common equity of 6.5%, Tier 1 leverage of 5%, Tier 1 risk-based capital of 8%, and Total Risk-Based capital of 10%.

As of December 31, 2013, management believes that the Bank would remain “well capitalized” under the new rules.

*Federal Deposit Insurance (“FDI”) Act and Part 363 of the FDIC Regulations*

Section 36 of the FDI Act and Part 363 of the FDIC's regulations, as amended, require insured depository institutions with at least \$500 million in total assets to file a Part 363 Annual Report with the applicable bank regulatory agencies, which, among other things, requires that the Company establish and maintain an effective internal control structure over financial reporting and provide an assessment by management of the institution's compliance with the designated laws and regulations pertaining to insider loans and dividend restrictions.

*Bank Holding Company Regulation*

As a bank holding company, the Company is subject to regulation and examination by the Pennsylvania Department of Banking and Securities (the “Pennsylvania Department of Banking”) and the Federal Reserve Board. The Company is required to file with the Federal Reserve Board an annual report and such additional information as the Federal Reserve Board may require pursuant to the Bank Holding Company Act of 1956, as amended (the “BHC Act”). The BHC Act requires each bank holding company to obtain the approval of the Federal Reserve Board before it may acquire substantially all the assets of any bank, or before it may acquire ownership or control of any voting shares of any bank if, after such acquisition, it would own or control, directly or indirectly, more than five percent of the voting shares of such bank. Such a transaction may also require approval of the Pennsylvania Department of Banking. Pennsylvania law permits Pennsylvania bank holding companies to control an unlimited number of banks.

Pursuant to provisions of the BHC Act and regulations promulgated by the Federal Reserve Board thereunder, the Company may only engage in or own companies that engage in activities deemed by the Federal Reserve Board to be so closely related to the business of banking or managing or controlling banks as to be a proper incident thereto, and the holding company must obtain permission from the Federal Reserve Board prior to engaging in most new business activities.

A bank holding company and its subsidiaries are subject to certain restrictions imposed by the BHC Act on any extensions of credit to the bank or any of its subsidiaries, investments in the stock or securities thereof, and on the taking of such stock or securities as collateral for loans to any borrower. A bank holding company and its subsidiaries are also prevented from engaging in certain tie-in arrangements in connection with any extension of credit, lease or sale of property or furnishing of services.

Under the Dodd-Frank Act and Federal Reserve Board regulations, a bank holding company is required to serve as a source of financial and managerial strength to its subsidiary banks and may not conduct its operations in an unsafe or unsound manner. In addition, in serving as a source of strength to its subsidiary banks, a bank holding company should stand ready to use available resources to provide adequate capital funds to its subsidiary banks during periods of financial stress or adversity and should maintain the financial flexibility and capital-raising capacity to obtain additional resources for assisting its subsidiary banks. A bank holding company's failure to meet its obligations to serve as a source of strength to its subsidiary banks will generally be considered by the Federal Reserve Board to be an unsafe and unsound banking practice or a violation of the Federal Reserve Board regulations or both. This doctrine is commonly known as the “source of strength” doctrine.

*Regulation of Embassy Bank for the Lehigh Valley*

Embassy Bank for the Lehigh Valley is a Pennsylvania-chartered banking institution and is subject to regulation, supervision and regular examination by the Pennsylvania Department of Banking and Securities and the Federal Deposit Insurance Corporation (“FDIC”). Federal and state banking laws and regulations govern, among other things, the scope of a bank's business, the investments a bank may make, the reserves against deposits a bank must maintain, the loans a bank makes and collateral it takes, the maximum interest rates a bank may pay on deposits, the activities of a bank with respect to mergers and consolidations, and the establishment of branches, and management practices and other aspects of banking operations.

### *Dividend Restrictions*

The Company is a legal entity separate and distinct from the Bank. Declaration and payment of cash dividends depends upon cash dividend payments to the Company by the Bank, which is the Company's primary source of revenue and cash flow. Accordingly, the right of the Company, and consequently the right of our creditors and shareholders, to participate in any distribution of the assets or earnings of any subsidiary is necessarily subject to the prior claims of creditors of the subsidiary, except to the extent that claims of the Company in its capacity as a creditor may be recognized.

As a Pennsylvania chartered bank, the Bank is subject to regulatory restrictions on the payment and amounts of dividends under the Pennsylvania Banking Code. Further, the ability of banking subsidiaries to pay dividends is also subject to their profitability, financial condition, capital expenditures and other cash flow requirements. See Note 16 to the consolidated financial statements included at Item 8 of this Report.

The payment of dividends by the Bank and the Company may also be affected by other factors, such as the requirement to maintain adequate capital above regulatory guidelines. The federal banking agencies have indicated that paying dividends that deplete a depository institution's capital base to an inadequate level would be an unsafe and unsound banking practice. Under the Federal Deposit Insurance Corporation Improvement Act of 1991, a depository institution may not pay any dividend if payment would cause it to become undercapitalized or if it already is undercapitalized. Moreover, the federal agencies have issued policy statements that provide that bank holding companies and insured banks should generally only pay dividends out of current operating earnings. Federal banking regulators have the authority to prohibit banks and bank holding companies from paying a dividend if the regulators deem such payment to be an unsafe or unsound practice.

### *Capital Adequacy and Operations*

Enacted in 1991, the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") contains provisions limiting activities and business methods of depository institutions. FDICIA required the primary federal banking regulators to promulgate regulations setting forth standards relating to, among other things, internal controls and audit systems; credit underwriting and loan documentation; interest rate exposure and other off-balance sheet assets and liabilities; and compensation of directors and officers. FDICIA also provided for expanded regulation of depository institutions and their affiliates, including parent holding companies, by such institutions' primary federal banking regulator. Each primary federal banking regulator is required to specify, by regulation, capital standards for measuring the capital adequacy of the depository institutions it supervises and, depending upon the extent to which a depository institution does not meet such capital adequacy measures, the primary federal banking regulator may prohibit such institution from paying dividends or may require such institution to take other steps to become adequately capitalized.

FDICIA established five capital tiers, ranging from "well capitalized" to "critically under-capitalized". A depository institution is well capitalized if it significantly exceeds the minimum level required by regulation for each relevant capital measure. Under FDICIA, an institution that is not well capitalized is generally prohibited from accepting brokered deposits and offering interest rates on deposits higher than the prevailing rate in its market; in addition, "pass through" insurance coverage may not be available for certain employee benefit accounts. FDICIA also requires an undercapitalized depository institution to submit an acceptable capital restoration plan to the appropriate federal bank regulatory agency. One requisite element of such a plan is that the institution's parent holding company must guarantee compliance by the institution with the plan, subject to certain limitations. In the event of the parent holding company's bankruptcy, the guarantee, and any other commitments that the parent holding company has made to federal bank regulators to maintain the capital of its depository institution subsidiaries, would be assumed by the bankruptcy trustee and entitled to priority in payment.

At December 31, 2013, the Bank qualified as "well capitalized" under these regulatory capital standards. See Note 16 of the Notes to Consolidated Financial Statements included at Item 8 of this Report.

### *Community Reinvestment Act*

Under the Community Reinvestment Act of 1977 (“CRA”), the FDIC is required to assess the record of all financial institutions regulated by it to determine if these institutions are meeting the credit needs of the community (including low and moderate income neighborhoods) which they serve. CRA performance evaluations are based on a four-tiered rating system: Outstanding, Satisfactory, Needs to Improve and Substantial Noncompliance. CRA performance evaluations are considered in evaluating applications for such things as mergers, acquisitions and applications to open branches. The Bank has a current CRA rating of “Satisfactory.”

### *Restrictions on Transactions with Affiliates and Insiders*

The Bank also is subject to the restrictions of Sections 23A, 23B, 22(g) and 22(h) of the Federal Reserve Act and Regulation O adopted by the Federal Reserve Board. Section 23A requires that loans or extensions of credit to an affiliate, purchases of securities issued by an affiliate, purchases of assets from an affiliate (except as may be exempted by order or regulation), the acceptance of securities issued by an affiliate as collateral and the issuance of a guarantee or acceptance of letters of credit on behalf of an affiliate (collectively, “Covered Transactions”) be on terms and conditions consistent with safe and sound banking practices. Section 23A also imposes quantitative restrictions on the amount of and collateralization requirements on such transactions. Section 23B requires that all Covered Transactions and certain other transactions, including the sale of securities or other assets to an affiliate and the payment of money or the furnishing of services to an affiliate, be on terms comparable to those prevailing for similar transactions with non-affiliates.

Section 22(g) and 22(h) of the Federal Reserve Act impose similar limitations on loans and extensions of credit from the bank to its executive officers, directors and principal shareholders and any of their related interests. The limitations restrict the terms and aggregate amount of such transactions. Regulation O implements the provisions of Sections 22(g) and 22(h) and requires maintenance of records of such transactions by the bank and regular reporting of such transactions by insiders. The FDIC also requires the bank, upon request, to disclose publicly loans and extensions of credit to insiders in excess of certain amounts.

### *Deposit Insurance and Premiums*

The deposits of the Bank are insured up to applicable limits per insured depositor by the FDIC. In October 2008, the FDIC increased FDIC deposit insurance coverage per separately insured depositor for all account types to \$250,000. While initially stipulated to be in effect through December 31, 2009, this increase has been subsequently extended permanently through the Dodd-Frank Act.

As a FDIC member institution, the Bank’s deposits are insured to a maximum of \$250,000 per depositor through the Deposit Insurance Fund (“DIF”) that is administered by the FDIC and each institution is required to pay semi-annual deposit insurance premium assessments to the FDIC.

The Deposit Insurance Funds Act of 1996 recapitalized the Savings Association Insurance Fund (“SAIF”) and provided that DIF deposits would be subject to one-fifth of the assessment to which SAIF deposits are subject for FICO bond payments. Beginning in 2000, DIF deposits and SAIF deposits were subject to the same assessment for FICO bonds. The FICO assessment for the Bank for 2013 was \$0.02 for each \$100 of DIF deposits.

In February 2011, the FDIC adopted final rules to implement changes required by the Dodd-Frank Act with respect to the FDIC assessment rules. In particular, the definition of an institution’s deposit insurance assessment base changed from total deposits to total assets less tangible equity. In addition, the FDIC decreased deposit insurance assessment rates, effective April 1, 2011. The new initial base assessment rates range from 5 to 9 basis points for Risk Category I banks to 35 basis points for risk category IV banks. Risk Category II and III banks will have an initial base assessment rate of 14 or 23 basis points, respectively. The Company expects that the new rates and assessment base will reduce the FDIC insurance assessment rate paid by the Bank. However, if the risk category of the Bank changes adversely, FDIC insurance premiums paid by the Bank could increase.

*Other Federal Laws and Regulations*

State usury and credit laws limit the amount of interest and various other charges collected or contracted by a bank on loans. The Bank's loans are also subject to federal laws applicable to credit transactions, such as the following:

- Federal Truth-In-Lending Act, which governs disclosures of credit terms to consumer borrowers;
- Home Mortgage Disclosure Act, requiring financial institutions to provide information to enable public officials to determine whether a financial institution is fulfilling its obligations to meet the housing needs of the community it serves;
- Equal Credit Opportunity Act prohibiting discrimination on the basis of race, creed or other prohibitive factors in extending credit;
- Real Estate Settlement Procedures Act, which requires lenders to disclose certain information regarding the nature and cost of real estate settlements, and prohibits certain lending practices, as well as limits escrow account amounts in real estate transactions;
- Fair Credit Reporting Act governing the manner in which consumer debts may be collected by collection agencies; and
- Various rules and regulations of various federal agencies charged with the implementation of such federal laws.

Additionally, the Company's operations are subject to additional federal laws and regulations applicable to financial institutions, including, without limitation:

- Privacy provisions of the Gramm-Leach-Bliley Act and related regulations, which require the Company to maintain privacy policies intended to safeguard customer financial information, to disclose the policies to the Company's customers and to allow customers to "opt out" of having their financial service providers disclose their confidential financial information to non-affiliated third parties, subject to certain exceptions;
- Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records;
- Consumer protection rules for the sale of insurance products by depository institutions, adopted pursuant to the requirements of the Gramm-Leach-Bliley Act; and
- USA Patriot Act, which requires financial institutions to take certain actions to help prevent, detect and prosecute international money laundering and the financing of terrorism.

Effective July 1, 2010, a new federal banking rule under the Electronic Fund Transfer Act prohibited financial institutions from charging consumers fees for paying overdrafts on automated teller machines ("ATM") and one-time debit card transactions, unless a consumer consents, or opts in, to the overdraft service for those type of transactions. If a consumer does not opt in, any ATM transaction or debit that overdraws the consumer's account will be denied. Overdrafts on the payment of checks and regular electronic bill payments are not covered by this new rule. Before opting in, the consumer must be provided a notice that explains the financial institution's overdraft services, including the fees associated with the service, and the consumer's choices. Financial institutions must provide consumers who do not opt in with the same account terms, conditions and features (including pricing) that they provide to consumers who do opt in. The Company did not charge customers for these transactions, nor provide these types of services.

*Sarbanes-Oxley Act of 2002*

Enacted in 2002, the Sarbanes-Oxley Act represented a comprehensive revision of laws affecting corporate governance, accounting obligations and corporate reporting. The Sarbanes-Oxley Act is applicable to all companies with equity securities registered or that file reports under the Securities Exchange Act of 1934, including publicly held bank holding companies such as the Company. In particular, the Sarbanes-Oxley Act establishes: (i) requirements for audit committees, including independence, expertise, and responsibilities; (ii) additional responsibilities regarding financial statements for the Chief Executive Officer and Chief Financial Officer of the reporting company; (iii) standards for auditors and regulation of audits; (iv) increased disclosure and reporting obligations for the reporting company and its directors and executive officers; and (v) new and increased civil and criminal penalties for violations of the securities laws.

*Governmental Policies*

The Company's earnings are significantly affected by the monetary and fiscal policies of governmental authorities, including the Federal Reserve Board. Among the instruments of monetary policy used by the Federal Reserve Board to implement these objectives are open-market operations in U.S. Government securities and federal funds, changes in the discount rate on member bank borrowings and changes in reserve requirements against member bank deposits. These instruments of monetary policy are used in varying combinations to influence the overall level of bank loans, investments and deposits, and the interest rates charged on loans and paid for deposits. The Federal Reserve Board frequently uses these instruments of monetary policy, especially its open-market operations and the discount rate, to influence the level of interest rates and to affect the strength of the economy, the level of inflation or the price of the dollar in foreign exchange markets. The monetary policies of the Federal Reserve Board have had a significant effect on the operating results of banking institutions in the past and are expected to continue to do so in the future. It is not possible to predict the nature of future changes in monetary and fiscal policies, or the effect which they may have on the Company's business and earnings.

*Other Legislative Initiatives*

Proposals may be introduced in the United States Congress and in the Pennsylvania Legislature and before various bank regulatory authorities which would alter the powers of, and restrictions on, different types of banking organizations and which would restructure part or all of the existing regulatory framework for banks, bank holding companies and other providers of financial services. Moreover, other bills may be introduced in Congress which would further regulate, deregulate or restructure the financial services industry, including proposals to substantially reform the regulatory framework. It is not possible to predict whether these or any other proposals will be enacted into law or, even if enacted, the effect which they may have on the Company's business and earnings.

**Forward-looking Statements**

This report contains forward-looking statements, including statements of goals, intentions, and expectations as to future trends, plans, events or results of Company operations and policies and regarding general economic conditions. These forward-looking statements are intended to be covered by the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995. These statements are based upon current and anticipated economic conditions, nationally and in the Company's market, interest rates and interest rate policy, competitive factors and other conditions that, by their nature, are not susceptible to accurate forecast, and are subject to significant uncertainty.

Such forward-looking statements can be identified by the use of forward-looking terminology such as "believes", "expects", "may", "intends", "will", "should", "anticipates", or the negative of any of the foregoing or other variations thereon or comparable terminology, or by discussion of strategy.

No assurance can be given that the future results covered by forward-looking statements will be achieved. Such statements are subject to risks, uncertainties, and other factors that could cause actual results to differ materially from future results expressed or implied by such forward-looking statements. Important factors that could impact the Company's operating results include, but are not limited to, (i) the effects of changing economic conditions in the Company's market areas and nationally, (ii) credit risks of commercial, real estate, consumer and other lending activities, (iii) significant changes in interest rates, (iv) changes in federal and state banking laws and regulations which could impact the Company's operations, and (iv) other external developments which could materially affect the Company's business and operations.

**Item 1A. Risk Factors.**

Not required of a smaller reporting company.

**Item 1B. Unresolved Staff Comments.**

None.

**Item 2. PROPERTIES.**

The Company, through the Bank, occupies seven full-service banking offices in the Lehigh Valley:

- Hanover Township, Northampton County (includes administrative offices)
- South Whitehall Township, Lehigh County
- Salisbury Township, Lehigh County
- Lower Macungie Township, Lehigh County
- City of Bethlehem, Lehigh County
- Lower Saucon Township, Northampton County
- Lower Nazareth Township, Northampton County

All properties are leased.

**Item 3. LEGAL PROCEEDINGS.**

The Company and the Bank are an occasional party to legal actions arising in the ordinary course of its business. In the opinion of management, the Company has adequate legal defenses and/or insurance coverage respecting any and each of these actions and does not believe that they will materially affect the Company's operations or financial position.

**Item 4. MINE SAFETY DISCLOSURES.**

Not applicable.

PART II

**Item 5. MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.**

- (a) Shares of Company common stock are traded over-the-counter and in privately negotiated transactions. The Company’s common stock is not listed on any national securities exchange.

Trades in Company common stock made by certain brokerage firms are reported on the OTCQB Market Tier of the OTC Markets under the symbol “EMYB”. The following table reflects high and low bid prices for shares of the Company’s common stock for the periods indicated, based upon information derived from www.otcm Markets.com.

	2013		2012	
	High	Low	High	Low
First	\$ 6.50	\$ 5.44	\$ 7.00	\$ 3.50
Second	\$ 8.99	\$ 6.06	\$ 6.00	\$ 4.50
Third	\$ 7.00	\$ 6.50	\$ 6.00	\$ 4.75
Fourth	\$ 8.00	\$ 6.75	\$ 6.25	\$ 5.10

The above quotations may not reflect inter-dealer prices and should not be considered over-the-counter market quotations as that term is customarily used.

- (b) As of March 25, 2014, there are approximately 1,132 owners of record of the common stock of the Company.
- (c) On September 30, 2013, the Company paid \$363,000, or \$0.05 per share, in an annual cash dividend on its common stock. On October 1, 2012, the Company paid \$288,000, or \$0.04 per share, in an annual cash dividend on its common stock. On July 14, 2011, the Company paid \$215,000 or \$0.03 per share in a special cash dividend on its common stock. As a general matter, cash available for dividend distribution to shareholders of the Company may come from dividends paid to the Company by the Bank, depending upon existing cash levels at the Company.
- (d) The following table sets forth information about options outstanding under the Company’s Stock Option Plan and the Company’s Stock Incentive Plan, as of December 31, 2013:

	Number of Shares to be issued upon exercise of outstanding options	Weighted average exercise price of outstanding options	Number of Shares remaining available for future issuance
Equity Compensation Plans and Individual Employment Agreements	149,692	\$ 8.35	400,891

- (e) Sales of Securities.  
None.
- (f) Repurchase of Equity Securities.  
None.

**Item 6. Selected Financial Data.**

Not required of a smaller reporting company.

## **Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

This discussion and analysis provides an overview of the consolidated financial condition and results of operations of the Company for the years ended December 31, 2013 and 2012. This discussion should be read in conjunction with the consolidated financial statements and notes to consolidated financial statements appearing elsewhere in this report.

### **Critical Accounting Policies**

Note 1 to the Company's financial statements lists significant accounting policies used in the development and presentation of its financial statements. This discussion and analysis, the significant accounting policies, and other financial statement disclosures identify and address key variables and other qualitative and quantitative factors that are necessary for an understanding and evaluation of the Company and its results of operations.

The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require the Company to make estimates and assumptions. The Company believes that its determination of the allowance for loan losses and the valuation of deferred tax assets involve a higher degree of judgment and complexity than the Company's other significant accounting policies. Further, these estimates can be materially impacted by changes in market conditions or the actual or perceived financial condition of the Company's borrowers, subjecting the Company to significant volatility of earnings.

The allowance for loan losses is established through the provision for loan losses, which is a charge against earnings. Provision for loan losses is made to reserve for estimated probable losses on loans. The allowance for loan losses is a significant estimate and is regularly evaluated by the Company for adequacy by taking into consideration factors such as changes in the nature and volume of the loan portfolio, trends in actual and forecasted credit quality, including delinquency, charge-off and bankruptcy rates, and current economic conditions that may affect a borrower's ability to pay. The use of different estimates of assumptions could produce different provision for loan losses. For additional discussion concerning the Company's allowance for loan losses and related matters, see "Provision for Loan Losses" and "Allowance for Loan Losses."

Real estate acquired through foreclosure, or deed-in-lieu of foreclosure is recorded at fair value less estimated selling costs at the date of acquisition or transfer, and subsequently at the lower of its new cost or fair value less estimated selling costs. Adjustments to the carrying value at the date of acquisition or transfer are charged to the allowance for loan losses. The carrying value of the individual properties is subsequently adjusted to the extent it exceeds estimated fair value less the estimated selling costs, at which time a provision for loan losses on such real estate is charged to operations. Appraisals are critical in determining the value of properties. Overly optimistic assumptions or negative changes to assumptions could significantly affect the valuation of a property. The assumptions supporting such appraisals are carefully reviewed by management to determine that the resulting values reasonably reflect amounts realizable.

Deferred taxes are provided on the liability method whereby deferred 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 and net operating loss carryforwards and their tax basis. Deferred tax assets are reduced by a valuations allowance when, in the opinion of management, it is more likely than not that some portion of the deferred tax assets will not be realized. Based upon the level of historical taxable income and projections for future taxable income over periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences.

## **GENERAL**

The Company is a Pennsylvania corporation organized in 2008 and registered as a bank holding company pursuant to the Bank Holding Company Act of 1956, as amended (the “BHC Act”). The Company was formed for purposes of acquiring Embassy Bank For The Lehigh Valley (the “Bank”) in connection with the reorganization of the Bank into a bank holding company structure, which was consummated on November 11, 2008. Accordingly, the Company owns all of the capital stock of the Bank, giving the organization more flexibility in meeting its capital needs as the Company continues to grow.

The Bank, which is the Company’s primary operating subsidiary, was originally incorporated as a Pennsylvania bank on May 11, 2001 and opened its doors on November 6, 2001. It was formed by a group of local business persons and professionals with significant prior experience in community banking in the Lehigh Valley area of Pennsylvania, the Bank’s primary market area.

## **OVERVIEW**

The Company’s assets grew \$27.8 million from \$643.0 million at December 31, 2012 to \$670.8 million at December 31, 2013. The Company’s deposits grew \$16.0 million from \$553.0 million at December 31, 2012 to \$569.0 million at December 31, 2013. During the same period, loans receivable, net of the allowance for loan losses, increased \$63.2 million to \$563.3 million at December 31, 2013 from \$500.1 million at December 31, 2012. The market is very competitive and the Company is committed to maintaining a high quality portfolio that returns a reasonable market rate. The Company expects increased lending activity, as the Company expands its presence in the market and continues to become more widely known. The past and current economic conditions have created lower demand for loans by credit-worthy customers. The lending staff has been active in contacting new prospects and promoting the Company’s name in the community. Management believes that this will translate into continued growth of a portfolio of quality loans, although there can be no assurance of this.

The Company reported net income of \$5.5 million for the year ended December 31, 2013 as compared to net income of \$5.7 million for the year ended December 31, 2012, a decrease of \$220 thousand, or 3.9%. Diluted earnings per share decreased to \$0.76 in 2013 from \$0.80 in 2012.

## **RESULTS OF OPERATIONS**

### **Net Interest Income and Net Interest Margin**

Net interest income is the difference between income on assets and the cost of funds supporting those assets. Earning assets are composed primarily of loans and investments. Interest-bearing deposits and borrowings make up the cost of funds. Non-interest bearing deposits and capital are other components representing funding sources. Changes in the volume and mix of assets and funding sources, along with the changes in yields earned and rates paid, determine changes in net interest income.

### **2013 Compared to 2012**

Total interest income for the year ended December 31, 2013 was \$24.7 million, compared to \$24.5 for the year ended December 31, 2012. Total interest expense for the year ended December 31, 2013 was \$2.9 million, compared to \$4.1 million for the year ended December 31, 2012. The increase in interest income is due to the growth in loan balances, offset by lower yields in this interest rate environment. The decrease in interest expense is due to the lower interest rate environment, as well as a shift in deposits from certificates of deposit to savings accounts. Net interest income increased 6.4% to \$21.7 million for the year ended December 31, 2013 as compared to \$20.4 million for the year ended December 31, 2012.

Generally, changes in net interest income are measured by net interest rate spread and net interest margin. Interest rate spread is the mathematical difference between the average interest earned on earning assets and interest paid on interest bearing liabilities. Interest margin represents the net interest yield on earning assets and is derived by dividing

net interest income by average earning assets. In a mature financial institution the interest margin gives a reader a better indication of asset earning results when compared to peer groups or industry standards.

The Company's net interest margin for the year ended December 31, 2013 was 3.57% compared to 3.47% for the year ended December 31, 2012. The increase in the margin is due primarily to the reduced loan, deposit and investment yields associated with current market conditions, coupled with the significant growth in the loan and interest bearing deposit balances. During this difficult market environment, the Company continued to grow and attract deposits and loans at competitive rates.

The following table includes the average balances, interest income and expense and the average rates earned and paid for assets and liabilities for the periods presented. All average balances are daily average balances.

**Average Balances, Rates and Interest Income and Expense**

	<u>Year Ended December 31, 2013</u>			<u>Year Ended December 31, 2012</u>			<u>Year Ended December 31, 2011</u>		
	Average		Tax	Average		Tax	Average		Tax
	Balance	Interest	Equivalent Yield	Balance	Interest	Equivalent Yield	Balance	Interest	Equivalent Yield
(Dollars in Thousands)									
<b>ASSETS</b>									
Loans - taxable (2)	\$ 530,174	\$ 22,471	4.24%	\$ 457,772	\$ 21,602	4.72%	\$ 394,650	\$ 20,734	5.25%
Loans - non-taxable (1)	3,848	146	5.75%	3,828	149	5.90%	3,234	127	5.95%
Investment securities - taxable (3)	50,364	832	1.65%	59,538	1,214	2.04%	61,332	1,609	2.62%
Investment securities - non-taxable (1) (3)	33,357	1,168	5.30%	38,587	1,344	5.17%	29,741	1,091	5.46%
Federal funds sold	792	2	0.20%	1,337	2	0.15%	3,178	3	0.09%
Time deposits	3,487	34	0.98%	7,045	94	1.33%	7,643	116	1.52%
Interest bearing deposits with banks	5,463	12	0.22%	40,926	93	0.23%	16,133	36	0.22%
<b>TOTAL INTEREST EARNING ASSETS</b>	<b>627,485</b>	<b>24,665</b>	<b>4.04%</b>	<b>609,033</b>	<b>24,498</b>	<b>4.15%</b>	<b>515,911</b>	<b>23,716</b>	<b>4.70%</b>
Less allowance for loan losses	(5,140)			(4,605)			(3,932)		
Other assets	28,496			23,751			21,076		
<b>TOTAL ASSETS</b>	<b>\$ 650,841</b>			<b>\$ 628,179</b>			<b>\$ 533,055</b>		
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>									
Interest bearing demand deposits, NOW and money market	\$ 57,651	\$ 38	0.07%	\$ 54,221	\$ 66	0.12%	\$ 39,006	\$ 79	0.20%
Savings	384,407	1,816	0.47%	370,420	2,467	0.67%	279,342	2,619	0.94%
Certificates of deposit	56,787	563	0.99%	64,848	812	1.25%	85,124	1,383	1.62%
Securities sold under agreements to repurchase and other borrowings	43,341	523	1.21%	44,594	762	1.71%	51,576	913	1.77%
<b>TOTAL INTEREST BEARING LIABILITIES</b>	<b>542,186</b>	<b>2,940</b>	<b>0.54%</b>	<b>534,083</b>	<b>4,107</b>	<b>0.77%</b>	<b>455,048</b>	<b>4,994</b>	<b>1.10%</b>
Non-interest bearing demand deposits	50,527			42,756			34,169		
Other liabilities	3,693			6,844			5,145		
Stockholders' equity	54,435			44,496			38,693		
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 650,841</b>			<b>\$ 628,179</b>			<b>\$ 533,055</b>		
Net interest income		\$ 21,725			\$ 20,391			\$ 18,722	
Net interest spread			3.50%			3.38%			3.60%
Net interest margin			3.57%			3.47%			3.73%

(1) Yields on tax exempt assets have been calculated on a fully tax equivalent basis.

(2) The average balance of taxable loans includes loans in which interest is no longer accruing.

(3) Investment security yields do not give effect to changes in fair value.

The table below demonstrates the relative impact on net interest income of changes in the volume of interest-earning assets and interest-bearing liabilities and changes in rates earned and paid by the Company on such assets and liabilities.

	2013 vs. 2012			2012 vs. 2011		
	Increase (decrease) due to changes in:			Increase (decrease) due to changes in:		
	Volume	Rate	Total	Volume	Rate	Total
(In Thousands)						
<b>Interest-earning assets:</b>						
Loans - taxable	\$ 3,417	\$ (2,548)	\$ 869	\$ 3,316	\$ (2,448)	\$ 868
Loans - non-taxable	1	(4)	(3)	23	(1)	22
Investment securities - taxable	(187)	(195)	(382)	(47)	(348)	(395)
Investment securities - non-taxable	(182)	6	(176)	319	(71)	253
Federal funds sold	(1)	-	-	(2)	1	(1)
Time deposits	(47)	(13)	(60)	(9)	(13)	(22)
Interest bearing deposits with banks	(81)	-	(81)	55	2	57
Total net change in income on interest-earning assets	<b>2,920</b>	<b>(2,754)</b>	<b>167</b>	3,655	(2,878)	782
<b>Interest-bearing liabilities:</b>						
Interest bearing demand deposits	4	(32)	(28)	31	(44)	(13)
Savings	93	(744)	(651)	854	(1,006)	(152)
Certificates of deposit	(101)	(148)	(249)	(329)	(242)	(571)
Total deposits	(4)	(924)	(928)	556	(1,292)	(736)
Securities sold under agreements to repurchase and other borrowings	(21)	(218)	(239)	(124)	(27)	(151)
Total net change in expense on interest-bearing liabilities	<b>(25)</b>	<b>(1,142)</b>	<b>(1,167)</b>	432	(1,319)	(887)
Change in net interest income	<b>\$ 2,945</b>	<b>\$ (1,612)</b>	<b>\$ 1,334</b>	<b>\$ 3,223</b>	<b>\$ (1,559)</b>	<b>\$ 1,669</b>

**Provision for Loan Losses**

The provision for loan losses represents the expense recognized to fund the allowance for loan losses. This amount is based on many factors that reflect management's assessment of the risk in its loan portfolio. Those factors include economic conditions and trends, the value and adequacy of collateral, volume and mix of the portfolio, performance of the portfolio, and internal loan processes of the Company.

For the year ended December 31, 2013, the provision for loan losses was \$992 thousand, compared to \$1.2 million for the year ended December 31, 2012. The decrease in the provision for loan losses was primarily due to the volume of loan growth in 2013 over 2012. Loans grew \$63.2 million in 2013 compared to \$82.3 million in 2012. The allowance for loan losses as of December 31, 2013 was \$5.3 million, which represents 0.94% of outstanding loans, which is comparable to the \$5.1 million as of December 31, 2012, representing 1.02% of outstanding loans. Based principally on current economic conditions, perceived asset quality, loan-loss experience of comparable institutions in the Company's market area, the allowance is believed to be adequate.

## **Non-interest Income**

Non-interest income is derived from the Company's operations and represents primarily credit card processing fees, service fees on deposit and loan relationships and income from bank owned life insurance. Non-interest income also may include net gains and losses from the sale of available for sale securities. Total non-interest income was \$2.3 million for the year ended December 31, 2013 compared to \$2.5 million for the year ended December 31, 2012. This decrease in non-interest income is due to the gain from sales of securities in 2012 of \$1.2 million, compared to \$337 thousand in 2013. In 2013, the Company derived increased service fees in the amount of \$104 thousand, or 21.8%, over 2012 due to the increase in the number of deposit accounts. There was also an increase in fees from merchant credit card processing services in the amount of \$203 thousand, or 17.7%, over 2012. As the deposit customer account base grows and the Company continues to mature and develop additional sources of fee income, non-interest income is expected to become a more significant contributor to the overall profitability of the Company.

## **Non-interest Expense**

Non-interest expenses represent the normal operating expenses of the Company. These expenses include salaries, employee benefits, occupancy, equipment, data processing, advertising and other expenses related to the overall operation of the Company.

Non-interest expenses for the year ended December 31, 2013 were \$15.4 million, compared to \$13.7 million for the year ended December 31, 2012. At December 31, 2013, the Company had seventy-one full-time equivalent employees compared to seventy full-time equivalent employees at December 31, 2012. Credit card processing costs increased \$184 thousand, or 18%, due to increased volume of accounts. Charitable contributions increased \$158 thousand, or 42%, due to an increase in contributions related to the Pennsylvania Earned Income Tax Credit (EITC) program, which was offset by a decrease in the Pennsylvania bank shares tax expenses. Salaries and employee benefits increased \$977 thousand, or 17%, due to the increased benefits in addition to salary adjustments and the hiring of additional employees. Advertising and promotion expenses increased \$93 thousand, or 11%, due to enhanced advertising initiatives. Loan and real estate expenses increased \$41 thousand, or 19%, due to the increase in loan volume. Other expenses increased \$95 thousand, or 12%, due to increased operating expenses associated with higher customer volume. Other real estate owned expenses decreased \$42 thousand, or 36%, due to the reduction of costs related to bank-owned properties that were sold in 2013.

A breakdown of other non-interest expenses is included in the Consolidated Statements of Income in the Consolidated Financial Statements included in Item 8 of this Report.

## **Income Taxes**

The provision for income taxes was \$2.1 million at December 31, 2013 compared to \$2.2 million at December 31, 2012. The effective rate on income taxes for the years ended December 31, 2013 and 2012 was consistently 27.9%.

## **FINANCIAL CONDITION**

### **Securities**

The Company's securities portfolio is classified, in its entirety, as "available for sale." Management believes that a portfolio classification of available for sale allows complete flexibility in the investment portfolio. Using this classification, the Company intends to hold these securities for an indefinite amount of time, but not necessarily to maturity. Such securities are carried at fair value with unrealized gains or losses reported as a separate component of stockholders' equity. The portfolio is structured to provide maximum return on investments while providing a consistent source of liquidity and meeting strict risk standards. The Company holds no high-risk securities or derivatives as of December 31, 2013.

The Company's securities portfolio was \$71.3 million at December 31, 2013, a \$20.6 million decrease from securities of \$91.9 million at December 31, 2012. The Company's securities have decreased primarily due to a combination of investment principal pay-downs, maturities and sales totaling \$5.4 million, offset by purchases in the amount of \$11.4 million and a \$2.6 million decrease in unrealized gains. The carrying value of the securities portfolio as of December 31, 2013 includes a net unrealized gain of \$818 thousand, as compared to a net unrealized gain of \$3.5 million as of December 31, 2012, which is recorded to accumulated other comprehensive income in stockholders' equity. This decrease in the unrealized gain is due primarily to the changes in market conditions from 2012 to 2013. No securities are deemed to be other than temporarily impaired.

The following table sets forth the composition of the securities portfolio at fair value as of December 31, 2013, 2012 and 2011.

	<u>2013</u>	<u>2012</u>	<u>2011</u>
	(In Thousands)		
U.S. Government agency obligations	\$ 27,005	\$ 40,605	\$ 33,689
Municipal securities	32,900	38,952	40,048
U.S. Government sponsored enterprise (GSE)			
- Mortgage-backed securities - residential	9,362	9,017	13,841
Corporate bonds	2,021	3,283	4,532
Total Securities Available for Sale	<u>\$ 71,288</u>	<u>\$ 91,857</u>	<u>\$ 92,110</u>

The following table presents the maturities and average weighted yields of the debt securities portfolio as of December 31, 2013. Maturities of mortgage-backed securities are based on estimated life. Yields are based on amortized cost.

**Securities by Maturities**

	<u>1 year or Less</u>		<u>1-5 Years</u>		<u>5-10 Years</u>		<u>Over 10 Years</u>		<u>Total</u>	
	Average		Average		Average		Average		Average	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
(Dollars In Thousands)										
U.S. Government agency obligations	\$ 3,019	0.95%	\$ 22,041	1.05%	\$ 1,945	1.33%	\$ -	-	\$ 27,005	1.06%
Municipal securities	506	4.87%	5,233	3.37%	14,173	4.90%	12,988	6.35%	32,900	5.23%
U.S. GSE - Mortgage-backed securities- residential	607	4.86%	8,034	4.23%	721	6.02%	-	-	9,362	3.26%
Corporate bonds	-	-	2,021	2.20%	-	-	-	-	2,021	2.20%
Total Debt Securities	<u>\$ 4,132</u>	<u>2.00%</u>	<u>\$ 37,329</u>	<u>1.83%</u>	<u>\$ 16,839</u>	<u>4.04%</u>	<u>\$ 12,988</u>	<u>6.15%</u>	<u>\$ 71,288</u>	<u>3.30%</u>

**Loans**

The following table sets forth information on the composition of the loan portfolio by type at December 31, 2013, 2012, 2011, 2010 and 2009. All of the Company's loans are to domestic borrowers.

	<b>December 31, 2013</b>		<b>December 31, 2012</b>		<b>December 31, 2011</b>	
	<b>Balance</b>	<b>Percentage of total Loans</b>	<b>Balance</b>	<b>Percentage of total Loans</b>	<b>Balance</b>	<b>Percentage of total Loans</b>
(Dollars in Thousands)						
Commercial real estate	\$ 235,545	41.40%	\$ 204,904	40.53%	\$ 171,792	40.56%
Commercial construction	21,109	3.71%	19,717	3.90%	13,414	3.17%
Commercial	28,017	4.92%	28,696	5.68%	26,879	6.35%
Residential real estate	283,421	49.82%	250,854	49.62%	210,361	49.65%
Consumer	846	0.15%	1,382	0.27%	1,140	0.27%
Gross loans	568,938	100.00%	505,553	100.00%	423,586	100.00%
Unearned origination (fees) costs	(355)		(334)		(245)	
	<b>\$ 568,583</b>		<b>\$ 505,219</b>		<b>\$ 423,341</b>	
	<b>December 31, 2010</b>		<b>December 31, 2009</b>			
	<b>Balance</b>	<b>Percentage of total Loans</b>	<b>Balance</b>	<b>Percentage of total Loans</b>		
(Dollars in Thousands)						
Commercial real estate	\$ 166,780	42.95%	\$ 150,439	43.00%		
Commercial construction	15,701	4.04%	12,292	3.51%		
Commercial	27,591	7.11%	25,796	7.37%		
Residential real estate	176,141	45.37%	159,180	45.50%		
Consumer	2,048	0.53%	2,160	0.62%		
Gross loans	388,261	100.00%	349,867	100.00%		
Unearned origination (fees) costs	(96)		51			
	<b>\$ 388,165</b>		<b>\$ 349,918</b>			

The following table shows the maturities of the commercial loan portfolio and the sensitivity of such loans to interest rate fluctuations at December 31, 2013.

	One year or Less	After One Year Through Five Years	After Five Years	Total
	(In Thousands)			
Commercial real estate	\$ 37,295	\$ 142,438	\$ 55,812	\$ 235,545
Commercial construction	12,405	8,689	15	21,109
Commercial	15,157	10,828	2,032	28,017
	<u>\$ 64,857</u>	<u>\$ 161,955</u>	<u>\$ 57,859</u>	<u>\$ 284,671</u>
Fixed Rates	\$ 24,430	\$ 149,604	\$ 57,232	\$ 231,266
Variable Rates	40,427	12,351	627	53,405
	<u>\$ 64,857</u>	<u>\$ 161,955</u>	<u>\$ 57,859</u>	<u>\$ 284,671</u>

### **Credit Risk and Loan Quality**

The allowance for loan losses increased \$179 thousand to \$5.3 million at December 31, 2013 from \$5.1 million at December 31, 2012. At December 31, 2013 and December 31, 2012, the allowance for loan losses represented 0.94% and 1.02%, respectively, of total loans. Based upon current economic conditions, the composition of the loan portfolio, the perceived credit risk in the portfolio and loan-loss experience of comparable institutions in the Bank's market area, management feels the allowance is adequate to absorb reasonably anticipated losses.

At December 31, 2013, aggregate balances on non-performing loans equaled \$10.4 million compared to \$10.6 million at December 31, 2012, representing 1.83% and 2.11% of total loans at December 31, 2013 and December 31, 2012, respectively. In certain circumstances in which the Company has deemed it prudent for reasons related to a borrower's financial condition, the Company has agreed to restructure certain loans (referred to as troubled debt restructurings). Troubled debt restructurings are considered non-performing loans. Generally, a loan is classified as nonaccrual when it is determined that the collection of all or a portion of interest or principal is doubtful or when a default of interest or principal has existed for 90 days or more, unless the loan is well secured and in the process of collection. A non-performing loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured.

As of December 31, 2013 the Company had four foreclosed assets, one in the amount of \$532 thousand acquired in October 2010, and three acquired from one borrower in November 2013 in the amounts of \$22 thousand, \$36 thousand and \$70 thousand. Subsequent to December 31, 2013, the Company sold two properties acquired in November 2013. The details for the non-performing loans and assets are included in the following table:

	<b>December 31,</b>				
	<b>2013</b>	<b>2012</b>	<b>2011</b>	<b>2010</b>	<b>2009</b>
	(Dollars In Thousands)				
Non-accrual - commercial	\$ 1,824	\$ 2,143	\$ 1,869	\$ 1,140	\$ 4,152
Non-accrual - consumer	481	301	-	381	-
Restructured, accruing interest	7,354	7,841	7,264	3,345	-
Loans past due 90 or more days, accruing interest	763	361	265	1,464	584
<b>Total nonperforming loans</b>	<b>10,422</b>	<b>10,646</b>	<b>9,398</b>	<b>6,330</b>	<b>4,736</b>
Foreclosed assets	659	3,038	3,388	3,069	-
<b>Total nonperforming assets</b>	<b>\$ 11,081</b>	<b>\$ 13,684</b>	<b>\$ 12,786</b>	<b>\$ 9,399</b>	<b>\$ 4,736</b>
Nonperforming loans to total loans	<b>1.83%</b>	2.11%	2.22%	1.63%	1.35%
Nonperforming assets to total assets	<b>1.65%</b>	2.13%	2.23%	1.83%	1.02%

**Allowance for Loan Losses**

Based upon current economic conditions, the composition of the loan portfolio and loan loss experience of comparable institutions in the Company's market areas, an allowance for loan losses has been provided at 0.94% of outstanding loans. Based on its knowledge of the portfolio and current economic conditions, management believes that, as of December 31, 2013, the allowance is adequate to absorb reasonably anticipated losses. As of December 31, 2013, the Company had \$12.0 million of impaired loans compared to \$12.7 million at December 31, 2012. Most of the Company's impaired loans required no specific reserves due to adequate collateral. As of December 31, 2013, the Company had impaired loans of \$2.0 million requiring a specific reserve of \$405 thousand. As of December 31, 2012, the Company had impaired loans of \$3.9 thousand requiring a specific reserve of \$750 thousand.

The activity in the allowance for loan losses is shown in the following table, as well as period end loans receivable and the allowance for loan losses as a percent of the total loan portfolio:

	<b>December 31,</b>				
	<b>2013</b>	<b>2012</b>	<b>2011</b>	<b>2010</b>	<b>2009</b>
	(Dollars In Thousands)				
Loans receivable at end of year	<b>\$ 568,583</b>	<b>\$ 505,219</b>	<b>\$ 423,341</b>	<b>\$ 388,165</b>	<b>\$ 349,918</b>
Allowance for loan losses:					
Balance, beginning	<b>\$ 5,147</b>	<b>\$ 4,215</b>	<b>\$ 3,709</b>	<b>\$ 3,598</b>	<b>\$ 2,932</b>
Provision for loan losses	<b>992</b>	<b>1,183</b>	<b>734</b>	<b>1,318</b>	<b>702</b>
Loans charged off:					
Commercial real estate	<b>(530)</b>	<b>(231)</b>	<b>(137)</b>	<b>(645)</b>	<b>(26)</b>
Commercial construction	<b>(197)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Commercial	<b>(13)</b>	<b>-</b>	<b>(50)</b>	<b>(474)</b>	<b>(10)</b>
Residential real estate	<b>(112)</b>	<b>(39)</b>	<b>(63)</b>	<b>(125)</b>	<b>-</b>
Consumer	<b>(5)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Total charged offs	<b>(857)</b>	<b>(270)</b>	<b>(250)</b>	<b>(1,244)</b>	<b>(36)</b>
Recoveries of loans previously charged-off:					
Commercial real estate	<b>13</b>	<b>1</b>	<b>2</b>	<b>28</b>	<b>-</b>
Commercial construction	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Commercial	<b>3</b>	<b>-</b>	<b>4</b>	<b>9</b>	<b>-</b>
Residential real estate	<b>28</b>	<b>18</b>	<b>4</b>	<b>-</b>	<b>-</b>
Consumer	<b>-</b>	<b>-</b>	<b>12</b>	<b>-</b>	<b>-</b>
Total recoveries	<b>44</b>	<b>19</b>	<b>22</b>	<b>37</b>	<b>-</b>
Net charged offs	<b>(813)</b>	<b>(251)</b>	<b>(228)</b>	<b>(1,207)</b>	<b>(36)</b>
Balance at end of year	<b>\$ 5,326</b>	<b>\$ 5,147</b>	<b>\$ 4,215</b>	<b>\$ 3,709</b>	<b>\$ 3,598</b>
Allowance for loan losses to loans receivable at end of year	<b>0.94%</b>	<b>1.02%</b>	<b>1.00%</b>	<b>0.96%</b>	<b>1.03%</b>

### Allocation of the Allowance for Loan Losses

The following table details the allocation of the allowance for loan losses to various loan categories. While allocations have been established for particular loan categories, management considers the entire allowance to be available to absorb losses in any category.

	December 2013	% of Total Loans	December 2012	% of Total Loans	December 2011	% of Total Loans	December 2010	% of Total Loans	December 2009	% of Total Loans
(Dollars in Thousands)										
Commercial real estate	\$ 1,791	41.40%	\$ 2,007	40.53%	\$ 1,264	40.56%	\$ 1,014	42.95%	\$ 1,654	43.00%
Commercial construction	495	3.71%	660	3.90%	352	3.17%	443	4.04%	207	3.51%
Commercial	349	4.92%	394	6.71%	423	6.35%	325	7.11%	679	7.37%
Residential real estate	2,068	49.82%	1,677	48.59%	1,691	49.65%	1,309	45.37%	1,005	45.50%
Consumer	24	0.15%	33	0.27%	40	0.27%	35	0.53%	53	0.62%
Unallocated	599		376		445		583		-	
Total Allowance for Loan Losses	<u>\$ 5,326</u>	<u>100.00%</u>	<u>\$ 5,147</u>	<u>100.00%</u>	<u>\$ 4,215</u>	<u>100.00%</u>	<u>\$ 3,709</u>	<u>100.00%</u>	<u>\$ 3,598</u>	<u>100.00%</u>

### Deposits

As growth continues, the Company expects that the principal sources of its funds will be deposits, consisting of demand deposits, NOW accounts, money market accounts, savings accounts, and certificates of deposit from the local market areas surrounding the Company's offices. These accounts provide the Company with a source of fee income and a relatively stable source of funds.

Total deposits at December 31, 2013 were \$569.0 million, an increase of \$16 million, or 2.9%, over total deposits of \$553.0 million as of December 31, 2012. The following table reflects the Company's deposits by category for the periods indicated. All deposits are domestic deposits.

	December 31, 2013	December 31, 2012	December 31, 2011
(In Thousands)			
Demand, non-interest bearing	\$ 58,705	\$ 51,741	\$ 38,386
Demand, NOW and money market, interest bearing	59,451	61,638	40,128
Savings	389,613	381,012	327,048
Time, \$100 and over	26,488	23,409	32,784
Time, other	34,780	35,220	43,429
Total deposits	<u>\$ 569,037</u>	<u>\$ 553,020</u>	<u>\$ 481,775</u>

The following table sets forth the average balance of the Company's deposits and the average rates paid on those deposits for the years ended December 31, 2013, 2012 and 2011:

	<b>December 31, 2013</b>		<b>December 31, 2012</b>		<b>December 31, 2011</b>	
	<b>Average Amount</b>	<b>Average Rate</b>	<b>Average Amount</b>	<b>Average Rate</b>	<b>Average Amount</b>	<b>Average Rate</b>
(Dollars In Thousands)						
Demand, NOW and money market, interest bearing	\$ 57,651	0.07%	\$ 54,221	0.12%	\$ 39,006	0.20%
Savings	384,407	0.47%	370,420	0.67%	279,342	0.94%
Certificates of deposit	56,787	0.99%	64,848	1.25%	85,124	1.62%
Total interest bearing deposits	498,845	0.48%	489,489	0.69%	403,472	1.01%
Non-interest bearing demand deposits	50,527		42,756		34,169	
Total	\$ 549,372		\$ 532,245		\$ 437,641	

The following table displays the maturities and the amounts of the Company's certificates of deposit of \$100,000 or more as of December 31, 2013:

	<b>December 31, 2013</b>
	(In Thousands)
3 months or less	\$ 3,347
Over 3 through 6 months	5,505
Over 6 through 12 months	7,086
Over 12 months	10,550
Total	\$ 26,488

As a FDIC member institution, the Company's deposits are insured to a maximum of \$250,000 per depositor through the Deposit Insurance Fund ("DIF") that is administered by the FDIC and each institution is required to pay semi-annual deposit insurance premium assessments to the FDIC.

## Liquidity

Liquidity is a measure of the Company's ability to meet the demands required for the funding of loans and to meet depositors' requirements for use of their funds. The Company's sources of liquidity are cash balances, due from banks, Federal funds sold and short-term securities. There are other sources of liquidity that are available to the Company.

The Bank has borrowing capacity with the FHLB of Pittsburgh of approximately \$321.1 million, of which \$10 million was outstanding at December 31, 2013, all of which is short term. This borrowing capacity with the FHLB includes a line of credit of \$25.0 million. The Bank also has a \$6.0 million line of credit with Atlantic Central Bankers Bank, of which none was outstanding at December 31, 2013. Advances from the Federal Home Loan Bank line are secured by qualifying assets of the Bank and advances from the Atlantic Central Bankers Bank line are unsecured. The Company

has two lines of credit with Univest Bank and Trust Co., totaling \$10.0 million, of which \$3.9 million was outstanding at December 31, 2013. These lines of credit are secured by 833,333 shares of Bank stock.

Because of the composition of the Company's balance sheet, its strong capital base, deposit growth, and borrowing capacity, the Company believes that it remains well positioned with respect to liquidity. While it is desirable to be liquid, it has the effect of a lower interest margin. The majority of funds are invested in loans; however, a sizeable portion is invested in investment securities that generally carry a lower yield.

### Contractual Obligations

The following table represents the Company's contractual obligations to make future payments as of the year ended December 31, 2013:

	2014	2015-2016	2017-2018	Thereafter	Total
	(In Thousands)				
Time deposits	\$ 36,598	\$ 20,607	\$ 4,063	\$ -	\$ 61,268
Short-term borrowings	10,000	-	-	-	10,000
Long-term borrowings	-	3,900	-	-	3,900
Operating Leases	1,166	2,386	1,725	734	6,011
Total	<u>\$ 47,764</u>	<u>\$ 26,893</u>	<u>\$ 5,788</u>	<u>\$ 734</u>	<u>\$ 81,179</u>

### Off-Balance Sheet Arrangements

The Company's financial statements do not reflect various off-balance sheet arrangements that are made in the normal course of business, which may involve some liquidity risk. These commitments consist of unfunded loans and lines of credit and letters of credit made under the same standards as on-balance sheet instruments. These off-balance sheet arrangements at December 31, 2013 totaled \$84.9 million. Because these instruments have fixed maturity dates, and because many of them will expire without being drawn upon, they do not generally present any significant liquidity risk to the Company.

Management believes that any amounts actually drawn upon can be funded in the normal course of operations.

The Company has no investment in or financial relationship with any unconsolidated entities that are reasonably likely to have a material effect on liquidity or the availability of capital resources.

**Capital Resources and Adequacy**

The Company and the Bank are subject to various regulatory capital requirements administered by banking regulators. Failure to meet minimum capital requirements can initiate certain actions by regulators that could have a material effect on the consolidated financial statements.

The regulations require that banks maintain minimum amounts and ratios of total and Tier 1 capital (as defined in the regulations) to risk weighted assets (as defined), and Tier 1 capital to average assets (as defined). As of December 31, 2013, the Bank met the minimum requirements. In addition, the Bank’s capital ratios exceeded the amounts required to be considered “well capitalized” as defined in the regulations.

The following table provides a comparison of the Bank’s risk-based capital ratios and leverage ratios:

	<b>December 31, 2013</b>	<b>December 31, 2012</b>
	(Dollars In Thousands)	
Tier 1, common stockholders' equity	\$ 56,820	\$ 52,046
Tier 2, allowable portion of allowance for loan losses	5,326	5,147
Total capital	<b>\$ 62,146</b>	<b>\$ 57,193</b>
Tier 1 risk based capital ratio	<b>12.0%</b>	12.1%
Total risk based capital ratio	<b>13.2%</b>	13.3%
Tier 1 leverage ratio	<b>8.5%</b>	8.0%

Note: Unrealized gains on securities available for sale are excluded from regulatory capital components of risk-based capital and leverage ratios.

The Federal banking regulators have adopted risk-based capital guidelines for bank holding companies. Currently, the required minimum ratio of total capital to risk-weighted assets (including off-balance sheet activities, such as standby letters of credit) is 8% (10% in order to be considered “well-capitalized”). At least 4% of the total capital (6% to be well-capitalized) is required to be Tier 1 capital, consisting principally of common shareholders’ equity, related surplus, retained earnings, qualifying perpetual preferred stock, and minority interests in the equity accounts of consolidated subsidiaries, less goodwill and certain other intangibles. The remainder (Tier 2 capital) may consist of a limited amount of subordinated debt, certain hybrid capital instruments and other debt securities, qualifying preferred stock and a limited amount of the general loan loss allowance.

In addition to the risk-based capital guidelines, the federal banking regulators established minimum leverage ratio (Tier 1 capital to total assets) guidelines for bank holding companies. These guidelines provide for a minimum leverage ratio of 3% for those bank holding companies which have the highest regulatory examination ratings and are not contemplating or experiencing significant growth or expansion. All other bank holding companies are required to maintain a leverage ratio of at least 4%.

The following table provides the Company's risk-based capital ratios and leverage ratios:

	<u>December 31, 2013</u>	<u>December 31, 2012</u>
	(Dollars In Thousands)	
Tier 1, common stockholders' equity	\$ 53,515	\$ 47,745
Tier 2, allowable portion of allowance for loan losses	<u>5,326</u>	<u>5,147</u>
Total capital	<u>\$ 58,841</u>	<u>\$ 52,892</u>
Tier 1 risk based capital ratio	<b>11.3%</b>	11.1%
Total risk based capital ratio	<b>12.5%</b>	12.3%
Tier 1 leverage ratio	<b>7.9%</b>	7.3%

### **Interest Rate Risk Management**

A principal objective of the Company's asset/liability management policy is to minimize the Company's exposure to changes in interest rates by an ongoing review of the maturity and repricing of interest-earning assets and interest-bearing liabilities. The Asset Liability Committee (ALCO Committee), which meets as part of the Board of Directors meeting, oversees this review, which establishes policies to control interest rate sensitivity. Interest rate sensitivity is the volatility of a company's earnings resulting from a movement in market interest rates. The Company monitors rate sensitivity in order to reduce vulnerability to interest rate fluctuations while maintaining adequate capital levels and acceptable levels of liquidity. The Company's asset/liability management policy, along with monthly financial reports, supplies management with guidelines to evaluate and manage rate sensitivity.

GAP, a measure of the difference in volume between interest bearing assets and interest bearing liabilities, is a means of monitoring the sensitivity of a financial institution to changes in interest rates. The chart below provides an indicator of the rate sensitivity of the Company. NOW and savings accounts are categorized by their respective estimated decay rates. The Company is liability sensitive, which means that if interest rates fall, interest income will fall slower than interest expense and net interest income will likely increase. If interest rates rise, interest income will rise slower than interest expense and net interest income will likely decrease.

	0-3 Months	4-12 Months	1-3 Years	4-5 Years	Over 5 Years	Total
(In Thousands)						
<b>Interest-earning assets</b>						
Federal funds sold and interest-bearing deposits	\$ 4,182	\$ 1,073	\$ 250	\$ -	\$ -	\$ 5,505
Investment securities	4,712	4,978	18,989	16,940	27,826	73,445
Loans, gross	109,669	99,020	167,994	85,445	106,455	568,583
<b>Total interest-earning assets</b>	<b>118,563</b>	<b>105,071</b>	<b>187,233</b>	<b>102,385</b>	<b>134,281</b>	<b>647,533</b>
<b>Interest-bearing liabilities</b>						
NOW and money market accounts	59,451	-	-	-	-	59,451
Savings	361,629	27,985	-	-	-	389,614
Certificates of deposit	8,180	28,601	20,423	4,063	-	61,267
Other borrowed funds	10,000	-	3,900	-	-	13,900
Repurchase agreements and federal funds purchased	30,418	-	-	-	-	30,418
<b>Total interest-bearing liabilities</b>	<b>469,678</b>	<b>56,586</b>	<b>24,323</b>	<b>4,063</b>	<b>-</b>	<b>554,650</b>
<b>GAP</b>	<b>\$ (351,115)</b>	<b>\$ 48,485</b>	<b>\$ 162,910</b>	<b>\$ 98,322</b>	<b>\$ 134,281</b>	<b>\$ 92,883</b>
<b>CUMULATIVE GAP</b>	<b>\$ (351,115)</b>	<b>\$ (302,630)</b>	<b>\$ (139,720)</b>	<b>\$ (41,398)</b>	<b>\$ 92,883</b>	
<b>GAP TO INTEREST EARNING ASSETS</b>						
	-54.22%	7.49%	25.16%	15.18%	20.74%	
<b>CUMULATIVE GAP TO INTEREST EARNING ASSETS</b>						
	-54.22%	-46.74%	-21.58%	-6.39%	14.34%	

Based on a twelve-month forecast of the balance sheet, the following table sets forth our interest rate risk profile at December 31, 2013. For income simulation purposes, NOW and savings accounts are repriced quarterly. The impact on net interest income, illustrated in the following table would vary substantially if different assumptions were used or if actual experience differs from that indicated by the assumptions.

<u>Change in Interest Rates</u>	<u>Percentage Change in Net Interest Income</u>
Down 100 basis points	-1.4%
Down 200 basis points	-3.8%
Up 100 basis points	-0.8%
Up 200 basis points	-1.5%

### **Return on Assets and Equity**

For the year ended December 31, 2013, the return on average assets was 0.85% the return on average equity was 10.15% and the ratio of average shareholders' equity to average total assets was 8.36%.

For the year ended December 31, 2012, the return on average assets was 0.91% the return on average equity was 12.91% and the ratio of average shareholders' equity to average total assets was 7.08%.

### **Effects of Inflation**

The majority of assets and liabilities of the Company are monetary in nature, and therefore, differ greatly from most commercial and industrial companies that have significant investments in fixed assets or inventories. The precise impact of inflation upon the Company is difficult to measure. Inflation may affect the borrowing needs of consumers, thereby impacting the growth rate of the Company's assets. Inflation may also affect the general level of interest rates, which can have a direct bearing on the Company.

**Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS.**

Not required of a smaller reporting company.

**Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.**

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**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders  
Embassy Bancorp, Inc.

We have audited the accompanying consolidated balance sheets of Embassy Bancorp, Inc. and its subsidiary, Embassy Bank for the Lehigh Valley (collectively the “Company”), as of December 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for the years then ended. The Company’s management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2013 and 2012, and the consolidated results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ ParenteBeard LLC

Allentown, Pennsylvania  
March 28, 2014

**Consolidated Balance Sheets**

<b>ASSETS</b>	<b>December 31, 2013</b>	<b>December 31, 2012</b>
(In Thousands, Except Share and Per Share Data)		
Cash and due from banks	\$ 14,148	\$ 16,116
Interest bearing demand deposits with banks	2,683	12,824
Federal funds sold	1,000	1,000
Cash and Cash Equivalents	17,831	29,940
Interest bearing time deposits	1,822	5,945
Securities available for sale	71,288	91,857
Restricted investment in bank stock	2,157	1,454
Loans receivable, net of allowance for loan losses of \$5,326 in 2013; \$5,147 in 2012	563,257	500,072
Premises and equipment, net of accumulated depreciation	1,882	2,095
Bank owned life insurance	7,630	4,976
Accrued interest receivable	1,533	1,578
Other real estate owned	659	3,038
Other assets	2,776	2,054
<b>Total Assets</b>	<b>\$ 670,835</b>	<b>\$ 643,009</b>
<b><u>LIABILITIES AND STOCKHOLDERS' EQUITY</u></b>		
Liabilities:		
Deposits:		
Non-interest bearing	\$ 58,705	\$ 51,741
Interest bearing	510,332	501,279
Total Deposits	569,037	553,020
Securities sold under agreements to repurchase	30,418	24,452
Short-term borrowings	10,000	-
Long-term borrowings	3,900	12,586
Accrued interest payable	235	327
Other liabilities	3,190	2,597
<b>Total Liabilities</b>	<b>616,780</b>	<b>592,982</b>
Stockholders' Equity:		
Common stock, \$1 par value; authorized 20,000,000 shares;		
2013 issued 7,323,555 shares; outstanding 7,323,555 shares;		
2012 issued 7,238,823 shares; outstanding 7,238,823 shares	7,324	7,239
Surplus	23,671	23,146
Retained earnings	22,520	17,360
Accumulated other comprehensive income	540	2,282
<b>Total Stockholders' Equity</b>	<b>54,055</b>	<b>50,027</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 670,835</b>	<b>\$ 643,009</b>

*See notes to consolidated financial statements.*

**Consolidated Statements of Income**

	Year Ended December 31,	
	2013	2012
(In Thousands, Except Per Share Data)		
<b>INTEREST INCOME</b>		
Loans receivable, including fees	\$ 22,617	21,751
Securities, taxable	832	1,214
Securities, non-taxable	1,168	1,344
Federal funds sold, and other	14	95
Interest on time deposits	34	94
<b>Total Interest Income</b>	<b>24,665</b>	<b>24,498</b>
<b>INTEREST EXPENSE</b>		
Deposits	2,417	3,345
Securities sold under agreements to repurchase and federal funds purchased	17	62
Short-term borrowings	14	-
Long-term borrowings	492	700
<b>Total Interest Expense</b>	<b>2,940</b>	<b>4,107</b>
<b>Net Interest Income</b>	<b>21,725</b>	<b>20,391</b>
<b>PROVISION FOR LOAN LOSSES</b>	<b>992</b>	<b>1,183</b>
<b>Net Interest Income after Provision for Loan Losses</b>	<b>20,733</b>	<b>19,208</b>
<b>OTHER INCOME</b>		
Credit card processing fees	1,348	1,145
Other service fees	583	478
Bank owned life insurance	258	85
Gain on sale of securities, net	337	1,155
Profit (loss) on sale of other real estate owned	22	(8)
Impairment on other real estate owned	(260)	(350)
<b>Total Other Income</b>	<b>2,288</b>	<b>2,505</b>
<b>OTHER EXPENSES</b>		
Salaries and employee benefits	6,877	5,900
Occupancy and equipment	2,379	2,315
Data processing	1,210	1,161
Credit card processing	1,209	1,025
Advertising and promotion	962	869
Professional fees	489	524
FDIC insurance	421	396
Insurance	54	51
Loan & real estate	255	214
Charitable contributions	532	374
Other real estate owned expenses	76	118
Other	893	798
<b>Total Other Expenses</b>	<b>15,357</b>	<b>13,745</b>
<b>Income before Income Taxes</b>	<b>7,664</b>	<b>7,968</b>
<b>INCOME TAX EXPENSE</b>	<b>2,141</b>	<b>2,225</b>
<b>Net Income</b>	<b>\$ 5,523</b>	<b>\$ 5,743</b>
<b>BASIC EARNINGS PER SHARE</b>	<b>\$ 0.76</b>	<b>\$ 0.80</b>
<b>DILUTED EARNINGS PER SHARE</b>	<b>\$ 0.76</b>	<b>\$ 0.80</b>
<b>DIVIDENDS PER SHARE</b>	<b>\$ 0.05</b>	<b>\$ 0.04</b>

See notes to consolidated financial statements.

**Consolidated Statements of Comprehensive Income**

	<b>Year Ended December 31,</b>	
	<b>2013</b>	<b>2012</b>
<b>(In Thousands)</b>		
<b>Net Income</b>	\$ 5,523	\$ 5,743
<b>Other Comprehensive Income (Loss):</b>		
Unrealized holding (loss) gains on securities available for sale	(2,302)	994
Less: reclassification adjustment for realized gains	(337)	(1,155)
	(2,639)	(161)
Income tax effect	897	55
Net unrealized (loss) gains	(1,742)	(106)
<b>Other comprehensive loss, net of tax</b>	<b>(1,742)</b>	<b>(106)</b>
<b>Comprehensive Income</b>	<b>\$ 3,781</b>	<b>\$ 5,637</b>

*See notes to consolidated financial statements.*

Consolidated Statements of Stockholders' Equity

Years Ended December 31, 2013 and 2012

	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Total
(In Thousands, Except Share Data)						
<b>BALANCE - DECEMBER 31, 2011</b>	\$ 7,171	\$ 22,872	\$ 11,905	\$ 2,388	\$ (3)	\$ 44,333
Net income	-	-	5,743	-	-	5,743
Other comprehensive income	-	-	-	(106)	-	(106)
Dividend declared, \$.04 per share	-	-	(288)	-	-	(288)
Exercise of stock options, 49,729 shares, Treasury issued 353 shares	50	141	-	-	3	194
Tax benefit of stock options exercised	-	23	-	-	-	23
Stock tendered for funding exercise of stock options, 10,481 shares	(10)	(63)	-	-	-	(73)
Compensation expense recognized on stock options	-	39	-	-	-	39
Common stock grants to directors, 7,992 shares	8	48	-	-	-	56
Shares issued under Dividend Reinvestment and Stock Purchase Plan, 20,385 shares	20	86	-	-	-	106
<b>BALANCE - DECEMBER 31, 2012</b>	\$ 7,239	\$ 23,146	\$ 17,360	\$ 2,282	\$ -	\$ 50,027
<b>BALANCE - DECEMBER 31, 2012</b>	\$ 7,239	\$ 23,146	\$ 17,360	\$ 2,282	\$ -	\$ 50,027
Net income	-	-	5,523	-	-	5,523
Other comprehensive loss	-	-	-	(1,742)	-	(1,742)
Dividend declared, \$.05 per share	-	-	(363)	-	-	(363)
Exercise of stock options, 43,617 shares Tax benefit of stock options exercised	44	236	-	-	-	280
Stock tendered for funding exercise of stock options, 22,549 shares	(23)	(146)	-	-	-	(169)
Compensation expense recognized on stock options	-	61	-	-	-	61
Common stock grants to directors, 8,764 shares	9	53	-	-	-	62
Shares issued under Dividend Reinvestment and Stock Purchase Plan, 54,900 shares	55	317	-	-	-	372
<b>BALANCE - DECEMBER 31, 2013</b>	\$ 7,324	\$ 23,671	\$ 22,520	\$ 540	\$ -	\$ 54,055

See notes to consolidated financial statements.

**Consolidated Statements of Cash Flows**

	Year Ended December 31,	
	2013	2012
	(In Thousands)	
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 5,523	\$ 5,743
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	992	1,183
Accretion of deferred loan costs	(78)	(73)
Depreciation and amortization	612	613
Net amortization of investment security premiums and discounts	285	396
Stock compensation expense	61	39
(Gain) loss on sale of other real estate owned	(22)	8
Impairment on other real estate owned	260	350
Income on bank owned life insurance	(258)	(85)
Deferred income taxes	(456)	(628)
Net realized gain on sale of securities available for sale	(337)	(1,155)
Decrease (increase) in accrued interest receivable	45	(10)
Decrease in other assets	631	123
Decrease in accrued interest payable	(92)	(255)
Increase in other liabilities	557	902
<b>Net Cash Provided by Operating Activities</b>	<b>7,723</b>	<b>7,151</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchases of securities available for sale	(11,390)	(25,836)
Maturities, calls and principal repayments of securities available for sale	23,588	15,889
Proceeds from sales of securities available for sale	5,784	10,798
Net increase in loans	(61,860)	(82,375)
Net (purchases) redemption of restricted investment in bank stock	(703)	187
Net maturities of interest bearing time deposits	4,123	1,753
Purchase of bank owned life insurance	(2,396)	(4,666)
Proceeds from sale of other real estate owned	-	311
Purchases of premises and equipment	(399)	(613)
<b>Net Cash Used in Investing Activities</b>	<b>(43,253)</b>	<b>(84,552)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net increase in deposits	16,017	71,245
Net decrease (increase) in securities sold under agreements to repurchase and federal funds purchased	5,966	(9,501)
Increase in short-term borrowed funds	10,000	-
Payment of long-term borrowed funds	(8,686)	(500)
Exercise of stock options, net payment for stock tendered	112	121
Proceeds from Dividend Reinvestment Plan	371	-
Tax benefit of stock options exercised	4	23
Dividends paid	(363)	(182)
<b>Net Cash Provided by Financing Activities</b>	<b>23,421</b>	<b>61,206</b>
<b>Net Decrease in Cash and Cash Equivalents</b>	<b>(12,109)</b>	<b>(16,195)</b>
<b>CASH AND CASH EQUIVALENTS - BEGINNING</b>	<b>29,940</b>	<b>46,135</b>
<b>CASH AND CASH EQUIVALENTS - ENDING</b>	<b>\$ 17,831</b>	<b>\$ 29,940</b>
<b>SUPPLEMENTARY CASH FLOWS INFORMATION</b>		
Interest paid	\$ 3,032	\$ 4,362
Income taxes paid	\$ 2,725	\$ 2,675
Other real estate sold through bank financing	\$ 2,381	\$ -
Deferral of gain from sale of other real estate sold through bank financing	\$ (97)	\$ -
Other real estate acquired in settlement of loans	\$ 142	\$ 319

See notes to consolidated financial statements.

## **Note 1 – Summary of Significant Accounting Policies**

### **Principles of Consolidation and Nature of Operations**

Embassy Bancorp, Inc. (the “Company”) is a Pennsylvania corporation organized in 2008 and registered as a bank holding company pursuant to the Bank Holding Company Act of 1956, as amended (the “BHC Act”). The Company was formed for purposes of acquiring Embassy Bank For The Lehigh Valley (the “Bank”) in connection with the reorganization of the Bank into a bank holding company structure, which was consummated on November 11, 2008. Accordingly, the Company owns all of the capital stock of the Bank, giving the organization more flexibility in meeting its capital needs as the Company continues to grow.

The Bank, which is the Company’s principal operating subsidiary, was originally incorporated as a Pennsylvania bank on May 11, 2001 and opened its doors on November 6, 2001. It was formed by a group of local business persons and professionals with significant prior experience in community banking in the Lehigh Valley area of Pennsylvania, the Bank’s primary market area.

### **Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of other real estate owned, and the valuation of deferred tax assets.

### **Concentrations of Credit Risk**

Most of the Company’s activities are with customers located in the Lehigh Valley area of Pennsylvania. Note 2 discuss the types of securities in which the Company invests. The concentrations of credit by type of loan are set forth in Note 3. The Company does not have any significant concentrations to any one specific industry or customer, with the exception of lending activity to a broad range of lessors of residential and non-residential real estate within the Lehigh Valley. Although the Company has a diversified loan portfolio, its debtors’ ability to honor their contracts is influenced by the region’s economy.

### **Presentation of Cash Flows**

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, interest-bearing demand deposits with bank, and federal funds sold. Generally, federal funds are purchased or sold for less than one week periods.

### **Securities**

Securities classified as available for sale are those securities that the Company intends to hold for an indefinite period of time, but not necessarily to maturity. Securities available for sale are carried at fair value. Any decision to sell a security classified as available for sale would be based on various factors, including significant movement in interest rates, changes in maturity mix of the Company’s assets and liabilities, liquidity needs, regulatory capital considerations and other similar factors. Unrealized gains and losses are reported as increases or decreases in other comprehensive income. Realized gains or losses, determined on the basis of the cost of the specific securities sold, are included in earnings. Premiums and discounts are recognized in interest income using the interest method over the terms of the securities.

Other than temporary accounting guidance specifies that (a) if a company does not have the intent to sell a debt security prior to recovery and (b) it is more likely than not that it will not have to sell the debt security prior to recovery, the security would not be considered other-than-temporarily impaired unless there is a credit loss. When an entity does not intend to sell the security, and it is more likely than not the entity will not have to sell the security before recovery of its cost basis, it will recognize the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income. The Company recognized no other-than-temporary impairment charges during the years ended December 31, 2013 and 2012.

### **Restricted Investments in Bank Stock**

Restricted investments in bank stock consist of Federal Home Loan Bank of Pittsburgh (“FHLB”) stock and Atlantic Community Bankers Bank (“ACBB”) stock. The restricted stocks are carried at cost. Federal law requires a member institution of the FHLB to hold stock of its district FHLB according to a predetermined formula.

In December 2008, the FHLB of Pittsburgh notified member banks that it was suspending dividend payments and the repurchase of capital stock, and any future capital stock repurchases will be made on a quarterly basis if conditions warrant such repurchases. During 2013, 2012 and 2011 the FHLB conducted limited excess capital stock repurchases based upon positive quarterly net income. Any future capital stock repurchases will be made on a quarterly basis if conditions warrant such repurchases. In February 2012, the FHLB announced that dividend payments would resume in 2012. Dividend payments of \$12 thousand and \$2 thousand were received during the years ended December 31, 2013 and 2012, respectively.

Management evaluates the FHLB and ACBB restricted stock for impairment. Management’s determination of whether these investments are impaired is based on their assessment of the ultimate recoverability of their cost rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of their cost is influenced by criteria such as (1) the significance of the decline in net assets of the issuer as compared to the capital stock amount for the issuer and the length of time this situation has persisted, (2) commitments by the issuer to make payments required by law or regulation and the level of such payments in relation to the operating performance of the issuer, and (3) the impact of legislative and regulatory changes on institutions and, accordingly, on the customer base of the issuer.

Management believes no impairment charge is necessary related to the FHLB or ACBB restricted stock as of December 31, 2013.

### **Loans Receivable**

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their outstanding unpaid principal balances, net of any deferred fees or costs. 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 yield using the effective interest method. Premiums and discounts on purchased loans are amortized as adjustments to interest income using the effective interest method. Delinquency fees are recognized in income when chargeable, assuming collectability is reasonably assured.

The loans receivable portfolio is segmented into commercial and consumer loans. Commercial loans consist of the following classes: commercial real estate, commercial construction and commercial. Consumer loans consist of the following classes: residential real estate and other consumer loans.

The Company makes commercial loans for real estate development and other business purposes required by the customer base. The Company's credit policies determine advance rates against the different forms of collateral that can be pledged against commercial loans. Typically, the majority of loans will be limited to a percentage of their underlying collateral values such as real estate values, equipment, eligible accounts receivable and inventory. Individual loan advance rates may be higher or lower depending upon the financial strength of the borrower and/or term of the loan. The assets financed through commercial loans are used within the business for its ongoing operation. Repayment of these kinds of loans generally comes from the cash flow of the business or the ongoing conversion of assets. Commercial real estate loans include long-term loans financing commercial properties. Repayments of these loans are dependent upon either the ongoing cash flow of the borrowing entity or the resale of or lease of the subject property. Commercial real estate loans typically require a loan to value of not greater than 80% and vary in terms.

Residential mortgages and home equity loans are secured by the borrower's residential real estate in either a first or second lien position. Residential mortgages and home equity loans have varying loan rates depending on the financial condition of the borrower and the loan to value ratio. Residential mortgages may have amortizations up to 30 years and home equity loans may have maturities up to 25 years. Other consumer loans include installment loans, car loans, and overdraft lines of credit. The majority of these loans are unsecured.

For all classes of loans receivable, the accrual of interest may be discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectability of principal or interest, even though the loan is currently performing. A loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured. When a loan is placed on nonaccrual status, unpaid interest credited to income in the current year is reversed. Interest received on nonaccrual loans, including impaired loans, generally is applied against principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time (generally six months) and the ultimate collectability of the total contractual principal and interest is no longer in doubt. The past due status of all classes of loans receivable is determined based on contractual due dates for loan payments.

### **Allowance for Loan Losses**

The allowance for loan losses represents management's estimate of losses inherent in the loan portfolio as of the balance sheet date and is recorded as a reduction to loans. The reserve for unfunded loan commitments represents management's estimate of losses inherent in its unfunded loan commitments and is recorded in other liabilities on the consolidated balance sheet. The allowance for loan losses is increased by the provision for loan losses, and decreased by charge-offs, net of recoveries. Loans, or portions of loans, determined to be confirmed losses are charged against the allowance account and subsequent recoveries, if any, are credited to the account. A loss is considered confirmed when information available at the financial statement date indicates the loan, or a portion thereof, is uncollectible.

Management performs a quarterly evaluation of the adequacy of the allowance. The allowance is based on the Company's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant revision as more information becomes available.

Management maintains the allowance for loan losses at a level it believes adequate to absorb probable credit losses related to specifically identified loans, as well as probable incurred losses inherent in the remainder of the loan portfolio as of the balance sheet dates. The allowance for loan losses account consists of specific and general reserves. The specific component consists of the specific reserve for impaired loans individually evaluated under Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 310, “Receivables,” and the general component is utilized for loss contingencies on those loans collectively evaluated under FASB ASC 450, “Contingencies.”

For the specific portion of the allowance for loan losses, a loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. All amounts due according to the contractual terms means that both the contractual interest and principal payments of a loan will be collected as scheduled in the loan agreement. Factors considered by management in determining impairment include payment status, ability to pay and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower’s prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Loans considered impaired under FASB ASC 310 are measured for impairment based on the present value of expected future cash flows discounted at the loan’s effective interest rate or the fair value of the collateral if the loan is collateral dependent. If the present value of expected future cash flows discounted at the loan’s effective interest rate or the fair value of the collateral, if the loan is collateral dependent, is less than the recorded investment in the loan, including accrued interest and net deferred loan fees or costs, the Company will recognize the impairment by adjusting the allowance for loan losses account through charges to earnings as a provision for loan losses.

For loans secured by real estate, estimated fair values are determined primarily through third-party appraisals. When a real estate secured loan becomes impaired, a decision is made regarding whether an updated certified appraisal of the real estate is necessary. This decision is based on various considerations, including the age of the most recent appraisal, loan-to-value ratio based on the original appraisal and the condition of the property. Appraised values are discounted to arrive at the estimated selling price of the collateral, which is considered to be the estimated fair value. The discounts also include estimated costs to sell the property.

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 or 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 general portion of the allowance for loan losses covers pools of loans by major loan class including commercial loans not considered impaired, as well as smaller balance homogeneous loans, such as residential real estate and other consumer loans. Loss contingencies for each of the major loan pools are determined by applying a total loss factor to the current balance outstanding for each individual pool. The total loss factor is comprised of a historical loss factor using the loss migration method plus a qualitative factor, which adjusts the historical loss factor for changes in trends, conditions and other relevant factors that may affect repayment of the loans in these pools as of the evaluation date. Loss migration involves determining the percentage of each pool that is expected to ultimately result in loss based on historical loss experience. Historical loss factors are based on the ratio of net loans charged-off to loans, net, for each of the major groups of loans evaluated and measured for impairment under FASB ASC 450. The historical loss factor for each pool is an average of the Company’s historical net charge-off ratio for the most recent rolling twenty quarters.

In addition to these historical loss factors, management also uses a qualitative factor that represents a number of environmental risks that may cause estimated credit losses associated with the current portfolio to differ from historical loss experience. These environmental risks include: (i) changes in lending policies and procedures including underwriting standards and collection, charge-off and recovery practices; (ii) changes in the composition and volume of the portfolio; (iii) changes in national, local and industry conditions, including the effects of such changes on the value of underlying collateral for collateral-dependent loans; (iv) changes in the volume and severity of classified loans, including past due, nonaccrual, troubled debt restructures and other loan modifications; (v) changes in the levels of, and trends in, charge-offs and recoveries; (vi) the existence and effect of any concentrations of credit and changes in the level of such concentrations; (vii) changes in the experience, ability and depth of lending management and other relevant staff; (viii) changes in the quality of the loan review system and the degree of oversight by the board of directors; and (ix) the effect of external factors such as competition and regulatory requirements on the level of estimated credit losses in the current loan portfolio. Each environmental risk 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 general allowance is used to cover inherent losses that exist as of the evaluation date, but which have not been identified as part of the allocated allowance using the above impairment evaluation methodology due to limitations in the process. One such limitation is the imprecision of accurately estimating the impact current economic conditions will have on historical loss rates. Variations in the magnitude of impact may cause estimated credit losses associated with the current portfolio to differ from historical loss experience, resulting in an allowance that is higher or lower than the anticipated level.

The allowance calculation methodology includes further segregation of loan classes into risk rating categories. The borrower's overall financial condition, repayment sources, guarantors and value of collateral, if appropriate, are evaluated annually for commercial loans or when credit deficiencies arise, such as delinquent loan payment, for commercial and consumer loans. Credit quality risk ratings include regulatory classifications of special mention, substandard, doubtful and loss. Loans criticized as special mention have potential weaknesses that deserve management's close attention. If uncorrected, the potential weakness may result in deterioration of the repayment prospects. Loans classified substandard have a well-defined weakness and borrowers are highly leveraged. They include loans that are inadequately protected by the current sound net worth and the 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.

Federal regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses and may require the Company 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, management believes the current level of the allowance for loan losses is adequate.

### **Other Real Estate Owned**

Other real estate owned is comprised of properties acquired through foreclosure proceedings or acceptance of a deed-in-lieu of foreclosure and loans classified as in-substance foreclosures. A loan is classified as an in-substance foreclosure when the Company has taken possession of the collateral, regardless of whether formal foreclosure proceedings take place. Other real estate owned is recorded at fair value less cost to sell at the time of acquisition. Any excess of the loan balance over the recorded value is charged to the allowance for loan losses. After foreclosure, valuations are periodically performed and the assets are carried at the lower of cost or fair value less cost to sell. Changes in the valuation allowance on foreclosed assets are included in other income. Costs to maintain the assets are included in other expenses. Any gain or loss realized upon disposal of other real estate owned is included in other income.

### **Bank Owned Life Insurance**

The Company invests in bank owned life insurance (“BOLI”) as a source of funding for employee benefit expenses. BOLI involves the purchasing of life insurance by the Company on certain of its employees and directors. The Company is the owner and beneficiary of the policies. This life insurance investment is carried at the cash surrender value of the underlying policies. Income from increases in cash surrender value of the policies is included in non-interest income.

### **Premises and Equipment**

Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over the following estimated useful lives of the related assets: furniture, fixtures and equipment for five to ten years, leasehold improvements for ten to fifteen years, computer equipment and data processing software for three to five years, and automobiles for five years.

### **Transfers of Financial Assets**

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

### **Advertising Costs**

The Company follows the policy of charging the costs of advertising to expense as incurred.

### **Income Taxes**

Income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to taxable income. Deferred income taxes are provided on the liability method whereby deferred 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 and net operating loss carry forwards 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 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.

## Earnings Per Share

Basic earnings per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period, as adjusted for stock dividends and splits. Diluted earnings per share reflect additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustments to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate solely to outstanding stock options and are determined using the treasury stock method.

	<u>2013</u>	<u>2012</u>
	(Dollars In Thousands, Except Per Share Data)	
Net income	\$ 5,523	\$ 5,743
Weighted average shares outstanding	7,261,293	7,195,353
Dilutive effect of potential common shares, stock options	8,710	21,331
Diluted weighted average common shares outstanding	<u>7,270,003</u>	<u>7,216,684</u>
Basic earnings per share	<u>\$ 0.76</u>	<u>\$ 0.80</u>
Diluted earnings per share	<u>\$ 0.76</u>	<u>\$ 0.80</u>

Stock options of 149,692 and 127,942 were not considered in computing diluted earnings per common share for the years ended December 31, 2013 and 2012, respectively, because they are not dilutive to earnings.

## Employee Benefit Plan

The Company has a 401(k) Plan (the "Plan") for employees. All employees are eligible to participate after they have attained the age of 21 and have also completed 12 consecutive months of service during which at least 1,000 hours of service are completed. The employees may contribute up to the maximum percentage allowable by law of their compensation to the Plan, and the Company provides a match of fifty percent of the first 8% percent to eligible participating employees. Full vesting in the Plan is prorated equally over a four-year period. The Company's contributions to the Plan for the years ended December 31, 2013 and 2012 were \$123 thousand and \$96 thousand, respectively.

## Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit and letters of credit. Such financial instruments are recorded in the balance sheet when they are funded.

## **Comprehensive Income**

Accounting principles generally accepted in the United States of America require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income. In accordance with Financial Accounting Standards Board guidance, the Company has disclosed the components of comprehensive income in the accompanying statements of comprehensive income.

## **Segment Reporting**

The Company acts as an independent, community, financial services provider, and offers traditional banking and related financial services to individual, business and government customers. The Company offers a full array of commercial and retail financial services, including the taking of time, savings and demand deposits; the making of commercial, consumer and home equity loans; and the provision of other financial services.

Management does not separately allocate expenses, including the cost of funding loan demand, between the commercial and retail operations of the Company. As such, discrete financial information is not available and segment reporting would not be meaningful.

## **Stock-Based Compensation**

The Company applies the fair value recognition provisions of ASC 718, Compensation-Stock Compensation. ASC 718 requires compensation costs related to share-based payment transactions to be recognized in the financial statements over the period that an employee provides service in exchange for the award based on the fair value of the award. The Black-Scholes model is used to estimate the fair value of stock options.

## **Subsequent Events**

The Company follows ASC Topic 855 Subsequent Events. This topic establishes general standards for accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued. The Company has evaluated events and transactions occurring subsequent to the balance sheet date of December 31, 2013 through the date these financial statements were available for issuance for items that should potentially be recognized or disclosed in these financial statements.

## **New Accounting Standards**

### **Accounting Standards Update (ASU) No. 2011-11, Balance Sheet (Topic 210)—Disclosures about Offsetting Assets and Liabilities, and ASU No. 2013-01, Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities.**

ASU 2011-11 amends Topic 210, “Balance Sheet”, to require an entity to disclose both gross and net information about financial instruments, such as sales and repurchase agreements and reverse sale and repurchase agreements and securities borrowing/lending arrangements, and derivative instruments that are eligible for offset in the statement of financial position and/or subject to master netting arrangement or similar agreement. ASU 2011-11 is effective for annual and interim periods beginning on January 1, 2013, and did not have a material impact on the Company’s financial statements. See Note 17 – Offsetting Assets and Liabilities.

### **Accounting Standards Update (ASU) No. 2013-02, Comprehensive Income (Topic 220) – Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income.**

ASU 2013-02 amends recent guidance related to the reporting of comprehensive income to enhance the reporting of reclassifications out of accumulated other comprehensive income. ASU 2013-02 became effective for the Company on January 1, 2013 and did not have a material impact on the Company’s financial statements. See Note 12 - Other Comprehensive Income.

### **Accounting Standards Update (ASU) 2014-04, Receivables – Troubled Debt Restructurings by Creditors (Subtopic 310-40) - Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure.**

The objective of this ASU is to reduce the diversity in practice of when a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan and when the related loan receivable should be derecognized and the real estate owned recognized. This amendment clarifies that an in substance repossession or foreclosure occurs when either a) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure, or b) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Upon completion of either of these two events the creditor is considered to have received physical possession of residential real estate property and therefore should derecognize the loan receivable and recognize the real estate owned. Additionally, this amendment requires interim and annual disclosure of both a) the amount of foreclosed residential real estate property held by the creditor and b) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to local requirements of the applicable jurisdiction.

The provisions of this ASU are effective for public business entities for annual periods and interim periods within those annual periods beginning after December 15, 2014. For entities other than public business entities, this ASU is effective for annual periods beginning after December 15, 2014, and interim periods within annual periods beginning after December 15, 2015. This ASU can be adopted using either a modified retrospective transition method or a prospective transition method. Early adoption is permitted. The Company is currently evaluating the impact of this ASU on its consolidated financial statements.

## **Reclassification**

Certain amounts in the 2012 financial statements may have been reclassified to conform to 2013 presentation. These reclassifications had no effect on 2012 net income.

**Note 2 – Securities Available For Sale**

The amortized cost and approximate fair values of securities available-for-sale were as follows:

	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>
(In Thousands)				
<b>December 31, 2013 :</b>				
U.S. Government agency obligations	\$ 27,191	\$ 118	\$ (304)	\$ 27,005
Municipal bonds	32,220	902	(222)	32,900
U.S. Government Sponsored Enterprise (GSE) - Mortgage-backed securities - residential	9,062	300	-	9,362
Corporate bonds	1,997	24	-	2,021
<b>Total</b>	<b>\$ 70,470</b>	<b>\$ 1,344</b>	<b>\$ (526)</b>	<b>\$ 71,288</b>
<b>December 31, 2012 :</b>				
U.S. Government agency obligations	\$ 40,386	\$ 237	\$ (18)	\$ 40,605
Municipal bonds	36,273	2,696	(17)	38,952
U.S. Government Sponsored Enterprise (GSE) - Mortgage-backed securities - residential	8,487	530	-	9,017
Corporate bonds	3,254	29	-	3,283
<b>Total</b>	<b>\$ 88,400</b>	<b>\$ 3,492</b>	<b>\$ (35)</b>	<b>\$ 91,857</b>

The amortized cost and fair value of securities as of December 31, 2013, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to prepay obligations with or without any penalties.

	<b>Amortized Cost</b>	<b>Fair Value</b>
(In Thousands)		
Due in one year or less	\$ 3,507	\$ 3,525
Due after one year through five years	29,350	29,295
Due after five years through ten years	15,882	16,118
Due after ten years	12,669	12,988
	61,408	61,926
U.S. Government Sponsored Enterprise (GSE) - Mortgage- backed securities - residential	9,062	9,362
	<b>\$ 70,470</b>	<b>\$ 71,288</b>

Gross gains of \$337 thousand and \$1.2 million were realized on sales of securities for the years ended December 31, 2013 and December 31, 2012, respectively. There were no gross losses in 2013 or 2012 on the sale of securities.

The following table shows the Company'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 December 31, 2013 and December 31, 2012, respectively:

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>December 31, 2013 :</b>	(In Thousands)					
U.S. Government agency obligations	\$ 16,895	\$ (304)	\$ -	\$ -	\$ 16,895	\$ (304)
Municipal bonds	7,441	(222)	-	-	7,441	(222)
<b>Total Temporarily Impaired Securities</b>	<b>\$ 24,336</b>	<b>\$ (526)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 24,336</b>	<b>\$ (526)</b>
<b>December 31, 2012 :</b>						
U.S. Government agency obligations	\$ 9,163	\$ (18)	\$ -	\$ -	\$ 9,163	\$ (18)
Municipal bonds	1,057	(17)	-	-	1,057	(17)
<b>Total Temporarily Impaired Securities</b>	<b>\$ 10,220</b>	<b>\$ (35)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 10,220</b>	<b>\$ (35)</b>

The Company had twenty-eight (28) securities in an unrealized loss position at December 31, 2013. Unrealized losses are due only to market rate fluctuations. As of December 31, 2013, the Company either has the intent and ability to hold the securities until maturity or market price recovery, or believes that it is more likely than not that it will not be required to sell such securities. Management believes that the unrealized loss only represents temporary impairment of the securities. None of the individual losses are significant.

Securities with a carrying value of \$43.6 million and \$45.8 million at December 31, 2013 and December 31, 2012, respectively, were subject to agreements to repurchase, pledged to secure public deposits, or pledged for other purposes required or permitted by law.

**Note 3 – Loans Receivable**

The following table presents the composition of loans receivable at December 31, 2013 and 2012 respectively:

	2013	2012
	(In Thousands)	
Commercial real estate	\$ 235,545	\$ 204,904
Commercial construction	21,109	19,717
Commercial	28,017	28,696
Residential real estate	283,421	250,854
Consumer	846	1,382
<b>Total Loans</b>	<b>568,938</b>	<b>505,553</b>
Unearned net loan origination fees	(355)	(334)
Allowance for Loan Losses	(5,326)	(5,147)
	<b>\$ 563,257</b>	<b>\$ 500,072</b>

**Note 4 – Allowance for Loan Losses**

The changes in the allowance for loan losses for the years ended December 31, 2013 and 2012 are as follows:

	2013	2012
Allowance for loan losses:	(In Thousands)	
Balance, beginning	\$ 5,147	\$ 4,215
Provision for loan losses	992	1,183
Loans charged off	(857)	(270)
Recoveries	44	19
Balance at end of year	<u>\$ 5,326</u>	<u>\$ 5,147</u>

The following table presents the classes of the loan portfolio summarized by the aggregate pass rating and the classified ratings of special mention (potential weaknesses), substandard (well defined weaknesses) and doubtful (full collection unlikely) within the Company's internal risk rating system as of December 31, 2013 and December 31, 2012, respectively:

	Pass	Special Mention	Substandard	Doubtful	Total
<b>December 31, 2013</b>	(In Thousands)				
Commercial real estate	\$ 229,987	\$ 703	\$ 4,794	\$ 61	\$ 235,545
Commercial construction	18,091	902	2,116	-	21,109
Commercial	27,499	480	38	-	28,017
Residential real estate	282,296	644	481	-	283,421
Consumer	846	-	-	-	846
Total	<u>\$ 558,719</u>	<u>\$ 2,729</u>	<u>\$ 7,429</u>	<u>\$ 61</u>	<u>\$ 568,938</u>
<b>December 31, 2012</b>					
Commercial real estate	\$ 197,879	\$ 748	\$ 6,277	\$ -	\$ 204,904
Commercial construction	16,102	341	3,274	-	19,717
Commercial	28,066	530	100	-	28,696
Residential real estate	249,737	156	660	301	250,854
Consumer	1,382	-	-	-	1,382
Total	<u>\$ 493,166</u>	<u>\$ 1,775</u>	<u>\$ 10,311</u>	<u>\$ 301</u>	<u>\$ 505,553</u>

The following table summarizes information in regards to impaired loans by loan portfolio class as of December 31, 2013 and 2012, respectively:

	Year to Date				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
<b>December 31, 2013</b>					
(In Thousands)					
With no related allowance recorded:					
Commercial real estate	\$ 6,151	\$ 6,446		\$ 6,263	\$ 286
Commercial construction	3,017	3,215		2,992	106
Commercial	171	170		241	8
Residential real estate	618	656		465	26
Consumer	-	-		-	-
With an allowance recorded:					
Commercial real estate	\$ 855	\$ 914	\$ 82	\$ 939	\$ 131
Commercial construction	-	-	-	325	-
Commercial	38	38	1	15	2
Residential real estate	1,113	1,113	322	985	37
Consumer	-	-	-	-	-
Total:					
Commercial real estate	\$ 7,006	\$ 7,360	\$ 82	\$ 7,202	\$ 417
Commercial construction	3,017	3,215	-	3,317	106
Commercial	209	208	1	256	10
Residential real estate	1,731	1,769	322	1,450	63
Consumer	-	-	-	-	-
	<u>\$ 11,963</u>	<u>\$ 12,552</u>	<u>\$ 405</u>	<u>\$ 12,225</u>	<u>\$ 596</u>

<b>December 31, 2012</b>					
With no related allowance recorded:					
Commercial real estate	\$ 5,985	\$ 5,985		\$ 6,031	\$ 301
Commercial construction	2,117	2,117		3,218	77
Commercial	291	291		302	7
Residential real estate	458	458		377	23
Consumer	-	-		-	-
With an allowance recorded:					
Commercial real estate	\$ 1,635	\$ 1,635	\$ 411	\$ 1,899	\$ 161
Commercial construction	1,498	1,498	198	749	44
Commercial	11	60	11	5	-
Residential real estate	660	660	130	689	18
Consumer	-	-	-	-	-
Total:					
Commercial real estate	\$ 7,620	\$ 7,620	\$ 411	\$ 7,930	\$ 462
Commercial construction	3,615	3,615	198	3,967	121
Commercial	302	351	11	307	7
Residential real estate	1,118	1,118	130	1,066	41
Consumer	-	-	-	-	-
	<u>\$ 12,655</u>	<u>\$ 12,704</u>	<u>\$ 750</u>	<u>\$ 13,270</u>	<u>\$ 631</u>

The following table presents nonaccrual loans by classes of the loan portfolio as of December 31, 2013 and 2012, respectively:

	<b>December 31, 2013</b>	<b>December 31, 2012</b>
	(In Thousands)	
Commercial real estate	\$ 1,635	\$ 2,104
Commercial construction	-	-
Commercial	189	39
Residential real estate	481	301
Consumer	-	-
Total	<u>\$ 2,305</u>	<u>\$ 2,444</u>

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 December 31, 2013 and 2012, respectively:

	<b>30-59 Days Past Due</b>	<b>60-89 Days Past Due</b>	<b>Greater than 90 Days</b>	<b>Total Past Due</b>	<b>Current</b>	<b>Total Loan Receivables</b>	<b>Loan Receivables &gt; 90 Days and Accruing</b>
<b>December 31, 2013</b>	(In Thousands)						
Commercial real estate	\$ 776	\$ 415	\$ 2,049	\$ 3,240	\$ 232,305	\$ 235,545	\$ 763
Commercial construction	-	2,622	-	2,622	18,487	21,109	-
Commercial	-	-	189	189	27,828	28,017	-
Residential real estate	-	-	481	481	282,940	283,421	-
Consumer	-	-	-	-	846	846	-
Total	<u>\$ 776</u>	<u>\$ 3,037</u>	<u>\$ 2,719</u>	<u>\$ 6,532</u>	<u>\$ 562,406</u>	<u>\$ 568,938</u>	<u>\$ 763</u>
<b>December 31, 2012</b>							
Commercial real estate	\$ 831	\$ -	\$ 1,809	\$ 2,640	\$ 202,264	\$ 204,904	\$ 351
Commercial construction	2,559	-	-	2,559	17,158	19,717	-
Commercial	-	39	10	49	28,647	28,696	10
Residential real estate	301	-	301	602	250,252	250,854	-
Consumer	13	-	-	13	1,369	1,382	-
Total	<u>\$ 3,704</u>	<u>\$ 39</u>	<u>\$ 2,120</u>	<u>\$ 5,863</u>	<u>\$ 499,690</u>	<u>\$ 505,553</u>	<u>\$ 361</u>

The following table summarizes information in regards to the allowance for loan losses and the recorded investment in loans receivable at December 31, 2013, and the activity in the allowance for loan losses for the year ended December 31, 2012:

	<u>Commercial Real Estate</u>	<u>Commercial Construction</u>	<u>Commercial</u>	<u>Residential Real Estate</u>	<u>Consumer</u>	<u>Unallocated</u>	<u>Total</u>
<b>Allowance for credit losses</b>	(In Thousands)						
<b>Year Ending December 31, 2013</b>							
<b>Beginning Balance - December 31, 2012</b>	\$ 2,007	\$ 660	\$ 394	\$ 1,677	\$ 33	\$ 376	\$ 5,147
Charge-offs	(530)	(197)	(13)	(112)	(5)	-	(857)
Recoveries	13	-	3	28	-	-	44
Provisions	301	32	(35)	475	(4)	223	992
<b>Ending Balance - December 31, 2013</b>	<b>\$ 1,791</b>	<b>\$ 495</b>	<b>\$ 349</b>	<b>\$ 2,068</b>	<b>\$ 24</b>	<b>\$ 599</b>	<b>\$ 5,326</b>
<b>Year Ending December 31, 2012</b>							
<b>Beginning Balance - December 31, 2011</b>	\$ 1,264	\$ 352	\$ 423	\$ 1,691	\$ 40	\$ 445	\$ 4,215
Charge-offs	(231)	-	-	(39)	-	-	(270)
Recoveries	1	-	-	18	-	-	19
Provisions	973	308	(29)	7	(7)	(69)	1,183
<b>Ending Balance - December 31, 2012</b>	<b>\$ 2,007</b>	<b>\$ 660</b>	<b>\$ 394</b>	<b>\$ 1,677</b>	<b>\$ 33</b>	<b>\$ 376</b>	<b>\$ 5,147</b>

The following tables represent the allocation of the allocation for loan losses and the related loan portfolio disaggregated based on impairment methodology at December 31, 2013 and December 31, 2012:

	<b>Commercial Real Estate</b>	<b>Commercial Construction</b>	<b>Commercial</b>	<b>Residential Real Estate</b>	<b>Consumer</b>	<b>Unallocated</b>	<b>Total</b>
(In Thousands)							
<b>December 31, 2013</b>							
<b>Allowance for Loan Losses</b>							
Ending Balance	\$ 1,791	\$ 495	\$ 349	\$ 2,068	\$ 24	\$ 599	\$ 5,326
Ending balance: individually evaluated for impairment	\$ 82	\$ -	\$ 1	\$ 322	\$ -	\$ -	\$ 405
Ending balance: collectively evaluated for impairment	\$ 1,709	\$ 495	\$ 348	\$ 1,746	\$ 24	\$ 599	\$ 4,921
<b>Loans receivables:</b>							
Ending balance	\$ 235,545	\$ 21,109	\$ 28,017	\$ 283,421	\$ 846		\$ 568,938
Ending balance: individually evaluated for impairment	\$ 7,006	\$ 3,017	\$ 209	\$ 1,731	\$ -		\$ 11,963
Ending balance: collectively evaluated for impairment	\$ 228,539	\$ 18,092	\$ 27,808	\$ 281,690	\$ 846		\$ 556,975
<b>December 31, 2012</b>							
<b>Allowance for Loan Losses</b>							
Ending Balance	\$ 2,007	\$ 660	\$ 394	\$ 1,677	\$ 33	\$ 376	\$ 5,147
Ending balance: individually evaluated for impairment	\$ 411	\$ 198	\$ 11	\$ 130	\$ -	\$ -	\$ 750
Ending balance: collectively evaluated for impairment	\$ 1,596	\$ 462	\$ 383	\$ 1,547	\$ 33	\$ 376	\$ 4,397
<b>Loans receivables:</b>							
Ending balance	\$ 204,904	\$ 19,717	\$ 28,696	\$ 250,854	\$ 1,382		\$ 505,553
Ending balance: individually evaluated for impairment	\$ 7,620	\$ 3,615	\$ 302	\$ 1,118	\$ -		\$ 12,655
Ending balance: collectively evaluated for impairment	\$ 197,284	\$ 16,102	\$ 28,394	\$ 249,736	\$ 1,382		\$ 492,898

## Troubled Debt Restructurings

The Company may grant a concession or modification for economic or legal reasons related to a borrower's financial condition than it would not otherwise consider, resulting in a modified loan which is then identified as troubled debt restructuring ("TDR"). The Company may modify loans through rate reductions, extensions to maturity, interest only payments, or payment modifications to better coincide the timing of payments due under the modified terms with the expected timing of cash flows from the borrowers' operations. Loan modifications are intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. TDRs are considered impaired loans for purposes of calculating the Company's allowance for loan losses.

The Company identifies loans for potential restructure primarily through direct communication with the borrower and the evaluation of the borrower's financial statements, revenue projections, tax returns, and credit reports. Even if the borrower is not presently in default, management will consider the likelihood that cash flow shortages, adverse economic conditions, and negative trends may result in a payment default in the near future.

The following table presents TDRs outstanding:

<b>December 31, 2013</b>			
	<u>Accrual Loans</u>	<u>Non-Accrual Loans</u>	<u>Total Modifications</u>
(In Thousands)			
Commercial real estate	\$ 4,996	\$ 348	\$ 5,345
Commercial construction	1,901	-	1,901
Commercial	20	150	170
Residential real estate	1,137	-	1,137
Consumer	-	-	-
	<u>\$ 8,054</u>	<u>\$ 499</u>	<u>\$ 8,553</u>

As of December 31, 2013, no available commitments were outstanding on TDRs.

The following table presents newly restructured loans that occurred during the years ended December 31, 2013 and 2012:

	<u>Number of Loans</u>	<u>Pre-Modification Outstanding Balance</u>	<u>Post- Modification Outstanding Balance</u>
(Dollars in Thousands)			
<b>Year Ending December 31, 2013</b>			
Residential real estate	3	\$ 344	\$ 344
	<u>3</u>	<u>\$ 344</u>	<u>\$ 344</u>
<b>Year Ending December 31, 2012</b>			
Commercial real estate	4	\$ 1,247	\$ 1,247
Commercial construction	1	341	341
Commercial	1	3	3
Residential real estate	1	660	660
	<u>7</u>	<u>\$ 2,251</u>	<u>\$ 2,251</u>

Of the TDRs described above, one loan required an impairment reserve of \$30 thousand, which was recorded in the allowance for loan losses for the twelve months ended December 31, 2013, and two loans required an impairment

reserve of \$206 thousand recorded in the allowance for loan losses for the twelve months ended December 31, 2012. As of the years ended December 31, 2013 and 2012, no available commitments were outstanding on TDRs.

There were no loans that were modified and classified as a TDR within the prior twelve months that experienced a payment default (loans ninety or more days past due) during the twelve months ended December 31, 2013.

**Note 5 - Bank Premises and Equipment**

The components of premises and equipment at December 31, 2013 and 2012 are as follows:

	<b>2013</b>	<b>2012</b>
	(In Thousands)	
Furniture, fixtures and equipment	\$ 2,480	\$ 2,416
Leasehold improvements	2,125	2,115
Computer equipment and data processing software	1,529	1,274
Automobiles	166	166
Construction in progress	70	-
	<b>6,370</b>	5,971
Accumulated depreciation	<b>(4,488)</b>	<b>(3,876)</b>
	<b>\$ 1,882</b>	<b>\$ 2,095</b>

**Note 6 – Deposits**

The components of deposits at December 31, 2013 and 2012 are as follows:

	<b>December 31, 2013</b>	<b>December 31, 2012</b>
	(In Thousands)	
Demand, non-interest bearing	\$ 58,705	\$ 51,741
Demand, NOW and money market, interest bearings	59,451	61,638
Savings	389,613	381,012
Time, \$100 and over	26,488	23,409
Time, other	34,780	35,220
Total deposits	<b>\$ 569,037</b>	<b>\$ 553,020</b>

At December 31, 2013, the scheduled maturities of time deposits are as follows (in thousands):

2014	\$ 36,598
2015	11,867
2016	8,740
2017	1,954
2018	2,109
	<b>\$ 61,268</b>

**Note 7 - Securities Sold under Agreements to Repurchase**

Securities sold under agreements to repurchase generally mature within a few days from the transaction date and are reflected at the amount of cash received in connection with the transaction. The securities are retained under the Company's control at its safekeeping agent. The Company adjusts collateral based on the fair value of the underlying securities, on a monthly basis. Information concerning securities sold under agreements to repurchase for the years ended December 31, 2013 and 2012 is summarized as follows:

	<u>2013</u>	<u>2012</u>
	(Dollars In Thousands)	
Balance outstanding at December 31	\$ 30,418	\$ 24,452
Weighted average interest rate at the end of the year	0.057%	0.10%
Average daily balance during the year	\$ 29,687	\$ 31,638
Weighted average interest rate during the year	0.057%	0.20%
Maximum month-end balance during the year	\$ 33,982	\$ 40,842

**Note 8 – Short-term and Long-term Borrowings**

The Bank has borrowing capacity with the FHLB of Pittsburgh of approximately \$321.1 million, of which \$10 million was outstanding at December 31, 2013, at an interest rate of 0.24%, all of which were short term. This borrowing capacity with the FHLB includes a line of credit of \$25.0 million. The Bank also has a \$6.0 million line of credit with ACBB, of which none was outstanding at December 31, 2013 and 2012, respectively. Advances from the Federal Home Loan Bank line are secured by qualifying assets of the Bank and advances from the ACBB line are unsecured.

The Company has two lines of credit with Univest Bank and Trust Co., totaling \$10.0 million, of which \$3.9 million and \$4.7 million was outstanding at December 31, 2013 and 2012, respectively. These lines of credit are secured by 833,333 shares of Bank stock, subordinate to all senior indebtedness of the Company.

There were no long-term borrowings with the FHLB at December 31, 2013. The components of long-term borrowings with the FHLB at December 31, 2012 are as follows:

	<u>2012</u>	
	(Dollars in Thousands)	
Maturity Date	Interest Rate	Outstanding
June 2013	3.86%	4,834
August 2013	3.98%	3,052
		<u>\$ 7,886</u>

The components of long-term borrowings with Univest at December 31, 2013 and 2012 are as follows:

	2013		2012	
(Dollars in Thousands)				
Maturity Date	Interest Rate	Outstanding	Interest Rate	Outstanding
November 2015	7.50%	\$ <u>3,900</u>	7.50%	\$ <u>4,700</u>

#### Note 9 - Lease Commitments

The Company leases its banking premises under leases which the Company classifies as operating leases. These leases expire at various dates through March 2020. In addition to fixed rentals, the leases require the Company to pay certain additional expenses of occupying these spaces, including real estate taxes, insurance, utilities and repairs. A portion of these leases are with related parties as described below.

Future minimum lease payments by year and in the aggregate, under all lease agreements, are as follows:

	Related Parties	Third Parties	Total
(In Thousands)			
2014	\$ 403	\$ 763	\$ 1,166
2015	410	778	1,188
2016	403	795	1,198
2017	62	821	883
2018	-	842	842
Thereafter	-	734	734
	\$ <u>1,278</u>	\$ <u>4,733</u>	\$ <u>6,011</u>

Total rent expense was \$1.2 million and \$1.1 million for the years ended December 31, 2013 and 2012. Rent expense to related parties was \$405 thousand and \$368 thousand for the years ended December 31, 2013 and 2012, respectively.

#### Note 10 - Employment Agreements and Supplemental Executive Retirement Plans

The Company has entered into employment agreements with its Chief Executive Officer, Chief Financial Officer and Executive Vice President of Commercial Lending.

The Company has a non-qualified Supplemental Executive Retirement Plan ("SERP") for certain executive officers that provides for payments upon retirement, death or disability. As of December 31, 2013 and 2012, respectively, other liabilities include \$2.2 million and \$1.6 million, respectively, accrued under these plans. For the years ended December 31, 2013 and 2012, \$600 thousand and \$409 thousand, respectively, were expensed under these plans.

## **Note 11 - Stock Option and Stock Incentive Plans**

### **Stock Option Plan:**

In connection with the reorganization of the Bank into a holding company structure, the Company assumed the Bank's 2001 Stock Option Plan which was renamed the Embassy Bancorp, Inc. Option Plan (the "Plan"). The plan expired on May 10, 2011, and no new options may be granted under this plan. The Plan authorized the Board of Directors to grant options to officers, other employees and directors of the Company. The options granted under the Plan to directors were non-qualified options. The options granted under the Plan to officers and other employees were generally intended to be "incentive stock options," and are subject to the limitations under Section 422 of the Internal Revenue Code. Shares issued upon exercise of options under the Plan may be funded from authorized but unissued shares of the Company or shares purchased in the open market. All options granted under the Plan were subject to vesting requirements of not less than three years and the term shall not exceed ten years. The exercise price of the options granted was intended to reflect the fair market value of a share of common stock at the time of the grant.

### **Stock Incentive Plan:**

At the Company's annual meeting on June 16, 2010, the shareholders approved the Embassy Bancorp, Inc. 2010 Stock Incentive Plan (the "SIP"). The SIP authorizes the Board of Directors, or a committee authorized by the Board of Directors, to award a stock based incentive to (i) designated officers (including officers who are directors) and other designated employees at the Company and its subsidiaries, and (ii) non-employee members of the Board of Directors and advisors and consultants to the Company and its subsidiaries. The SIP provides for stock based incentives in the form of incentive stock options as provided in Section 422 of the Internal Revenue Code of 1986, non-qualified stock options, stock appreciation rights, restricted stock and deferred stock awards. The term of the option, the amount of time for the option to vest after grant, if any, and other terms and limitations will be determined at the time of grant. Options granted under the SIP may not have an exercise period that is more than ten years from the time the option is granted.

At inception, the aggregate number of shares available for issuance under the SIP was 500,000. The SIP provides for appropriate adjustments in the number and kind of shares available for grant or subject to outstanding awards under the SIP to avoid dilution in the event of merger, stock splits, stock dividends or other changes in the capitalization of the Company. The SIP expires on June 15, 2020. There were no awards granted under the SIP for the years ended December 31, 2011 and 2010. In January 2014, February 2013 and 2012, the Company granted 10,209, 8,764, and 7,992 shares of restricted stock, respectively, to certain members of its Board of Directors as compensation for their service in 2013, 2012 and 2011, respectively, in accordance with the Company's Non-employee Directors Compensation program adopted in October of 2010. Such compensation was accrued for as of December 31, 2013, 2012 and 2011. In February 2013 and 2012, the Company also granted stock options to purchase 29,742 and 52,611 shares of stock to certain executive officers in accordance with their respective employment agreements. Stock compensation expense related to these options was \$61 thousand and \$39 thousand for the year ended December 31, 2013 and 2012, respectively. At December 31, 2013, approximately \$92 thousand unrecognized cost to these stock options granted in 2013 and 2012 will be recognized over the next 2.05 and 1.15 years, respectively. The fair value of the options granted in 2013 and 2012 was determined with the following weighted average assumptions: dividend yield of 0%, risk free interest rate of 1.34% and 1.43%, respectively, expected life of 6.0 years and 7.5 years, respectively, and expected volatility of 28.79% and 31.10%, respectively. The weighted average fair value of options granted in 2013 and 2012 was \$2.14 per share and \$2.56 per share, respectively. In January 2014, the Company granted stock options to purchase 29,663 shares of stock to certain executive officers in accordance with their respective employment agreements.

Activities under these plans, related to stock options, are summarized as follows:

	Number of Options	Weighted Average Exercise Price
<b>Outstanding, December 31, 2011</b>	192,391	\$ 6.96
Granted	52,611	7.00
Exercised	(49,729)	3.91
Forfeited	(19,561)	5.87
<b>Outstanding, December 31, 2012</b>	<b>175,712</b>	<b>\$ 7.96</b>
Granted	29,742	7.00
Exercised	(43,617)	6.40
Forfeited	(12,145)	6.40
<b>Outstanding, December 31, 2013</b>	<b>149,692</b>	<b>\$ 8.35</b>
<b>Exercisable, December 31, 2013</b>	<b>84,877</b>	<b>\$ 9.38</b>

Stock options outstanding at December 31, 2013 are exercisable at prices ranging from \$7.00 to \$10.00 per share. The weighted-average remaining contractual life of options outstanding and exercisable at December 31, 2013 is 4.56 years. The weighted-average remaining contractual life of options outstanding and exercisable at December 31, 2012 was 3.52 years. At December 31, 2013, the aggregate intrinsic value of options outstanding and exercisable was \$9 thousand. The intrinsic value was determined by using the latest known sales price of the Company's common stock. For the years ending December 31, 2013 and 2012, the aggregate intrinsic value of options exercised was \$313 thousand and \$154 thousand, respectively.

The following table summarizes information about the range of exercise prices for stock options outstanding at December 31, 2013:

Range of Exercise Price	Weighted Average Exercise Price	Number Outstanding	Weighted Average Remaining Contractual Life (Years)	Number Exercisable
\$6.00 to \$7.00	7.00	82,353	7.50	17,538
\$9.00 to \$10.00	10.00	67,339	0.97	67,339
		<b>149,692</b>	<b>4.56</b>	<b>84,877</b>

**Note 12 – Other Comprehensive Income**

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income (loss).

The components of other comprehensive income (loss), both before tax and net of tax, are as follows:

	Year Ended December 31,					
	2013			2012		
	(In Thousands)					
	Before Tax	Tax Effect	Net of Tax	Before Tax	Tax Effect	Net of Tax
Other comprehensive (loss) income:						
Unrealized holding (losses) gains on available for sale	\$ (2,302)	\$ 783	\$ (1,519)	\$ 994	\$ (338)	\$ 656
Reclassification adjustments for gains on securities transactions						
in net income (A),(B)	(337)	114	(223)	(1,155)	393	(762)
Total other comprehensive loss	<u>\$ (2,639)</u>	<u>\$ 897</u>	<u>\$ (1,742)</u>	<u>\$ (161)</u>	<u>\$ 55</u>	<u>\$ (106)</u>

(A)Realized gains on securities transactions included in gain on sales of securities, net, in the accompanying Consolidated Statements of Income.

(B)Tax effect included in income tax expense in the accompanying Consolidated Statements of Income.

A summary of the realized gains on securities available for sale, net of tax, is as follows:

	Year Ended December 31,	
	2013	2012
	(In Thousands)	
Securities available for sale:		
Realized gains on securities transactions	\$ (337)	\$ (1,155)
Income taxes	114	393
Net of tax	<u>\$ (223)</u>	<u>\$ (762)</u>

A summary of the accumulated other comprehensive income, net of tax, is as follows:

	<b>Securities Available for Sale</b>
<b>Year Ended December 31, 2013</b>	
<b>Balance January 1, 2013</b>	<b>\$ 2,282</b>
Other comprehensive loss before reclassifications	(2,639)
Amounts reclassified from accumulated other comprehensive income	897
Net other comprehensive loss during the period	<u>(1,742)</u>
<b>Balance December 31, 2013</b>	<b><u>\$ 540</u></b>
<b>Balance January 1, 2012</b>	<b>\$ 2,388</b>
Other comprehensive income before reclassifications	(161)
Amounts reclassified from accumulated other comprehensive income	55
Net other comprehensive income during the period	<u>(106)</u>
<b>Balance December 31, 2012</b>	<b><u>\$ 2,282</u></b>

**Note 13 - Federal Income Taxes**

The components of income tax expense for the years ended December 31, 2013 and 2012 are as follows:

	<b>2013</b>	<b>2012</b>
	(In Thousands)	
Current	<b>\$ 2,597</b>	\$ 2,853
Deferred	<u>(456)</u>	<u>(628)</u>
	<b><u>\$ 2,141</u></b>	<b><u>\$ 2,225</u></b>

A reconciliation of the statutory federal income tax at a rate of 34% to the income tax expense included in the statement of income for the years ended December 31, 2013 and 2012 is as follows:

	<b>2013</b>	<b>2012</b>
	(In Thousands)	
Federal income tax at statutory rate	<b>\$ 2,606</b>	\$ 2,709
Tax free interest	<u>(437)</u>	<u>(490)</u>
Other	<u>(28)</u>	<u>6</u>
	<b><u>\$ 2,141</u></b>	<b><u>\$ 2,225</u></b>

The Company follows guidance in ASC Topic 740 regarding accounting for uncertainty in income taxes. The Company has evaluated its tax positions. A tax position is recognized as a benefit only if it is “more likely than not” that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that has a likelihood of being realized on examination of more than 50 percent. For tax positions not meeting the “more likely than not” test, no tax benefit is recorded. Under the “more likely than not” threshold guidelines, the Company believes no significant uncertain tax positions exist, either individually or in the aggregate, that would give rise to the non-recognition of an existing tax benefit. As of December 31, 2013 and 2012, the Company had no material unrecognized tax benefits or accrued interest and penalties. The Company’s policy is to account for interest as a component of interest expense and penalties as a component of other expense. The Company is subject to U.S. federal income tax. Neither the Company nor the Bank is subject to examination by U.S. Federal taxing authorities for years before 2010.

The components of the net deferred tax asset at December 31, 2013 and 2012 are as follows:

	2013	2012
	(In Thousands)	
Deferred tax assets:		
Allowance for loan losses	\$ 1,765	\$ 1,669
Accrued SERP	757	553
Other	368	209
<b>Total Deferred Tax Assets</b>	<b>2,890</b>	<b>2,431</b>
Deferred tax liabilities:		
Premises and equipment	44	95
Prepaid assets	245	223
Deferred loan costs	295	263
Unrealized gain on securities available for sale	278	1,175
<b>Total Deferred Tax Liabilities</b>	<b>\$ 862</b>	<b>\$ 1,756</b>
<b>Net Deferred Tax Asset (Liability)</b>	<b>\$ 2,028</b>	<b>\$ 675</b>

Based upon the level of historical taxable income and projections for future taxable income over periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences.

**Note 14 - Transactions with Executive Officers, Directors and Principal Stockholders**

The Company has had, and may be expected to have in the future, banking transactions in the ordinary course of business with its executive officers, directors, principal stockholders, their immediate families and affiliated companies (commonly referred to as related parties), on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others.

Related parties were indebted to the Company for loans totaling \$2.9 million and \$2.6 million at December 31, 2013 and 2012, respectively. During 2013, loans totaling \$978 thousand were disbursed and loan repayments totaled \$678 thousand.

Fees paid to related parties for legal services for the years ended December 31, 2013 and 2012 were approximately \$58 thousand and \$39 thousand, respectively. The Company leases its main banking office from an investment group comprised of related parties and its West Broad Street office also from a related party, as described in Note 9.

**Note 15 - Financial Instruments with Off-Balance Sheet Risk**

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheets.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

At December 31, 2013 and 2012, the following financial instruments were outstanding whose contract amounts represent credit risk:

	2013	2012
	(In Thousands)	
Commitments to grant loans, fixed	\$ 6,195	\$ 5,285
Commitments to grant loans, variable	2,324	8,994
Unfunded commitments under lines of credit, fixed	14,152	16,377
Unfunded commitments under lines of credit, variable	57,481	60,627
Standby letters of credit	4,748	4,994
	<u>\$ 84,900</u>	<u>\$ 96,277</u>

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation.

Collateral held varies but may include personal or commercial real estate, accounts receivable, inventory and equipment.

Outstanding letters of credit written are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. The majority of these standby letters of credit expire within the next twelve months. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending other loan commitments. The Company requires collateral supporting these letters of credit as deemed necessary. The maximum undiscounted exposure related to these commitments at December 31, 2013 and 2012 was \$4.7 million and \$5.0 million, respectively, and the approximate value of underlying collateral upon liquidation that would be expected to cover this maximum potential exposure was \$4.2 million and \$4.5 million, respectively. The current amount of the liability as of December 31, 2013 and 2012 for guarantees under standby letters of credit issued is not considered material.

#### **Note 16 - Regulatory Matters**

The Company is required to maintain cash reserve balances in vault cash and with the Federal Reserve Bank. As of December 31, 2013, the Company had a \$1.9 million minimum reserve balance.

The Company and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet the minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, both the Company and the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification 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 the Company and the Bank to maintain minimum amounts and ratios (set forth below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets and of Tier 1 capital to average assets. Management believes, as of December 31, 2013, that the Company and the Bank meet all capital adequacy requirements to which it is subject.

As of December 31, 2013, the most recent notification from the regulatory agencies categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table below. There are no conditions or events since that notification that management believes have changed the Bank's category.

The Bank's actual capital amounts and ratios at December 31, 2013 and 2012 are presented below:

	Actual		For Capital Adequacy Purposes		To be Well Capitalized under Prompt Corrective Action	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollar Amounts in Thousands)						
<b>December 31, 2013:</b>						
Total capital (to risk-weighted assets)	\$ 62,146	13.2 %	\$ ≥ 37,748	≥ 8.0 %	\$ ≥ 47,185	≥ 10.0 %
Tier 1 capital (to risk-weighted assets)	56,820	12.0	≥ 18,874	≥ 4.0	≥ 28,311	≥ 6.0
Tier 1 capital (to average assets)	56,820	8.5	≥ 26,736	≥ 4.0	≥ 33,420	≥ 5.0
<b>December 31, 2012:</b>						
Total capital (to risk-weighted assets)	\$ 57,193	13.3 %	\$ ≥ 34,400	≥ 8.0 %	\$ ≥ 43,000	≥ 10.0 %
Tier 1 capital (to risk-weighted assets)	52,046	12.1	≥ 17,200	≥ 4.0	≥ 25,800	≥ 6.0
Tier 1 capital (to average assets)	52,046	8.0	≥ 25,999	≥ 4.0	≥ 32,498	≥ 5.0

The Company's actual capital amounts and ratios at December 31, 2013 and 2012 are presented below:

	Actual		For Capital Adequacy Purposes	
	Amount	Ratio	Amount	Ratio
(Dollar Amounts in Thousands)				
<b>December 31, 2013:</b>				
Total capital (to risk-weighted assets)	\$ 58,841	12.5 %	\$ ≥ 37,526	≥ 8.0 %
Tier 1 capital (to risk-weighted assets)	53,515	11.3	≥ 18,763	≥ 4.0
Tier 1 capital (to average assets)	53,515	7.9	≥ 26,943	≥ 4.0
<b>December 31, 2012:</b>				
Total capital (to risk-weighted assets)	\$ 52,892	12.3 %	\$ ≥ 34,401	≥ 8.0 %
Tier 1 capital (to risk-weighted assets)	47,745	11.1	≥ 17,200	≥ 4.0
Tier 1 capital (to average assets)	47,745	7.3	≥ 26,223	≥ 4.0

The Bank is subject to certain restrictions on the amount of dividends that it may declare due to regulatory considerations. The Pennsylvania Banking Code provides that cash dividends may be declared and paid only out of accumulated net earnings.

**Note 17 – Offsetting Assets and Liabilities**

The Company enters into agreements under which it sells securities subject to an obligation to repurchase the same or similar securities. Under these arrangements, the Company may transfer legal control over the assets but still retain effective control through an agreement that both entitles and obligates the Company to repurchase the assets. As a result, these repurchase agreements are accounted for as collateralized financing arrangements (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 Company'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 Company 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 Company 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 Company 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 Company 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 December 31, 2013 and December 31, 2012:

	Gross		Net Amounts			
	Amounts	Offset in the	of Liabilities			
	Recognized	Consolidated	Consolidated	Financial	Cash	
	Liabilities	Balance	Balance	Instruments	Pledged	Net
(In Thousands)						
<b>December 31, 2013</b>						
Repurchase Agreements:						
Corporate Institutions	\$ 30,418	\$ -	\$ 30,418	\$ (30,418)	\$ -	\$ -
<b>December 31, 2012</b>						
Repurchase Agreements:						
Corporate Institutions	\$ 24,452	\$ -	\$ 24,452	\$ (24,452)	\$ -	\$ -

As of December 31, 2013 and December 31, 2012, the fair value of securities pledged was \$34.3 million and \$35.1 million, respectively.

**Note 18 - Fair Value of Financial Instruments**

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

Fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

ASC Topic 860 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 under ASC Topic 860 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's 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 financial assets measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy utilized at December 31, 2013 and 2012 are as follows:

Description	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs	Total
	(In Thousands)			
U.S. Government agency obligations	\$ -	\$ 27,005	\$ -	\$ 27,005
Municipal bonds	-	32,900	-	32,900
U.S. Government Sponsored Enterprise (GSE) - Mortgage-backed securities - residential	-	9,362	-	9,362
Corporate bonds	-	2,021	-	2,021
<b>December 31, 2013 Securities available for sale</b>	<b>\$ -</b>	<b>\$ 71,288</b>	<b>\$ -</b>	<b>\$ 71,288</b>
U.S. Government agency obligations	\$ -	40,605	\$ -	40,605
Municipal bonds	-	38,952	-	38,952
U.S. Government Sponsored Enterprise (GSE) - Mortgage-backed securities - residential	-	9,017	-	9,017
Corporate bonds	-	3,283	-	3,283
<b>December 31, 2012 Securities available for sale</b>	<b>\$ -</b>	<b>\$ 91,857</b>	<b>\$ -</b>	<b>\$ 91,857</b>

For financial assets measured at fair value on a nonrecurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2013 and 2012 are as follows:

Description	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs	Total
(In Thousands)				
December 31, 2013 Impaired loans (1)	\$ -	\$ -	\$ 1,102	\$ 1,102
December 31, 2013 Impaired loans (2)	\$ -	\$ -	\$ 499	\$ 499
December 31, 2013 Other real estate owned (1)	\$ -	\$ -	\$ 659	\$ 659
December 31, 2012 Impaired loans (1)	\$ -	\$ -	\$ 2,006	\$ 2,006
December 31, 2012 Impaired loans (2)	\$ -	\$ -	\$ 1,048	\$ 1,048
December 31, 2012 Other real estate owned (1)	\$ -	\$ -	\$ 3,038	\$ 3,038

(1) Fair Value is generally determined through independent appraisals of the underlying collateral, which generally include various Level 3 input which are not identifiable. Fair values may also include qualitative adjustments by management based on economic conditions and liquidation expenses.

(2) Fair Value determined using the debt service of the borrower.

Impaired loans are those that are accounted for under existing FASB guidance, in which the Bank has measured impairment 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.

Real estate properties acquired through, or in lieu of, foreclosure are to be sold and are carried at fair value less estimated cost to sell. Fair value is based upon independent market prices or appraised value of the property. These assets are included in Level 3 fair value based upon the lowest level of input that is significant to the fair value measurement.

At December 31, 2013, of the impaired loans having an aggregate balance of \$12.0 million, \$10.0 million did not require a valuation allowance because the value of the collateral securing the loan was determined to meet or exceed the balance owed on the loan. Of the remaining \$2.0 million in impaired loans, an aggregate valuation allowance of \$405 thousand was required to reflect what was determined to be a shortfall in the value of the collateral as compared to the balance on such loans.

Real estate properties acquired through, or in lieu of, foreclosure are to be sold and are carried at fair value less estimated cost to sell. Fair value is based upon independent market prices or appraised value of the property. These assets are included in Level 3 fair value based upon the lowest level of input that is significant to the fair value measurement.

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

Quantitative Information about Level 3 Fair Value Measurements				
Description	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range (Weighted Average)
(Dollars In Thousands)				
<b>December 31, 2013:</b>				
Impaired loans	\$ 1,102	Appraisal of collateral (1)	Appraisal adjustments (2)	0% to -25% (-15.7%)
			Liquidation expenses (3)	0 to -10% (-8.4%)
Impaired loans	\$ 499	Discounted Cash Flows (5)		
Other real estate owned	\$ 659	Listings, Letters of Intent & Third Party Evaluations (4)	Liquidation expenses (3)	-5% (-5%)

- (1) Fair value is generally determined through independent appraisals of the underlying collateral, which generally include Level 3 inputs which are not identifiable.
- (2) Appraisals may be adjusted by management for qualitative factors including economic conditions and the age of the appraisal. The range and weighted average of appraisal adjustments are presented as a percent of the appraisal.
- (3) Appraisals and pending agreements of sale are adjusted by management for liquidation expenses. The range and weighted liquidation expense adjustments are presented as a percent of the appraisal or pending agreement of sale.
- (4) Fair value is determined by listings, letters of intent or third-party evaluations.
- (5) Fair value is determined using the debt service of the borrower.

The following information should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only provided for a limited portion of the Company'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 Company'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 Company's financial instruments at December 31, 2013 and December 31, 2012:

#### Cash and Cash Equivalents (Carried at Cost)

The carrying amounts reported in the balance sheet for cash and short-term instruments approximate those assets' fair values.

#### Interest Bearing Time Deposits (Carried at Cost)

Fair values for fixed-rate time certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered in the market on certificates to a schedule of aggregated expected monthly maturities on time deposits. The Company generally purchases amounts below the insured limit, limiting the amount of credit risk on these time deposits.

**Securities Available for Sale (Carried at Fair Value)**

The fair value of securities available for sale are determined 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 securities, but rather by relying on the securities' relationship to other benchmark quoted prices. For these securities, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the security's terms and conditions, among other things.

**Loans Receivable (Carried at Cost)**

The fair values of loans, excluding impaired loans carried at fair value of collateral, are estimated using discounted cash flow analyses, 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, and 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.

**Restricted Investment in Bank Stock (Carried at Cost)**

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

**Accrued Interest Receivable and Payable (Carried at Cost)**

The carrying amount of accrued interest receivable and accrued interest payable approximates its fair value.

**Deposit Liabilities (Carried at Cost)**

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

**Securities Sold Under Agreements to Repurchase and Short-term Borrowings (Carried at Cost)**

These borrowings are short term and the carrying amount approximates the fair value.

**Long-Term Borrowings (Carried at Cost)**

Fair values of FHLB and Uninvest advances are estimated using discounted cash flow analysis, based on quoted prices for new FHLB and Uninvest advances with similar credit risk characteristics, terms and remaining maturity. These 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 Financial Instruments (Disclosed at Cost)**

Fair values for the Company'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 estimated fair values of the Company's financial instruments were as follows at December 31, 2013 and 2012:

	Carrying Amount	Fair Value Estimate	(Level 1) Quoted Prices in Active Markets for Identical	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
(In Thousands)					
<b>December 31, 2013:</b>					
Financial assets:					
Cash and cash equivalents	\$ 17,831	\$ 17,831	\$ 17,831	\$ -	\$ -
Interest bearing time deposits	1,822	1,830	-	1,830	-
Securities available-for-sale	71,288	71,288	-	71,288	-
Loans receivable, net of allowance	563,257	563,444	-	-	563,444
Restricted investments in bank stock	2,157	2,157	-	2,157	-
Accrued interest receivable	1,533	1,533	-	1,533	-
Financial liabilities:					
Deposits	569,037	569,400	-	569,400	-
Securities sold under agreements to repurchase and federal funds purchased	30,418	30,415	-	30,415	-
Short-term borrowings	10,000	10,000	-	10,000	-
Long-term borrowings	3,900	3,797	-	-	3,797
Accrued interest payable	235	235	-	235	-
Off-balance sheet financial instruments:					
Commitments to grant loans	-	-	-	-	-
Unfunded commitments under lines of credit	-	-	-	-	-
Standby letters of credit	-	-	-	-	-
<b>December 31, 2012:</b>					
Financial assets:					
Cash and cash equivalents	\$ 29,940	\$ 29,940	\$ 29,940	\$ -	\$ -
Interest bearing time deposits	5,945	5,977	-	5,977	-
Securities available-for-sale	91,857	91,857	-	91,857	-
Loans receivable, net of allowance	500,072	508,053	-	-	508,053
Restricted investments in bank stock	1,454	1,454	-	1,454	-
Accrued interest receivable	1,578	1,578	-	1,578	-
Financial liabilities:					
Deposits	553,020	553,756	-	553,756	-
Securities sold under agreements to repurchase and federal funds purchased	24,452	24,452	-	24,452	-
Long-term borrowings	12,586	12,708	-	-	12,708
Accrued interest payable	327	327	-	327	-
Off-balance sheet financial instruments:					
Commitments to grant loans	-	-	-	-	-
Unfunded commitments under lines of credit	-	-	-	-	-
Standby letters of credit	-	-	-	-	-

**Note 19 – Parent Company Only Financial**

Condensed financial information pertaining only to the parent company, Embassy Bancorp, Inc., is as follows:

**BALANCE SHEETS**

	As of December 31,	
	2013	2012
(In Thousands)		
<b><u>ASSETS</u></b>		
Cash	\$ 749	\$ 520
Other assets	16	19
Investment in subsidiary	57,359	54,328
Total Assets	<u>\$ 58,124</u>	<u>\$ 54,867</u>
<b><u>LIABILITIES AND STOCKHOLDERS' EQUITY</u></b>		
Long-term borrowings	\$ 3,900	\$ 4,700
Other liabilities	169	140
Stockholders' equity	54,055	50,027
Total Liabilities and Stockholders' Equity	<u>\$ 58,124</u>	<u>\$ 54,867</u>

**STATEMENTS OF INCOME AND COMPREHENSIVE INCOME**

	Years Ending December 31,	
	2013	2012
(In Thousands)		
Interest expense on borrowings	\$ (334)	\$ (387)
Other expenses	(313)	(333)
Equity in net income of banking subsidiary	5,958	6,227
Income before income taxes	5,311	5,507
Income tax benefit	212	236
Net income	<u>\$ 5,523</u>	<u>\$ 5,743</u>
Equity in other comprehensive loss of banking subsidiary	(1,742)	(106)
Comprehensive income	<u>\$ 3,781</u>	<u>\$ 5,637</u>

STATEMENT OF CASH FLOWS

	Years Ending December 31,	
	2013	2012
	(In Thousands)	
<b>Cash Flows from Operating Activities:</b>		
Net income	\$ 5,523	\$ 5,743
Adjustments to reconcile net income to net cash provided by operating activities:		
Net change in other assets and liabilities	94	67
Equity in net income of banking subsidiary	(5,958)	(6,227)
<b>Net Cash Used in Operating Activities</b>	<b>(341)</b>	<b>(417)</b>
<b>Cash Flows from Investing Activities:</b>		
Dividend from banking subsidiary	1,250	891
<b>Net Cash Provided by Investing Activities</b>	<b>1,250</b>	<b>891</b>
<b>Cash Flows from Financing Activities:</b>		
Repayment of long-term borrowings	(800)	(500)
Exercise of stock options, net of payment stock tendered and proceeds from DRIP	483	121
Dividends Paid	(363)	(182)
<b>Net Cash Used in Financing Activities</b>	<b>(680)</b>	<b>(561)</b>
<b>Net (Decrease) Increase in Cash</b>	<b>229</b>	<b>(87)</b>
<b>Cash – Beginning</b>	<b>520</b>	<b>607</b>
<b>Cash - Ending</b>	<b>\$ 749</b>	<b>\$ 520</b>

**Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.**

None.

**Item 9A. CONTROLS AND PROCEDURES.**

(a) Disclosure Controls and Procedures.

The Company maintains controls and procedures designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission. Based upon their evaluation of those controls and procedures as of December 31, 2013, the Chief Executive and Chief Financial Officers of the Company concluded that the Company's disclosure controls and procedures were effective.

(b) Management's Report on Internal Control Over Financial Reporting.

Management is responsible for establishing and maintaining effective internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f) under the Securities Exchange Act of 1934. Under the supervision and with the participation of the principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our control over financial reporting based on the original Internal Control- Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on our evaluation under the framework, management has concluded that our internal control over financial reporting was effective as of December 31, 2013.

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David M. Lobach, Jr.  
Chairman, President and Chief Executive Officer

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Judith A. Hunsicker  
Senior Executive Vice President, Chief Operating  
Officer, Secretary and Chief Financial Officer

This annual report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to provisions of the Dodd-Frank Act, which exempt smaller reporting companies from this requirement, thus permitting the Company to provide only management's report in this annual report.

(c) Changes in Internal Controls Over Financial Reporting.

There have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the final fiscal quarter of the year to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Item 9B. OTHER INFORMATION.**

None.

**PART III**

**Item 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE.**

The information required by Part III, Item 10, is incorporated herein by reference to the information under the captions “Board of Directors,” “Information as to Nominees and Directors,” “Executive Officers,” “Nominating Process,” “Code of Conduct (Ethics),” “Committees of the Board” and “Section 16(a) Beneficial Ownership Reporting Compliance” in the Company’s definitive proxy statement to be filed with the SEC in connection with the Company’s 2014 annual meeting of shareholders.

**Item 11. EXECUTIVE COMPENSATION.**

The information required by Part III, Item 11, is incorporated herein by reference to the information under the captions “Director Compensation,” “Executive Compensation” and “Agreements with Executive Officers” in the Company’s definitive proxy statement to be filed with the SEC in connection with the Company’s 2014 annual meeting of shareholders.

**Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.**

The information required by Part III, Item 12, is incorporated herein by reference to the information under Item 5 of this report and the information under the caption “Information Concerning Share Ownership” in the Company’s definitive proxy statement to be filed with the SEC in connection with the Company’s 2014 annual meeting of shareholders.

**Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE.**

The information required by Part III, Item 13, is incorporated herein by reference to the information under the captions “Certain Relationships and Related Transactions” and “Director Independence” in the Company’s definitive proxy statement to be filed with the SEC in connection with the Company’s 2014 annual meeting of shareholders.

**Item 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.**

The following fees were incurred by the Company for 2013 and 2012:

	<b>2013</b>	<b>2012</b>
Audit fees (1)	\$ <b>75,745</b>	\$ 74,467
Audit -related fees	-	2,591
Tax fees (3)	<b>15,673</b>	9,163
All other fees (4)	-	45,695
	<b><u>\$ 91,418</u></b>	<b><u>\$ 131,916</u></b>

(1) Includes professional services rendered for the audit of the Company's annual financial statements and review of financial statements included in Forms 10-Q and 10-K, or services normally provided in connection with statutory and regulatory filing and engagements, including out-of-pocket expenses.

(2) Includes assurance and related services reasonably related to the performance of the audit or review of financial statements.

(3) Tax fees include the following: preparation of state and federal tax returns and consultation on various other tax matters.

(4) Other fees include assistance in implementing XBRL reporting.

These fees were approved in accordance with the Company's Audit Committee's policy.

Additional information required by Part III, Item 14, is incorporated herein by reference to the information under the captions "Fees Paid to Independent Accountants" and "Report of Audit Committee" in the Company's definitive proxy statement to be filed with the SEC in connection with the Company's 2014 annual meeting of shareholders.

**Part IV**

**Item 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES.**

- (a) Financial Statement Schedules can be found under Item 8 of this report.
- (b) Exhibits required by Item 601 of Regulation S-K:

Exhibit

Number

Description

- |       |   |
|-------|---|
| 3.1   | Articles of Incorporation, as amended (conformed) (Incorporated by reference to Exhibit 3.1 of Registrants Form 10-Q filed on May 14, 2010).  |
| 3.2   | By-Laws (Incorporated by reference to Exhibit 2 of Registrant’s Form 8-A filed on December 11, 2008).   |
| 10.1  | Embassy Bancorp, Inc. Dividend Reinvestment and Stock Purchase Plan (Incorporated by reference to Exhibit 99.1 of Registrant’s Registration Statement on Form S-3 filed on June 18, 2012).  |
| 10.2  | Embassy Bancorp, Inc. Option Plan (Incorporated by reference to Exhibit 10.1 of Registrant’s Registration Statement on Form S-8 filed on February 22, 2010).  |
| 10.3  | Embassy Bancorp, Inc. 2010 Stock Incentive Plan (Incorporated by reference to Annex A of Registrant’s definitive proxy statement filed on April 30, 2010).  |
| 10.4  | Form of Stock Option Grant Agreement – Directors (Incorporated by reference to Exhibit 10.1 of Registrant’s Form 10-Q filed on May 14, 2010).   |
| 10.5  | Form of Stock Option Grant Agreement – Executive Officers (Incorporated by reference to Exhibit 10.2 of Registrant’s Form 10-Q filed on May 14, 2010).  |
| 10.6  | Lease Agreement for the Rte. 512 Bethlehem Office (Incorporated by reference to Exhibit 10.2 of Registrant’s Form 10-K filed on March 31, 2009).  |
| 10.7  | Lease Agreement dated October 21, 2005 for Hamilton Blvd. and Mill Creek Rd., Lower Macungie Township, Pennsylvania (Incorporated by reference to Exhibit 10.3 of Registrant’s Form 10-K filed on March 31, 2009).                    |
| 10.8  | Lease Addendum for additional space in the Rte. 512, Bethlehem Office (Incorporated by reference to Exhibit 10.4 of Registrant’s Form 10-K filed on March 31, 2009).  |
| 10.9  | Lease Agreement dated March 11, 2009 for Cedar Crest Blvd., Allentown, Pennsylvania (Incorporated by reference to Exhibit 10.5 of Registrant’s Form 10-K filed on March 31, 2009).  |
| 10.10 | Lease Agreement for Tilghman Street location (Incorporated by reference to Exhibit 10.6 of Registrant’s Form 10-K filed on March 31, 2009).   |
| 10.11 | Lease Agreement dated March 17, 2006 for 925 West Broad St, Bethlehem PA (Incorporated by reference to Exhibit 10.7 of Registrant’s Form 10-K filed on March 31, 2009).   |
| 10.12 | Lease Agreement dated June 17, 2008 for 5828 Old Bethlehem Pike, Center Valley, PA (Incorporated by reference to Exhibit 10.8 of Registrant’s Form 10-K filed on March 31, 2009).   |
| 10.13 | Lease Agreement dated March 19, 2009 for Corriere Road and Route 248 in Lower Nazareth Township, PA (Incorporated by reference to Exhibit 10.9 of Registrant’s Form 10-K filed on March 31, 2009).                                    |
| 10.14 | Second Lease Expansion Addendum dated October 21, 2011 by and between Embassy Bank for the Lehigh Valley and Red Bird Associates, LLC (Incorporated by reference to Exhibit 10.1 of Registrant’s Form 8-K filed on October 26, 2011). |
| 10.15 | Lease Renewal and Modification Agreement dated May 4, 2012 by and between Embassy Bank for the Lehigh Valley and Red Bird Associates LLC (Incorporated by reference to Exhibit 10.1 of registrant’s Form 8-K filed on May 7, 2012).   |
| 10.16 | Employment Agreement – D. Lobach, dated January 1, 2006 (Incorporated by reference to Exhibit 10.10 of Registrant’s Form 10-K filed on March 31, 2009).   |
| 10.17 | Amendment to Employment Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated November 19, 2010 (Incorporated by reference to Exhibit 10.5 of Registrant’s Form 8-K filed on November 23, 2010).       |
| 10.18 | Employment Agreement – J. Hunsicker, dated January 1, 2006 (Incorporated by reference to Exhibit 10.11 of Registrant’s Form 10-K filed on March 31, 2009).  |

**Item 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES. (Continued)**

<u>Exhibit</u>	
<u>Number</u>	<u>Description</u>
10.19	Amendment to Employment Agreement between Embassy Bank for the Lehigh Valley and Judith A. Hunsicker, dated November 19, 2010 (Incorporated by reference to Exhibit 10.6 of Registrant's Form 8-K filed on November 23, 2010).
10.20	Employment Agreement – J. Bartholomew, dated February 20, 2009 (Incorporated by reference to Exhibit 10.12 of Registrant's Form 10-K filed on March 31, 2009).
10.21	Amendment to Employment Agreement between Embassy Bank for the Lehigh Valley and James R. Bartholomew, dated November 19, 2010 (Incorporated by reference to Exhibit 10.7 of Registrant's Form 8-K filed on November 23, 2010).
10.22	Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated November 19, 2010 (Incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed on November 23, 2010).
10.23	Amendment No. 1 to Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated November 21, 2011 (Incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed on November 23, 2011).
10.24	Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated November 19, 2010 (Incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed on November 23, 2010).
10.25	Amendment No. 2 to Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated January 1, 2013 (Incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed on January 2, 2013).
10.26	Amendment No. 3 to Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated January 23, 2014 (Incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed on January 24, 2014).
10.27	Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and Judith A. Hunsicker, dated November 19, 2010 (Incorporated by reference to Exhibit 10.3 of Registrant's Form 8-K filed on November 23, 2010).
10.28	Amendment No. 2 to Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and Judith A. Hunsicker, dated January 1, 2013 (Incorporated by reference to Exhibit 10.3 of Registrant's Form 8-K filed on January 2, 2013).
10.29	Amendment No. 3 to Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and Judith A. Hunsicker, dated January 23, 2014 (Incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed on January 24, 2014).
10.30	Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and James R. Bartholomew, dated November 19, 2010 (Incorporated by reference to Exhibit 10.4 of Registrant's Form 8-K filed on November 23, 2010).
10.31	Amendment No. 2 to Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and James R. Bartholomew, dated January 1, 2013 (Incorporated by reference to Exhibit 10.4 of Registrant's Form 8-K filed on January 2, 2013).
10.32	Amendment No. 3 to Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and James R. Bartholomew, dated January 23, 2014 (Incorporated by reference to Exhibit 10.3 of Registrant's Form 8-K filed on January 24, 2014).
10.33	Loan Agreement, dated as of December 22, 2009, by and between Embassy Bancorp, Inc. and Univest National Bank and Trust Co. (Incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed on December 24, 2009).
10.34	Subordinated Term Loan Note, dated as of December 22, 2009, by Embassy Bancorp, Inc. in favor of Univest National Bank and Trust Co. (Incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed on December 24, 2009).

**Item 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES. (Continued)**

<u>Exhibit</u>	
<u>Number</u>	<u>Description</u>
10.35	Stock Pledge Agreement, dated as of December 22, 2009, by and between Embassy Bancorp, Inc. and Univest National Bank and Trust Co. (Incorporated by reference to Exhibit 10.3 of Registrant's Form 8-K filed on December 24, 2009).
10.36	Loan Agreement, dated as of November 11, 2008, by and between Embassy Bancorp, Inc. and Univest National Bank and Trust Co. (Incorporated by reference to Exhibit 10.4 of Registrant's Form 8-K filed on December 24, 2009).
10.37	Subordinated Term Loan Note, dated as of November 11, 2008, by Embassy Bancorp, Inc. in favor of Univest National Bank and Trust Co. (Incorporated by reference to Exhibit 10.5 of Registrant's Form 8-K filed on December 24, 2009).
10.38	Stock Pledge Agreement, dated as of November 11, 2008, by and between Embassy Bancorp, Inc. and Univest National Bank and Trust Co. (Incorporated by reference to Exhibit 10.6 of Registrant's Form 8-K filed on December 24, 2009).
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11.1	The statement regarding computation of per share earnings required by this exhibit is contained in Note 5 to the financial statements captions "Basic and Diluted Earnings Per Share."
21.1	Subsidiaries of the Registrant.
23.1	Consent of ParenteBeard LLC.
31.1	Certification of Principal Executive Officer pursuant to Rule 13a-14(a)/15d-14(a).
31.2	Certification of Principal Financial Officer pursuant to Rule 13a-14(a)/15d-14(a).
32.1	Certification of Principal Executive Officer and Principal Financial Officer pursuant to Section 1350 of the Sarbanes-Oxley Act of 2002.
101.1	XBRL - Related Documents
	No.          Description
101. INS	XBRL Instance Document.
101. SCH	XBRL Taxonomy Extension Schema Document.
101. CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101. LAB	XBRL Taxonomy Extension Label Linkbase Document.
101. PRE	XBRL Taxonomy Extension Presentation Linkbase Document.
101. DEF	XBRL Taxonomy Extension Definitions Linkbase Document.

**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 in its behalf by the undersigned, thereunto duly authorized.

EMBASSY BANCORP, INC.

Dated: March 28, 2014

By: /s/ David M. Lobach Jr.  
David M. Lobach, Jr.  
Chairman, President and Chief Executive Officer

Dated: March 28, 2014

By: /s/ Judith A. Hunsicker  
Judith A. Hunsicker  
Senior Executive Vice President, Chief Operating  
Officer, Secretary and Chief Financial Officer



**EXHIBIT INDEX**

<u>Exhibit</u>	
<u>Number</u>	<u>Description</u>
3.1	Articles of Incorporation, as amended (conformed) (Incorporated by reference to Exhibit 3.1 of Registrants Form 10-Q filed on May 14, 2010).
3.2	By-Laws (Incorporated by reference to Exhibit 2 of Registrant’s Form 8-A filed on December 11, 2008).
10.1	Embassy Bancorp, Inc. Dividend Reinvestment and Stock Purchase Plan (Incorporated by reference to Exhibit 99.1 of Registrant's Registration Statement on Form S-3 filed on June 18, 2012).
10.2	Embassy Bancorp, Inc. Option Plan (Incorporated by reference to Exhibit 10.1 of Registrant’s Registration Statement on Form S-8 filed on February 22, 2010).
10.3	Embassy Bancorp, Inc. 2010 Stock Incentive Plan (Incorporated by reference to Annex A of Registrant’s definitive proxy statement filed on April 30, 2010).
10.4	Form of Stock Option Grant Agreement – Directors (Incorporated by reference to Exhibit 10.1 of Registrant’s Form 10-Q filed on May 14, 2010).
10.5	Form of Stock Option Grant Agreement – Executive Officers (Incorporated by reference to Exhibit 10.2 of Registrant’s Form 10-Q filed on May 14, 2010).
10.6	Lease Agreement for the Rte. 512 Bethlehem Office (Incorporated by reference to Exhibit 10.2 of Registrant’s Form 10-K filed on March 31, 2009).
10.7	Lease Agreement dated October 21, 2005 for Hamilton Blvd. and Mill Creek Rd., Lower Macungie Township, Pennsylvania (Incorporated by reference to Exhibit 10.3 of Registrant’s Form 10-K filed on March 31, 2009).
10.8	Lease Addendum for additional space in the Rte. 512, Bethlehem Office (Incorporated by reference to Exhibit 10.4 of Registrant’s Form 10-K filed on March 31, 2009).
10.9	Lease Agreement dated March 11, 2009 for Cedar Crest Blvd., Allentown, Pennsylvania (Incorporated by reference to Exhibit 10.5 of Registrant’s Form 10-K filed on March 31, 2009).
10.10	Lease Agreement for Tilghman Street location (Incorporated by reference to Exhibit 10.6 of Registrant’s Form 10-K filed on March 31, 2009).
10.11	Lease Agreement dated March 17, 2006 for 925 West Broad St, Bethlehem PA (Incorporated by reference to Exhibit 10.7 of Registrant’s Form 10-K filed on March 31, 2009).
10.12	Lease Agreement dated June 17, 2008 for 5828 Old Bethlehem Pike, Center Valley, PA (Incorporated by reference to Exhibit 10.8 of Registrant’s Form 10-K filed on March 31, 2009).
10.13	Lease Agreement dated March 19, 2009 for Corriere Road and Route 248 in Lower Nazareth Township, PA (Incorporated by reference to Exhibit 10.9 of Registrant’s Form 10-K filed on March 31, 2009).
10.14	Second Lease Expansion Addendum dated October 21, 2011 by and between Embassy Bank for the Lehigh Valley and Red Bird Associates, LLC (Incorporated by reference to Exhibit 10.1 of Registrant’s Form 8-K filed on October 26, 2011).
10.15	Lease Renewal and Modification Agreement dated May 4, 2012 by and between Embassy Bank for the Lehigh Valley and Red Bird Associates LLC (Incorporated by reference to Exhibit 10.1 of registrant's Form 8-K filed on May 7, 2012).
10.16	Employment Agreement – D. Lobach, dated January 1, 2006 (Incorporated by reference to Exhibit 10.10 of Registrant’s Form 10-K filed on March 31, 2009).
10.17	Amendment to Employment Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated November 19, 2010 (Incorporated by reference to Exhibit 10.5 of Registrant’s Form 8-K filed on November 23, 2010).
10.18	Employment Agreement – J. Hunsicker, dated January 1, 2006 (Incorporated by reference to Exhibit 10.11 of Registrant’s Form 10-K filed on March 31, 2009).

EXHIBIT INDEX (Continued)

<u>Exhibit</u> <u>Number</u>	<u>Description</u>
10.19	Amendment to Employment Agreement between Embassy Bank for the Lehigh Valley and Judith A. Hunsicker, dated November 19, 2010 (Incorporated by reference to Exhibit 10.6 of Registrant's Form 8-K filed on November 23, 2010).
10.20	Employment Agreement – J. Bartholomew, dated February 20, 2009 (Incorporated by reference to Exhibit 10.12 of Registrant's Form 10-K filed on March 31, 2009).
10.21	Amendment to Employment Agreement between Embassy Bank for the Lehigh Valley and James R. Bartholomew, dated November 19, 2010 (Incorporated by reference to Exhibit 10.7 of Registrant's Form 8-K filed on November 23, 2010).
10.22	Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated November 19, 2010 (Incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed on November 23, 2010).
10.23	Amendment No. 1 to Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated November 21, 2011 (Incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed on November 23, 2011).
10.24	Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated November 19, 2010 (Incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed on November 23, 2010).
10.25	Amendment No. 2 to Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated January 1, 2013 (Incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed on January 2, 2013).
10.26	Amendment No. 3 to Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and David M. Lobach, Jr., dated January 23, 2014 (Incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed on January 24, 2014).
10.27	Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and Judith A. Hunsicker, dated November 19, 2010 (Incorporated by reference to Exhibit 10.3 of Registrant's Form 8-K filed on November 23, 2010).
10.28	Amendment No. 2 to Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and Judith A. Hunsicker, dated January 1, 2013 (Incorporated by reference to Exhibit 10.3 of Registrant's Form 8-K filed on January 2, 2013).
10.29	Amendment No. 3 to Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and Judith A. Hunsicker, dated January 23, 2014 (Incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed on January 24, 2014).
10.30	Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and James R. Bartholomew, dated November 19, 2010 (Incorporated by reference to Exhibit 10.4 of Registrant's Form 8-K filed on November 23, 2010).
10.31	Amendment No. 2 to Amended and Restated Supplemental Executive Retirement Plan Agreement between Embassy Bank for the Lehigh Valley and James R. Bartholomew, dated January 1, 2013 (Incorporated by reference to Exhibit 10.4 of Registrant's Form 8-K filed on January 2, 2013).
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**Exhibit 21.1**

**SUBSIDIARIES OF THE REGISTRANT**

1. Embassy Bank for the Lehigh Valley, Bethlehem, Pennsylvania; a state-chartered bank organized under Pennsylvania Banking Code of 1965.

**Exhibit 23.1**

**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We hereby consent to the incorporation by reference in the Registration Statements on Forms S-8 (Nos. 333-165015 and 333-169018) and S-3 (No. 333-182189) of Embassy Bancorp, Inc. of our report dated March 28, 2014, relating to the consolidated financial statements, which appears in this Annual Report on Form 10-K.

/s/ ParenteBeard LLC

Allentown, Pennsylvania  
March 28, 2014

**EXHIBIT 31.1**

**CERTIFICATION**

I, David M. Lobach, Jr., certify that:

1. I have reviewed this annual report on Form 10-K of Embassy Bancorp, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant is made known to us by others, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) I evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

By: /s/ David M. Lobach Jr.

David M. Lobach, Jr.

Chairman, President and Chief Executive Officer

DATED: March 28, 2014

**EXHIBIT 31.2**

**CERTIFICATION**

I, Judith A. Hunsicker, certify that:

1. I have reviewed this annual report on Form 10-K of Embassy Bancorp, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant is made known to us by others, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) I evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

By: /s/ Judith A. Hunsicker

Judith A. Hunsicker  
Senior Executive Vice President, Chief Operating  
Officer, Secretary and Chief Financial Officer  
DATED: March 28, 2014

**EXHIBIT 32.1**

**Certification Pursuant to 18 U.S.C. 1350 and  
Section 906 of Sarbanes-Oxley Act of 2002**

We hereby certify that the foregoing Form 10-K of Embassy Bancorp, Inc. for the year ended December 31, 2013 complies in all respects with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained therein fairly presents, in all material respects, the financial condition and results of operations of Embassy Bancorp, Inc.

/s/ David M. Lobach Jr.

David M. Lobach, Jr.  
Chairman, President and Chief Executive Officer

/s/ Judith A. Hunsicker

Judith A. Hunsicker  
Senior Executive Vice President, Chief Operating  
Officer, Secretary and Chief Financial Officer

DATED: March 28, 2014

Embassy Bancorp, Inc. (the “Company”) is a Pennsylvania corporation and registered bank holding company. It is the parent company of Embassy Bank For The Lehigh Valley (the “Bank”), a full service bank providing personal and business lending and deposit service through seven branch offices in the Lehigh Valley area of Pennsylvania.

### Transfer Agent

Registrar and Transfer Company  
10 Commerce Drive  
Cranford, NJ 07016  
Phone: 1-800-368-5948

### Corporate Headquarters

100 Gateway Drive, Suite 100  
P.O. Box 20405  
Lehigh Valley, PA 18002-0405  
610-882-8800 Fax: 610-691-5600  
www.embassybank.com

### Annual Meeting

The Annual Meeting of Embassy Bancorp, Inc. is scheduled for 5:30 PM, June 19, 2014 at the Best Western Lehigh Valley Hotel and Conference Center at 300 Gateway Drive, Bethlehem, Pennsylvania. All shareholders are invited to join us for a reception immediately following the meeting.

### Form 10-K Request

The Company’s Annual Report on Form 10-K, as filed with the Securities and Exchange Commission, is available without charge at the Company’s website at [www.embassybank.com](http://www.embassybank.com) or by contacting:

Judith Hunsicker, Chief Operating Officer  
Embassy Bancorp, Inc.  
P.O. Box 20405  
Lehigh Valley, PA 18002-0405

Shares of the Company common stock are traded over-the-counter under the symbol EMYB and in privately negotiated transactions. There is no established public trading market for the shares of the Company’s common stock and the Company’s common stock is not listed on any national securities exchange. Quotations may be obtained by researching the stock symbol EMYB. Various Internet quotation services detail information about daily transaction volume and price. One such service is the OTC Markets ([www.otcm Markets.com](http://www.otcm Markets.com)), which includes a list of market makers of Company common stock.

On June 20, 2013, the Company declared an annual cash dividend of \$0.05 per share.

### Dividend Reinvestment and Stock Purchase Plan

The Company provides shareholders of record the opportunity to purchase shares of Company common stock through our Dividend Reinvestment and Stock Purchase Plan. Under the Plan, shareholders have the opportunity to use their cash dividends on some or all of their shares of Company common stock, as well as optional cash payments, to purchase additional shares of Company common stock. Eligibility to participate in the plan may be limited to certain jurisdictions, as determined in the discretion of the Company.

To request a prospectus describing the plan, please contact the plan agent:

Registrar and Transfer Company  
Dividend Reinvestment Department  
P.O. Box 664  
Cranford, NJ 07016  
Phone: 1-800-368-5948  
Internet: [www.rtco.com](http://www.rtco.com)

ALLENTOWN  
1142 S Cedar Crest Blvd.  
(484) 223-0018

ALLENTOWN  
4148 W Tilghman St.  
(484) 223-1782

TREXLERTOWN  
6379 Hamilton Blvd.  
(610) 336-8034

BETHLEHEM  
925 West Broad St.  
(484) 821-1210

BETHLEHEM  
100 Gateway Dr.  
(610) 882-8800

SAUCON VALLEY  
Route 378 & Colesville Rd.  
(610) 332-2981

EASTON  
Easton-Nazareth Hwy.  
& Corriere Rd.  
(484) 536-1870



[www.embassybank.com](http://www.embassybank.com)

