

CSB BANCORP INC /OH
Form 10-Q
November 13, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended: September 30, 2013

OR

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

Commission file number: 0-21714

CSB Bancorp, Inc.

(Exact name of registrant as specified in its charter)

Ohio
(State or other jurisdiction of
incorporation or organization)
91 North Clay, P.O. Box 232, Millersburg, Ohio 44654

34-1687530
(I.R.S. Employer
Identification Number)

(Address of principal executive offices)

(330) 674-9015
(Registrant's telephone number)

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

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

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

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

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

Indicate the number of shares outstanding of the registrant's common stock, as of the latest practicable date.

Common stock, \$6.25 par value

Outstanding at November 1, 2013:
2,736,634 common shares

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CSB BANCORP, INC.

FORM 10-Q

QUARTER ENDED September 30, 2013

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CSB BANCORP, INC.

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS

(Unaudited)

	September 30, 2013	December 31, 2012
<i>(Dollars in thousands)</i>		
ASSETS		
Cash and cash equivalents		
Cash and due from banks	\$ 16,683	\$ 21,485
Interest-earning deposits in other banks	31,437	45,393
Federal funds sold	499	
Total cash and cash equivalents	48,619	66,878
Securities		
Available-for-sale securities	102,453	129,291
Held-to-maturity securities	36,808	
Restricted stock, at cost	5,463	5,463
Total securities	144,724	134,754
Loans held for sale	70	
Loans	377,434	364,580
Less allowance for loan losses	5,077	4,580
Net loans	372,357	360,000
Premises and equipment, net	8,550	8,475
Core deposit intangible	793	894
Goodwill	4,728	4,728
Bank-owned life insurance	9,486	8,298
Accrued interest receivable and other assets	4,568	2,873
TOTAL ASSETS	\$ 593,895	\$ 586,900

LIABILITIES AND SHAREHOLDERS EQUITY

LIABILITIES

Deposits		
Noninterest-bearing	\$ 117,925	\$ 104,147
Interest-bearing	362,936	371,296
Total deposits	480,861	475,443
Short-term borrowings	46,044	43,992
Other borrowings	12,511	12,672
Accrued interest payable and other liabilities	2,330	2,340
Total liabilities	541,746	534,447

SHAREHOLDERS EQUITY

Common stock, \$6.25 par value. Authorized 9,000,000 shares; issued 2,980,602 shares; shares outstanding 2,736,634 in 2013 and 2,736,060 in 2012	18,629	18,629
Additional paid-in capital	9,964	9,974
Retained earnings	29,501	26,962
Treasury stock, at cost - 243,968 in 2013 and 244,542 shares in 2012	(4,958)	(4,976)
Accumulated other comprehensive (loss) income	(987)	1,864
Total shareholders equity	52,149	52,453

TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	\$ 593,895	\$ 586,900
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See notes to unaudited consolidated financial statements.

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CSB BANCORP, INC.

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

<i>(Dollars in thousands, except per share data)</i>	Three Months Ended		Nine Months Ended	
	September 30,	2012	September 30,	2012
INTEREST AND DIVIDEND INCOME				
Loans, including fees	\$ 4,413	\$ 4,357	\$ 13,421	\$ 12,881
Taxable securities	669	638	1,835	2,074
Nontaxable securities	130	120	385	363
Other	23	32	67	112
Total interest and dividend income	5,235	5,147	15,708	15,430
INTEREST EXPENSE				
Deposits	423	559	1,346	1,789
Short-term borrowings	18	22	50	71
Other borrowings	117	140	351	434
Total interest expense	558	721	1,747	2,294
NET INTEREST INCOME	4,677	4,426	13,961	13,136
PROVISION FOR LOAN LOSSES	210	206	630	617
Net interest income, after provision for loan losses	4,467	4,220	13,331	12,519
NONINTEREST INCOME				
Service charges on deposit accounts	353	345	1,001	971
Trust services	201	175	641	503
Debit card interchange fees	198	195	566	590
Gain on sale of loans, net	67	169	283	362
Securities gain, net	149		159	
Other	222	189	644	629
Total noninterest income	1,190	1,073	3,294	3,055
NONINTEREST EXPENSES				
Salaries and employee benefits	2,028	1,985	6,119	5,909
Occupancy expense	245	280	758	767
Equipment expense	182	154	525	448

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Professional and director fees	174	172	465	621
Franchise tax expense	147	138	440	415
FDIC insurance expense	90	83	262	238
Software expense	133	94	365	275
Marketing and public relations	89	83	274	235
Debit card expense	62	82	175	230
Amortization of intangible assets	34	37	101	103
Net cost of operation of other real estate			9	8
Other	450	420	1,363	1,383
Total noninterest expenses	3,634	3,528	10,856	10,632
Income before income taxes	2,023	1,765	5,769	4,942
FEDERAL INCOME TAX PROVISION	616	534	1,753	1,515
NET INCOME	\$ 1,407	\$ 1,231	\$ 4,016	\$ 3,427
Basic and diluted net earnings per share	\$ 0.52	\$ 0.45	\$ 1.47	\$ 1.25

See notes to unaudited consolidated financial statements.

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CSB BANCORP, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

<i>(Dollars in thousands)</i>	Three Months Ended		Nine Months Ended	
	September 30, 2013	2012	September 30, 2013	2012
Net income	\$ 1,407	\$ 1,231	\$ 4,016	\$ 3,427
Other comprehensive (loss) income				
Unrealized (losses) gains arising during the period	1,644	282	(2,428)	1,093
Unrealized (losses) on held to maturity transfer	(1,733)		(1,733)	
Reclassification adjustment for gains included in income	(149)		(159)	
Net unrealized (losses) gains	(238)	282	(4,320)	1,093
Income tax effect	81	(96)	1,469	(372)
Other comprehensive (loss) income	(157)	186	(2,851)	721
Total comprehensive income	\$ 1,250	\$ 1,417	\$ 1,165	\$ 4,148

See notes to unaudited consolidated financial statements.

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CSB BANCORP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
<i>(Dollars in thousands, except per share data)</i>				
Balance at beginning of period	\$ 51,391	\$ 51,176	\$ 52,453	\$ 49,429
Net income	1,407	1,231	4,016	3,427
Other comprehensive (loss) income	(157)	186	(2,851)	721
Stock options exercised, 574 shares			8	
Cash dividends declared	(492)	(492)	(1,477)	(1,476)
Balance at end of period	\$ 52,149	\$ 52,101	\$ 52,149	\$ 52,101
Cash dividends declared per share	\$ 0.18	\$ 0.18	\$ 0.54	\$ 0.54

See notes to unaudited consolidated financial statements.

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CSB BANCORP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended	
	September 30,	
	2013	2012
<i>(Dollars in thousands)</i>		
NET CASH FROM OPERATING ACTIVITIES	\$ 4,912	\$ 4,388
CASH FLOWS FROM INVESTING ACTIVITIES		
Securities:		
Proceeds from repayments held-to-maturity	572	
Proceeds from maturities and repayments available-for-sale	27,560	54,051
Purchases available-for-sale	(46,941)	(65,222)
Proceeds from sale of securities available-for-sale	4,309	
Loan originations, net of repayments	(12,946)	(28,702)
Proceeds from sale of other real estate	18	26
Property, equipment, and software acquisitions	(1,127)	(503)
Purchase of bank-owned life insurance	(1,000)	(5,000)
Net cash used in investing activities	(29,555)	(45,350)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net change in deposits	5,470	10,849
Net change in short-term borrowings	2,052	5,938
Repayments of other borrowings	(161)	(2,423)
Cash dividends	(985)	(985)
Proceeds from stock options exercised	8	
Net cash provided by financing activities	6,384	13,379
NET DECREASE IN CASH AND CASH EQUIVALENTS	(18,259)	(27,583)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	66,878	82,258
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 48,619	\$ 54,675
SUPPLEMENTAL DISCLOSURES		
Cash paid during the year for:		
Interest	\$ 1,814	\$ 2,426
Income taxes	1,585	1,170
Noncash investing activities:		
Transfer of securities from available-for-sale to held-to-maturity	38,930	

Transfer of loans to other real estate owned		56
Noncash financing activities:		
Dividends declared	492	492

See notes to unaudited consolidated financial statements.

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying condensed consolidated financial statements include the accounts of CSB Bancorp, Inc. and its wholly-owned subsidiaries, The Commercial and Savings Bank (the Bank) and CSB Investment Services, LLC (together referred to as the Company or CSB). All significant intercompany transactions and balances have been eliminated in consolidation.

The condensed consolidated financial statements have been prepared without audit. In the opinion of management, all adjustments (which include normal recurring adjustments) necessary to present fairly the Company s financial position at September 30, 2013, and the results of operations and changes in cash flows for the periods presented have been made.

Certain information and footnote disclosures typically included in financial statements prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) have been omitted. The Annual Report for CSB for the year ended December 31, 2012, contains Consolidated Financial Statements and related footnote disclosures, which should be read in conjunction with the accompanying Consolidated Financial Statements. The results of operations for the period ended September 30, 2013 are not necessarily indicative of the operating results for the full year or any future interim period.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. This Update requires that companies present either in a single note or parenthetically on the face of the financial statements, the effect of significant amounts reclassified from each component of accumulated other comprehensive income based on its source and the income statement line items affected by the reclassification. The new requirements will take effect for public companies in fiscal years, and interim periods within those years, beginning after December 15, 2012. The Company adopted this ASU on January 1, 2013. The effect of adopting this ASU increased our disclosure surrounding reclassification items out of accumulated other comprehensive income.

In July 2013, the FASB issued ASU 2013-10, *Derivatives and Hedging (Topic 815): Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a Benchmark Interest Rate for Hedge Accounting Purposes*. The amendments in this Update permit the Fed Funds Effective Swap Rate (OIS) to be used as a U.S. benchmark interest rate for hedge accounting purposes under Topic 815, in addition to UST and LIBOR. The amendments also remove the restriction on using different benchmark rates for similar hedges. The amendments are effective prospectively for qualifying new or redesignated hedging relationships entered into on or after July 17, 2013. This ASU did not have a significant impact on the Company s financial statements.

In July 2013, the FASB issued ASU 2013-11, *Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*. This Update applies to all entities that have unrecognized tax benefits when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists at the reporting date. An unrecognized tax benefit, or a portion of an

unrecognized tax benefit, should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. The assessment of whether a deferred tax asset is available is based on the unrecognized tax benefit and deferred tax asset that exist at the reporting date and should be made presuming disallowance of the tax position at the reporting date. The amendments in this Update are effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. For nonpublic entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2014.

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Early adoption is permitted. The amendments should be applied prospectively to all unrecognized tax benefits that exist at the effective date. Retrospective application is permitted. This ASU is not expected to have a significant impact on the Company's financial statements.

NOTE 2 SECURITIES

Securities consist of the following at September 30, 2013 and December 31, 2012:

<i>(Dollars in thousands)</i>	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
September 30, 2013				
Available-for-sale securities				
U.S. Treasury securities	\$ 1,005	\$	\$ 9	\$ 996
U.S. government agencies	23,998	10	590	23,418
Mortgage-backed securities	51,563	696	175	52,084
Asset-backed securities	2,764	22		2,786
States and political subdivisions	18,280	378	136	18,522
Corporate bonds	4,500	29	3	4,526
Equity securities	106	16	1	121
Total available-for-sale securities	102,216	1,151	914	102,453
Held-to-maturity securities				
U.S. government agencies	15,169		583	14,586
Mortgage-backed securities	21,639		535	21,104
Total held-to-maturity securities	36,808		1,118	35,690
Restricted stock	5,463			5,463
Total securities	\$ 144,487	\$ 1,151	\$ 2,032	\$ 143,606

December 31, 2012

Available-for-sale securities							
U.S. Treasury securities	\$	100	\$	\$	100		
U.S. government agencies		35,996		27	43	35,980	
Mortgage-backed securities		66,933		2,107	1	69,039	
Asset-backed securities		2,862			39	2,823	
States and political subdivisions		16,194		701	12	16,883	
Corporate bonds		4,313		112	28	4,397	
Equity securities		69		9	9	69	
Total available-for-sale securities		126,467		2,956	132	129,291	
Restricted stock		5,463				5,463	
Total securities	\$	131,930	\$	2,956	\$	132	\$ 134,754

As of July 31, 2013, approximately \$39 million par value U.S. government agency and U.S. agency mortgage-backed securities were transferred from Available for sale to Held to maturity. These bonds carried gross unrealized losses of \$1.9 million at the transfer date. The bonds were transferred to provide stability to the other comprehensive income component in shareholders' equity should interest rates continue to rise and to accurately reflect the strategic purpose of these investments.

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 2 SECURITIES (CONTINUED)

The amortized cost and fair value of debt securities at September 30, 2013, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

<i>(Dollars in thousands)</i>	Amortized cost	Fair value
Available-for-sale:		
Due in one year or less	\$ 279	\$ 280
Due after one through five years	16,589	16,812
Due after five through ten years	26,318	25,955
Due after ten years	58,924	59,285
Total debt securities available-for-sale	\$ 102,110	\$ 102,332
Held-to-maturity:		
Due in one year or less	\$	\$
Due after one through five years		
Due after five through ten years	3,710	3,655
Due after ten years	33,098	32,035
Total debt securities held-to-maturity	\$ 36,808	\$ 35,690

Securities with a carrying value of approximately \$89.5 million and \$79.2 million were pledged at September 30, 2013 and December 31, 2012, respectively, to secure public deposits, as well as other deposits and borrowings as required or permitted by law.

Restricted stock primarily consists of investments in FHLB and Federal Reserve Bank stock. The Bank's investment in FHLB stock amounted to approximately \$5.0 million at September 30, 2013 and December 31, 2012. Federal Reserve Bank stock was \$471 thousand at September 30, 2013 and December 31, 2012.

The following table shows the proceeds from sales of available-for-sale securities and the gross realized gains and losses on the sales of those securities that have been included in earnings as a result of the sales.

<i>(Dollars in thousands)</i>	Three months ended		Nine months ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Proceeds	\$ 3,809	\$	\$ 4,309	\$
Realized gains	\$ 149	\$	\$ 159	\$
Realized losses				
Net securities gains	\$ 149	\$	\$ 159	\$

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 2 SECURITIES (CONTINUED)

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

	Securities in a continuous unrealized loss position					
	Less than 12 months		12 months or more		Total	
	Gross unrealized losses	Fair value	Gross unrealized losses	Fair value	Gross unrealized losses	Fair value
<i>(Dollars in thousands)</i>						
September 30, 2013						
Available-for-sale						
U.S. Treasury securities	\$ 9	\$ 996	\$	\$	\$ 9	\$ 996
U.S. Government agencies	590	19,408			590	19,408
Mortgage-backed securities	175	22,096			175	22,096
State and political subdivisions	134	3,599	2	301	136	3,900
Corporate bonds	2	573	1	499	3	1,072
Equity securities			1	1	1	1
Held-to-maturity						
U.S. Government agencies	583	14,586			583	14,586
Mortgage-backed securities	535	21,103			535	21,103
Total temporarily impaired securities	\$ 2,028	\$ 82,361	\$ 4	\$ 801	\$ 2,032	\$ 83,162
December 31, 2012						
Available-for-sale						
U.S. Government agencies	\$ 43	\$ 15,957	\$	\$	\$ 43	\$ 15,957
Mortgage-backed securities	1	344			1	344
Asset-backed securities	39	1,833			39	1,833
State and political subdivisions	12	1,737			12	1,737
Corporate bonds	4	366	24	975	28	1,341
Equity securities			9	45	9	45

Total temporarily impaired securities	\$	99	\$ 20,237	\$ 33	\$ 1,020	\$ 132	\$ 21,257
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There were sixty-eight (68) securities in an unrealized loss position at September 30, 2013, three (3) of which were in a continuous loss position for twelve months or more. At least quarterly, the Company conducts a comprehensive security-level impairment assessment. The assessments are based on the nature of the securities, the extent and duration of the securities in an unrealized loss position, the extent and duration of the loss and management's intent to sell or if it is more likely than not that management will be required to sell a security before recovery of its amortized cost basis, which may be maturity. Management believes the Company will fully recover the cost of these securities. It does not intend to sell these securities and likely will not be required to sell them before the anticipated recovery of the remaining amortized cost basis, which may be maturity. As a result, management concluded that these securities were not other-than-temporarily impaired at September 30, 2013.

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 3 LOANS

Loans consist of the following:

<i>(Dollars in thousands)</i>	September 30, 2013	December 31, 2012
Commercial	\$ 116,190	\$ 104,899
Commercial real estate	126,423	119,192
Residential real estate	112,819	110,412
Construction & land development	14,904	23,358
Consumer	6,838	6,480
Total loans before deferred costs	377,174	364,341
Deferred loan costs	260	239
Total Loans	\$ 377,434	\$ 364,580

Loan Origination/Risk Management

The Company has certain lending policies and procedures in place that are designed to maximize loan income within an acceptable level of risk. Management reviews and approves these policies and procedures on a regular basis. A reporting system supplements the review process by providing management with frequent reports related to loan production, loan quality, concentrations of credit, loan delinquencies and non-performing and potential problem loans. Diversification in the loan portfolio is a means of managing risk associated with fluctuations in economic conditions.

Commercial loans are underwritten after evaluating and understanding the borrower's ability to operate profitably and prudently expand its business. Underwriting standards are designed to promote relationship banking rather than transactional banking. The Company's management examines current and occasionally projected cash flows to determine the ability of the borrower to repay their obligations as agreed. Commercial loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

Commercial real estate loans are subject to underwriting standards and processes similar to commercial loans, in addition to those of real estate loans. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the

repayment of these loans is largely dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be adversely affected by conditions in the real estate markets or in the general economy. The properties securing the Company's commercial real estate portfolio are diverse in terms of type. This diversity helps reduce the Company's exposure to adverse economic events that affect any single industry. Management monitors and evaluates commercial real estate loans based on collateral, geography and risk grade criteria. In addition, management tracks the level of owner-occupied commercial real estate loans versus non-owner occupied loans. At September 30, 2013 and December 31, 2012, approximately 80% and 81%, respectively of the outstanding principal balance of the Company's commercial real estate loans were secured by owner-occupied properties.

With respect to loans to developers and builders that are secured by non-owner occupied properties, the Company generally requires the borrower to have had an existing relationship with the Company and have a proven record of success. Construction and land development loans are underwritten utilizing independent appraisal reviews, sensitivity analysis of absorption and lease rates and financial analysis of the developers and property owners. Construction and land development loans are generally based upon estimates of costs and value associated with the completed project. These estimates may be inaccurate.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 3 LOANS (CONTINUED)

Construction and land development loans often involve the disbursement of substantial funds with repayment substantially dependent on the success of the ultimate project. Sources of repayment for these types of loans may be pre-committed permanent loans from approved long-term lenders, sales of developed property or an interim loan commitment from the Company until permanent financing is obtained. These loans are closely monitored by on-site inspections and are considered to have higher risk than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, governmental regulation of real property, general economic conditions and the availability of long-term financing.

The Company originates consumer loans utilizing a judgmental underwriting process. To monitor and manage consumer loan risk, policies and procedures are developed and modified, as needed, jointly by line and staff personnel. This activity, coupled with relatively small loan amounts that are spread across many individual borrowers, minimizes risk.

The Company maintains an independent loan review department that reviews and validates the credit risk program on a periodic basis. Results of these reviews are presented to management. The loan review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel, as well as the Company's policies and procedures.

Loans serviced for others approximated \$59.0 million and \$60.2 million at September 30, 2013 and December 31, 2012, respectively.

Concentrations of Credit

Nearly all of the Company's lending activity occurs within the state of Ohio, including the four (4) counties of Holmes, Stark, Tuscarawas and Wayne, as well as other markets. The majority of the Company's loan portfolio consists of commercial and industrial and commercial real estate loans. As of September 30, 2013 and December 31, 2012, there were no concentrations of loans related to any single industry.

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 3 LOANS (CONTINUED)**Allowance for Loan Losses**

The following table details activity in the allowance for loan losses by portfolio segment for the three and nine month periods ended September 30, 2013 and 2012. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories. The increase in the provision for possible loan losses related to commercial loans was affected by a qualitative adjustment for loans rated special mention, as well as changes in volume and credit quality of loans in this category. The provision for possible loan losses related to residential real estate increased during third quarter 2013 as a result of an increase in non performing loans within this category.

<i>(Dollars in thousands)</i>	Commercial		Construction		Consumer	Unallocated	Total
	Commercial	Real Estate	Residential Real Estate	& Land Development			
Three months ended September 30, 2013							
Beginning balance, June 30, 2013	\$ 1,316	\$ 1,815	\$ 1,174	\$ 162	\$ 144	\$ 334	\$ 4,945
Provision for possible loan losses	27	(5)	95	18	(48)	123	210
Charge-offs	(54)		(28)		(9)		(91)
Recoveries	5		3		5		13
Net charge-offs	(49)		(25)		(4)		(78)
Ending balance	\$ 1,294	\$ 1,810	\$ 1,244	\$ 180	\$ 92	\$ 457	\$ 5,077

<i>(Dollars in thousands)</i>	Commercial		Construction		Consumer	Unallocated	Total
	Commercial	Real Estate	Residential Real Estate	& Land Development			

**Nine months ended
September 30, 2013**

Beginning balance, December 31, 2012	\$ 933	\$ 1,902	\$ 1,096	\$ 253	\$ 76	\$ 320	\$ 4,580
Provision for possible loan losses	455	(41)	162	(73)	(10)	137	630
Charge-offs	(112)	(51)	(28)		(11)		(202)
Recoveries	18		14		37		69
Net charge-offs	(94)	(51)	(14)		26		(133)
Ending balance	\$ 1,294	\$ 1,810	\$ 1,244	\$ 180	\$ 92	\$ 457	\$ 5,077

<i>(Dollars in thousands)</i>	Commercial		Construction		Consumer	Unallocated	Total
	Commercial	Real Estate	Residential Real Estate	& Land Development			
Three months ended September 30, 2012							
Beginning balance, June 30, 2012	\$ 896	\$ 1,927	\$ 1,051	\$ 217	\$ 64	\$ 316	\$ 4,471
Provision for possible loan losses	94	108	(45)	85	46	(82)	206
Charge-offs					(39)		(39)
Recoveries	2		10		11		23
Net charge-offs	2		10		(28)		(16)
Ending balance	\$ 992	\$ 2,035	\$ 1,016	\$ 302	\$ 82	\$ 234	\$ 4,661

<i>(Dollars in thousands)</i>	Commercial		Construction		Consumer	Unallocated	Total
	Commercial	Real Estate	Residential Real Estate	& Land Development			
Nine months ended September 30, 2012							
Beginning balance, December 31, 2011	\$ 1,024	\$ 1,673	\$ 894	\$ 180	\$ 78	\$ 233	\$ 4,082
Provision for possible loan losses	(33)	376	127	122	24	1	617
Charge-offs	(15)	(14)	(104)		(70)		(203)
Recoveries	16		99		50		165
Net charge-offs	1	(14)	(5)		(20)		(38)
Ending balance	\$ 992	\$ 2,035	\$ 1,016	\$ 302	\$ 82	\$ 234	\$ 4,661

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 3 LOANS (CONTINUED)

The following table presents the balance in the allowance for loan losses and the ending loan balances by portfolio segment and based on the impairment method as of September 30, 2013 and December 31, 2012:

<i>(Dollars in thousands)</i>	Commercial		Construction		Consumer		Unallocated		Total
	Commercial	Real Estate	Residential Real Estate	& Land Development	Consumer	Unallocated	Unallocated	Unallocated	Total
September 30, 2013									
Allowance for loan losses:									
Ending allowance balances attributable to loans:									
Individually evaluated for impairment	\$ 185	\$ 442	\$ 292	\$	\$	\$	\$	\$	\$ 919
Collectively evaluated for impairment	1,109	1,368	952	180	92	457	457	457	4,158
Total ending allowance balance	\$ 1,294	\$ 1,810	\$ 1,244	\$ 180	\$ 92	\$ 457	\$ 457	\$ 457	\$ 5,077
Loans:									
Loans individually evaluated for impairment	\$ 3,898	\$ 3,460	\$ 1,832	\$	\$	\$	\$	\$	\$ 9,190
Loans collectively evaluated for impairment	112,292	122,963	110,987	14,904	6,838	6,838	6,838	6,838	367,984
Total ending loans balance	\$ 116,190	\$ 126,423	\$ 112,819	\$ 14,904	\$ 6,838	\$ 6,838	\$ 6,838	\$ 6,838	\$ 377,174
December 31, 2012									
Allowance for loan losses:									
Ending allowance balances attributable to loans:									
Individually evaluated for impairment	\$ 85	\$ 522	\$ 172	\$	\$	\$	\$	\$	\$ 779
Collectively evaluated for impairment	848	1,380	924	253	76	320	320	320	3,801

Total ending allowance balance	\$	933	\$	1,902	\$	1,096	\$	253	\$	76	\$	320	\$	4,580
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Loans:

Loans individually evaluated for impairment	\$	4,315	\$	4,573	\$	1,137	\$	166	\$		\$	10,191
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Loans collectively evaluated for impairment		100,584		114,619		109,275		23,192		6,480		354,150
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Total ending loans balance	\$	104,899	\$	119,192	\$	110,412	\$	23,358	\$	6,480	\$	364,341
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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 3 LOANS (CONTINUED)

The following table presents loans individually evaluated for impairment by class of loans as of September 30, 2013 and December 31, 2012:

<i>(Dollars in thousands)</i>	Unpaid Principal Balance	Recorded Investment with no Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
September 30, 2013							
Commercial	\$ 3,913	\$ 7	\$ 3,902	\$ 3,909	\$ 185	\$ 3,917	\$ 126
Commercial real estate	3,767	306	3,155	3,461	442	3,730	125
Residential real estate	1,942	583	1,237	1,820	292	1,270	29
Construction & land development						28	2
Total impaired loans	\$ 9,622	\$ 896	\$ 8,294	\$ 9,190	\$ 919	\$ 8,945	\$ 282
December 31, 2012							
Commercial	\$ 4,315	\$	\$ 4,329	\$ 4,329	\$ 85	\$ 4,123	\$ 167
Commercial real estate	4,906	1,723	2,849	4,572	522	4,396	152
Residential real estate	1,223	86	1,057	1,143	172	770	18
Construction & land development	173	166		166		167	
Total impaired loans	\$ 10,617	\$ 1,975	\$ 8,235	\$ 10,210	\$ 779	\$ 9,456	\$ 337

The following table presents the aging of past due loans and nonaccrual loans as of September 30, 2013 and December 31, 2012 by class of loans:

<i>(Dollars in thousands)</i>	Current	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days + Past Due	Non-Accrual	Total Past Due and Non- Accrual	Total Loans
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September 30, 2013

Commercial	\$ 115,714	\$ 405	\$	\$	\$ 71	\$ 476	\$ 116,190
Commercial real estate	124,753	271	216		1,183	1,670	126,423
Residential real estate	110,681	767	257	36	1,078	2,138	112,819
Construction & land development	13,954	950				950	14,904
Consumer	6,616	137	85			222	6,838
Total Loans	\$ 371,718	\$ 2,530	\$ 558	\$ <u>36</u>	\$ 2,332	\$ 5,456	\$ 377,174

December 31, 2012

Commercial	\$ 104,348	\$ 60	\$ 8	\$	\$ 483	\$ 551	\$ 104,899
Commercial real estate	117,372	41	34		1,745	1,820	119,192
Residential real estate	108,574	472	430	131	805	1,838	110,412
Construction & land development	23,180		5		173	178	23,358
Consumer	6,325	132	23			155	6,480
Total Loans	\$ 359,799	\$ 705	\$ 500	\$ <u>131</u>	\$ 3,206	\$ 4,542	\$ 364,341

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 3 LOANS (CONTINUED)**Troubled Debt Restructurings**

All troubled debt restructurings (TDR s) are individually evaluated for impairment and a related allowance is recorded, as needed. Loans whose terms have been modified as TDR s totaled \$8.2 million as of September 30, 2013, and \$8.7 million as of December 31, 2012, with \$823 thousand and \$718 thousand of specific reserves allocated to those loans, respectively. At September 30, 2013, \$7.5 million of the loans classified as TDR s were performing in accordance with their modified terms. Of the remaining \$736 thousand, all were in nonaccrual of interest status.

None of the loans that were restructured in 2011 or 2012 have subsequently defaulted in the three or nine month periods ended September 30, 2013 and 2012. Loan modifications that are considered TDR s completed during the three and nine month periods ended September 30, 2013 and 2012 were as follows:

	For the Three Months Ended September 30, 2013		
	Number of loans restructured	Pre- Modification Recorded Investment	Post- Modification Recorded Investment
<i>(Dollars in thousands)</i>			
Commercial	1	\$ 7	\$ 7
Residential Real Estate	2	188	188
Total Restructured Loans	3	\$ 195	\$ 195

	For the Nine Months Ended September 30, 2013		
	Number of loans restructured	Pre- Modification Recorded Investment	Post- Modification Recorded Investment
<i>(Dollars in thousands)</i>			
Commercial	3	\$ 83	\$ 83
Residential Real Estate	2	188	188
Total Restructured Loans	5	\$ 271	\$ 271

For the Three Months Ended September 30, 2012

<i>(Dollars in thousands)</i>	Number of loans restructured	Pre- Modification Recorded Investment	Post- Modification Recorded Investment
Commercial Real Estate	1	\$ 140	\$ 140
Residential Real Estate	5	333	333
Total Restructured Loans	6	\$ 473	\$ 473

For the Nine Months Ended September 30, 2012

<i>(Dollars in thousands)</i>	Number of loans restructured	Pre- Modification Recorded Investment	Post- Modification Recorded Investment
Commercial Real Estate	1	\$ 140	\$ 140
Residential Real Estate	7	488	488
Total Restructured Loans	8	\$ 628	\$ 628

The loans restructured during the three and nine months ended September 30, 2013 and 2012 were modified by changing the monthly payment to interest only. No principal reductions were made.

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 3 LOANS (CONTINUED)

Credit Quality Indicators

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes commercial loans individually by classifying the loans as to credit risk. This analysis includes commercial loans with an outstanding balance greater than \$275 thousand and is performed on an annual basis.

The Company uses the following definitions for risk ratings:

Pass. Loans classified as pass (Acceptable, Low Acceptable or Pass Watch) may exhibit a wide array of characteristics but at minimum represent an acceptable risk to the Bank. Borrowers in this rating may have leveraged but acceptable balance sheet positions, satisfactory asset quality, and stable to favorable sales and earnings trends, acceptable liquidity and adequate cash flow. Loans are considered fully collectible and require an average amount of administration. While generally adhering to credit policy, these loans may exhibit occasional exceptions that do not result in undue risk to the Bank. Borrowers are generally capable of absorbing setbacks, financial and otherwise, without the threat of failure.

Special Mention. Loans classified as special mention have material weaknesses that deserve management's close attention. If left uncorrected, these weaknesses may result in deterioration of the repayment prospects for the loan at some future date.

Substandard. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 3 LOANS (CONTINUED)

Loans that do not meet the criteria for special mention, substandard or doubtful classification, when analyzed individually as part of the above described process are considered to be pass rated loans. As of September 30, 2013 and December 31, 2012, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

<i>(Dollars in thousands)</i>	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
September 30, 2013						
Commercial	\$ 100,746	\$ 9,850	\$ 5,170	\$	\$ 424	\$ 116,190
Commercial real estate	111,168	7,553	5,879		1,823	126,423
Residential real estate	243		48		112,528	112,819
Construction & land development	11,598		2,040		1,266	14,904
Consumer					6,838	6,838
Total	\$ 223,755	\$ 17,403	\$ 13,137	\$	\$ 122,879	\$ 377,174
December 31, 2012						
Commercial	\$ 92,123	\$ 5,854	\$ 6,637	\$	\$ 285	\$ 104,899
Commercial real estate	102,602	5,671	8,459		2,460	119,192
Residential real estate	200		53		110,159	110,412
Construction & land development	18,063	2,750	1,244		1,301	23,358
Consumer					6,480	6,480
Total	\$ 212,988	\$ 14,275	\$ 16,393	\$	\$ 120,685	\$ 364,341

Loans listed as not rated are either less than \$275 thousand or are included in groups of homogeneous loans. The following table presents loans that are not rated by class of loans as of September 30, 2013 and December 31, 2012. Non-performing loans include loans past due 90 days and greater and loans on nonaccrual of interest.

<i>(Dollars in thousands)</i>	Performing	Non-Performing	Total
September 30, 2013			

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Commercial	\$ 424	\$	\$ 424
Commercial real estate	1,823		1,823
Residential real estate	111,462	1,066	112,528
Construction & land development	1,266		1,266
Consumer	6,838		6,838
Total	\$ 121,813	\$ 1,066	\$ 122,879

December 31, 2012

Commercial	\$ 285	\$	\$ 285
Commercial real estate	2,460		2,460
Residential real estate	109,276	883	110,159
Construction & land development	1,294	7	1,301
Consumer	6,480		6,480
Total	\$ 119,795	\$ 890	\$ 120,685

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 4 FAIR VALUE MEASUREMENTS

The Company provides disclosures about assets and liabilities carried at fair value. The framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities and lowest priority to unobservable inputs. The three broad levels of the fair value hierarchy are described below:

- Level I: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Company has the ability to access.
- Level II: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; inputs other than quoted prices that are observable for the asset or liability; and inputs that are derived principally from or corroborated by observable market data by corroborated or other means. If the asset or liability has a specified (contractual) term, the Level II input must be observable for substantially the full term of the asset or liability.
- Level III: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

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CSB BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 4 FAIR VALUE MEASUREMENTS (CONTINUED)

The following table presents the assets reported on the consolidated statements of financial condition at their fair value as of September 30, 2013 and December 31, 2012, by level within the fair value hierarchy. No liabilities are carried at fair value. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Equity securities and U.S. Treasury Notes are valued at the closing price reported on the active market on which the individual securities are traded. Obligations of U.S. government agencies, mortgage-backed securities, asset-backed securities, obligations of states and political subdivisions and corporate bonds are valued at observable market data for similar assets.

<i>(Dollars in thousands)</i>	Level			Total
	Level I	II	Level III	
<u>September 30, 2013</u>				
ASSETS:				
Securities available-for-sale:				
U.S. Treasury securities				