COMMERCIAL NATIONAL FINANCIAL CORP /PA
Form 10-Q/A
September 12, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2011

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission file number 0-18676

COMMERCIAL NATIONAL FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

PENNSYLVANIA	25-1623213
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
900 LIGONIER STREET LATROBE, PA	15650
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (724) 539-3501

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

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

submit and post such files).
Yes[ ] No [ ]

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

Large Accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [ ] Smaller Reporting Company [X]

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

[ ]YES [X] NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock.

CLASS	OUTSTANDING AT August 1, 2011
Common Stock, $2 Par Value	2,860,953 Shares

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PART II - OTHER INFORMATION

COMMERCIAL NATIONAL FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(dollars in thousands, except per share amounts)

	June 30, 2011 (unaudited)	December 31, 2010 (unaudited)
ASSETS		
Cash and due from banks	$6,949	$5,578
Interest bearing deposits with banks	11	16
Total cash and cash equivalents	6,960	5,594
Investment securities available for sale	159,026	131,159
Restricted investments in bank stock	3,916	4,339
Loans receivable	190,858	191,906
Allowance for loan losses	(1,683)	(1,686)
Net loans	189,175	190,220
Premises and equipment, net	3,192	3,323
Accrued interest receivable	2,052	1,519
Investment in life insurance	15,715	15,471
Other assets	2,101	3,852
Total assets	$382,137	$355,477
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits (all domestic):		
Non-interest bearing	$87,711	$77,209
Interest bearing	202,724	199,285
Total deposits	290,435	276,494
Short-term borrowings	30,125	17,700
Long-term borrowings	10,000	10,000
Other liabilities	3,563	5,271
Total liabilities	334,123	309,465
Shareholders' equity:		
Common stock, par value $2 per share; 10,000,000 shares authorized; 3,600,000 issued; 2,860,953 shares outstanding in 2011 and 2010	7,200	7,200
Retained earnings	48,795	47,207
Accumulated other comprehensive income	4,563	4,149
Treasury stock, at cost, 739,047 shares in 2011 and 2010	(12,544)	(12,544)

Total shareholders' equity	48,014	46,012
Total liabilities and shareholders' equity	$382,137	$355,477

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

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COMMERCIAL NATIONAL FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(dollars in thousands, except per share data)

	Three Months Ended June 30 (unaudited)		Six Months Ended June 30 (unaudited)	
	2011	2010	2011	2010
INTEREST INCOME:				
Interest and fees on loans	$ 2,666	$ 2,854	$ 5,383	$ 5,774
Interest and dividends on investments:				
Taxable	887	1,165	1,810	2,488
Exempt from federal income taxes	910	590	1,638	1,038
Other	1	1	1	2
Total interest income	4,464	4,610	8,832	9,302
INTEREST EXPENSE:				
Interest on deposits	475	633	960	1,283
Interest on short-term borrowings	11	36	29	77
Interest on long-term borrowings	59	59	118	118
Total interest expense	545	728	1,107	1,478
NET INTEREST INCOME	3,919	3,882	7,725	7,824
PROVISION FOR LOAN LOSSES	0	0	0	0
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	3,919	3,882	7,725	7,824
OTHER INCOME:				
Trust department income	254	217	506	429
Service charges on deposit accounts	270	298	526	570
Income from investment in life insurance	121	122	244	243
Other income	80	62	143	170
Total other operating income	725	699	1,419	1,412
OTHER EXPENSES:				
Salaries and employee benefits	1,516	1,490	3,101	3,009
Net occupancy	200	199	414	426
Furniture and equipment expense	104	135	213	277
Pennsylvania shares tax	127	126	253	252
Legal and professional	129	115	222	239
FDIC insurance	83	85	170	167

Other expenses	738	720	1,413	1,427
Total other operating expenses	2,897	2,870	5,786	5,797
INCOME BEFORE INCOME TAXES	1,747	1,711	3,358	3,439
Income tax expense	260	330	511	708
NET INCOME	$ 1,487	$ 1,381	$ 2,847	$ 2,731
Average Shares Outstanding	2,860,953	2,860,953	2,860,953	2,860,953
EARNINGS PER SHARE, BASIC	$ 0.52	$ 0.48	$ 1.00	$ 0.95
Dividends Paid Per Share	$ 0.22	$ 0.22	$ 0.44	$ 0.44

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

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COMMERCIAL NATIONAL FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(dollars in thousands, except per share data)
(unaudited)

	Common Stock	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance at December 31, 2010	$7,200	$47,207	$(12,544)	$ 4,149	$ 46,012
Comprehensive Income					
Net income	0	2,847	0	0	2,847
Other comprehensive income, net of tax:					
Unrealized net gains on securities	0	0	0	414	414
Total Comprehensive income					3,261
Cash dividends paid					
$0.44 per share	0	(1,259)	0	0	(1,259)
Balance at June 30, 2011	$7,200	$48,795	$(12,544)	$ 4,563	$ 48,014
Balance at December 31, 2009	$7,200	$44,223	$(12,544)	$ 4,613	$ 43,492
Comprehensive Income					
Net income	0	2,731	0	0	2,731
Other comprehensive income, net of tax:					
Unrealized net gains on securities	0	0	0	512	512
Total Comprehensive income					3,243
Cash dividends paid					
$0.44 per share	0	(1,259)	0	0	(1,259)
Balance at June 30, 2010	$7,200	$45,695	$(12,544)	$ 5,125	$ 45,476

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

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COMMERCIAL NATIONAL FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)
(unaudited)

	For Six Months Ended June 30	
	2011	2010
OPERATING ACTIVITIES		
Net income	$2,847	$2,731
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	164	209
Loss on sale of securities	0	5
Amortization of intangibles	49	49
Net accretion of loans and securities	(33)	(86)
Income from investment in life insurance	(244)	(243)
Decrease (increase) in other assets	1,190	(71)
Decrease in other liabilities	(1,921)	(278)
Net cash provided by operating activities	2,052	2,316
INVESTING ACTIVITIES		
Purchase of securities	(36,022)	(21,754)
Maturities and calls of securities	8,815	22,766
Redemption of restricted investments in bank stock	423	0
Net decrease in loans	1,023	6,982
Proceeds from sale of foreclosed real estate	1	2
Purchase of premises and equipment	(33)	(109)
Net cash provided by (used in) investing activities	(25,793)	7,887
FINANCING ACTIVITIES		
Net increase in deposits	13,941	4,649
Increase (decrease) in other short-term borrowings	12,425	(14,200)
Dividends paid	(1,259)	(1,259)
Net cash provided by (used in) financing activities	25,107	(10,810)
Increase (decrease) in cash and cash equivalents	1,366	(607)
Cash and cash equivalents at beginning of year	5,594	6,741
Cash and cash equivalents at end of quarter	$6,960	$6,134
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	$1,144	$1,533
Income Taxes	$625	$800

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

COMMERCIAL NATIONAL FINANCIAL CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2011

Note 1 Basis of Presentation

The accompanying consolidated financial statements include the accounts of Commercial National Financial Corporation (the Corporation) and its wholly owned subsidiaries, Commercial Bank & Trust of PA (the “Bank”) and Ridge Properties, Inc. All material intercompany transactions have been eliminated.

The accompanying unaudited consolidated interim financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information. However, they do not include all information and footnotes required by generally accepted accounting principles for complete financial statements and should be read in conjunction with the annual financial statements of the Corporation for the year ended December 31, 2010, including the notes thereto. In the opinion of management, the unaudited interim consolidated financial statements include all adjustments (consisting of normal recurring adjustments) necessary for a fair statement of financial position as of June 30, 2011 and the results of operations for the three and six-month periods ended June 30, 2011 and 2010. The results of operations for the three and six- months ended June 30, 2011 are not necessarily indicative of the results to be expected for the entire year.

Reclassifications

Certain comparative amounts for the prior year have been reclassified to conform to current year classifications. Such classifications had no effect on net income or changes in shareholders’ equity.

Note 2 Credit Quality Indicators

The allowance for credit losses consists of the allowance for loan losses and the reserve for unfunded lending commitments. 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 allowance for credit losses is increased by the provision for loan losses, and decreased by charge-offs, net of recoveries. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance. All, or part, of the principal balance of loans receivable is charged off to the allowance as soon as it is determined that the repayment of all, or part, of the principal balance is highly unlikely. Non-residential consumer loans are generally charged off no later than 90 days past due on a contractual basis, earlier in the event of Bankruptcy, or if there is an amount deemed uncollectible. Because all identified losses are immediately charged off, no portion of the allowance for loan losses is restricted to any individual loan or groups of loans, and the entire allowance is available to absorb any and all loan losses.

The following discusses key risk within each portfolio segment:

Commercial, industrial and other financing – these loans are made to operating companies or manufacturers for the purpose of production, operating capacity, accounts receivable, inventory or equipment financing. Cash flow from the operations of the company is the primary source of repayment for these loans. The condition of the local economy is an important indicator of risk, but there are also more specific risks depending on the industry of the company. Collateral for these types of loans often do not have sufficient value in a distressed or liquidation scenario to satisfy the outstanding debt.

Commercial real estate – These loans are secured by commercial purpose real estate, including both owner occupied properties and investment properties for various purposes such as strip malls and apartment buildings. Individual projects as well as global cash flows are the primary sources of repayment for these loans. The condition of the local economy is an important indicator of risk, but there are also more specific risks depending on the collateral type as well as the business prospects of the lessee, if the project is not owner occupied.

Residential mortgages – These are loans secured by 1-4 family residences, including purchase money mortgages. We currently originate fixed-rate, fully amortizing mortgage loans with maturities of 15 to 30 years. The primary source of repayment for these loans is the income and assets of the borrower. The condition of the local economy, in particular the unemployment rate, is an important indicator of risk for this segment. The state of the local housing market can also have a significant impact on this portfolio, since low demand and/or declining home values can limit the ability of borrowers to sell a property and satisfy the debt.

Loans to individuals – Loans made to individuals may be secured by junior lien positions on a borrower's primary residence or other assets of the borrower, as well as unsecured loans. This segment includes home equity loans, auto loans, and secured or unsecured lines. The primary source of repayment for these loans is the income and assets of the borrower. The condition of the local economy, in particular the unemployment rate, is an important indicator of risk for this segment. The value of the collateral, if there is any, is less likely to be a source of repayment due to less certain collateral values.

An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

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

An allowance for loan losses is established for an impaired loan if its carrying value exceeds its estimated fair value. The estimated fair values of substantially all of the Corporation's impaired loans are measured based on the estimated fair value of the loan's collateral.

For commercial 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, the 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 agings 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.

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

Loans whose terms are modified are classified as troubled debt restructurings if the Corporation grants such borrowers concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring generally involve a temporary reduction in interest rate or an extension of a loan's stated maturity date. Non-accrual troubled debt restructurings are restored to accrual status if principal and interest payments, under the modified terms, are current for twelve consecutive months after modification. Loans classified as troubled debt restructurings are designated as impaired.

The allowance for loan loss 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 payments, for commercial and consumer loans. Credit quality risk ratings include categories of "pass," "special mention," "substandard" and "doubtful." Assets which do not currently expose the insured institution to sufficient risk, warrant classification as pass. Assets that are not classified as pass and possess weaknesses are required to be designated "special mention." If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. An asset is considered "substandard" if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. "Substandard" assets include those characterized by the "distinct possibility" that the insured institution will sustain "some loss" if the deficiencies are not corrected. Assets classified as "doubtful" have all of the weaknesses inherent in those classified "substandard" with the added characteristic that the weaknesses present make "collection or liquidation in full," on the basis of currently existing facts, conditions, and values, "highly questionable and improbable." In addition, Federal regulatory agencies, as an integral part of their examination process, periodically review the Corporation's allowance for loan losses and may require the Corporation to recognize additions to the allowance based on their judgments about information available to them at the time of their examination, which may not be currently available to management. Based on management's comprehensive analysis of the loan portfolio, management believes the current level of the allowance for loan losses is adequate.

The following table presents the classes of the loan portfolio summarized by the aggregate pass rating and the classified ratings of special mention, substandard and doubtful within the Corporation's internal risk rating system as of June 30, 2011:

(Dollars in Thousands)

	Pass	Special Mention	Substandard	Doubtful	Total
Commercial					
Commercial,					
Industrial & Other	$40,295	$83	$298	$0	$40,676
Commercial real estate	51,854	4,999	7,488	0	64,341
Residential mortgages	63,309	0	143	0	63,452
Loans to Individuals	22,346	43	0	0	22,389
Total	$177,804	$5,125	$7,929	$0	$190,858

The following table presents the classes of the loan portfolio summarized by the aggregate pass rating and the classified ratings of special mention, substandard and doubtful within the Corporation's internal risk rating system as of December 31, 2010:

(Dollars in Thousands)

	Pass	Special Mention	Substandard	Doubtful	Total
Commercial					
Commercial,					
Industrial & Other	$35,802	$90	$353	$0	$36,245
Commercial real estate	50,554	5,362	7,613	0	63,529
Residential mortgages	68,498	105	152	0	68,755
Loans to Individuals	23,331	46	0	0	23,377
Total	$178,185	$5,603	$8,118	$0	$191,906

Past due loans are reviewed on a monthly basis to identify loans for non-accrual status. The Corporation generally places a loan on non-accrual status and discontinues interest accruals when principal or interest is due and has remained unpaid for 90 days. When a loan is placed on non-accrual status, all unpaid interest recognized in the current year is reversed and interest accrued in prior years is charged to the allowance for loan losses. Non-accrual loans may not be restored to accrual status until all delinquent principal and interest have been paid and the ultimate collectability of the remaining principal and interest is reasonably assured.

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The performance and credit quality of the loan portfolio is also monitored by analyzing the age of the 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 June 30, 2011:

(Dollars in Thousands)

	30-89 Days Past Due	>90 Days Past Due and Still Accruing	Non-Accrual	Total Past Due	Current	Total Loans
Commercial						
Commercial, Industrial & Other	$0	$0				