ALLERGAN INC
Form 5
January 20, 2015

FORM 5

OMB APPROVAL

OMB Number:	3235-0362
Expires:	January 31, 2005
Estimated average burden hours per response...	1.0

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. *See* Instruction 1(b).
Form 3 Holdings Reported
Form 4 Transactions Reported

ANNUAL STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

1. Name and Address of Reporting Person *
PYOTT DAVID E I

(Last) (First) (Middle)

2525 DUPONT DRIVE

(Street)

IRVINE,Â CAÂ 92612

(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
ALLERGAN INC [AGN]

3. Statement for Issuer's Fiscal Year Ended (Month/Day/Year)
12/31/2014

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

__X__ Director _____ 10% Owner
__X__ Officer (give title below) _____ Other (specify below)
Chairman of the Board and CEO

6. Individual or Joint/Group Reporting

(check applicable line)

_X_ Form Filed by One Reporting Person
___ Form Filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1.Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)	4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned at end of Issuer's Fiscal Year (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
				Amount	(A) or (D)	Price			

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 2270 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)	5. Number of Derivative Securities Acquired (A) or Disposed of (D)	6. Date Exercisable and Expiration Date (Month/Day/Year)	7. Title and A Underlying S (Instr. 3 and

	Derivative Security				(Instr. 3, 4, and 5)				
					(A)	(D)	Date Exercisable	Expiration Date	Title
Employee Stock Option (Right to Buy)	$ 125.07	03/20/2014	Â	G	257,756	Â	Â (1)	02/21/2024	Common Stock
Employee Stock Option (Right to Buy)	$ 125.07	03/20/2014	Â	G	Â	257,756	Â (2)	02/21/2024	Common Stock

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
PYOTT DAVID E I 2525 DUPONT DRIVE IRVINE,Â CAÂ 92612	Â X	Â	Â Chairman of the Board and CEO	Â

Signatures

/s/ Matthew J. Maletta, attorney-in-fact for David E.I. Pyott	01/16/2015
**Signature of Reporting Person	Date

Explanation of Responses:

* If the form is filed by more than one reporting person, see Instruction 4(b)(v).

** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

(1) The option becomes exercisable in four equal annual installments beginning February 21, 2015.

(2) The option becomes exercisable in four equal annual installments beginnng February 21, 2015.

Note: File three copies of this Form, one of which must be manually signed. If space provided is insufficient, *see* Instruction 6 for procedure.
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Government-sponsored entities (GSE) - residential

96,434,029 1,045,043 1,206,718 96,272,354

Total investment securities

$179,909,415 $3,227,402 $2,198,074 $180,938,743

The amortized cost and fair value of securities available for sale at September 30, 2014, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	2014			
	Available for Sale		Held to Maturity	
Maturity Distributions at September 30	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Within one year	$ 361,838	$ 364,162	$ 370,000	$ 370,000
One to five years	17,776,366	17,982,193	1,790,000	1,790,000
Five to ten years	33,477,407	34,761,494		
After ten years	25,609,763	26,625,868		
	77,225,374	79,733,717	2,160,000	2,160,000
SBA Pools	2,796,373	2,789,289		
Other asset backed securities	2,025,224	2,018,800		
Mortgage-backed securities - GSE residential	85,155,037	85,222,914	8,824,331	8,791,776
	$ 167,202,008	$ 169,764,720	$ 10,984,331	$ 10,951,776

Securities with a carrying value of $2,426,000 and $2,409,000 were pledged at September 30, 2014 and 2013 to secure repurchase agreements. Securities with a carrying value of $9,121,000 and $4,217,000 were pledged at September 30, 2014 and 2013 to secure certain deposits.

Proceeds from sales of securities available for sale during 2014 and 2013 were approximately $20,457,000 and $17,534,000, respectively. Gross gains of approximately $710,000 and $1,108,000 were realized on investment transactions during 2014 and 2013, respectively. Gross losses of $0 and approximately $7,000 were realized on investment transactions during 2014 and 2013, respectively.

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September 30, 2014 and 2013

Certain investments in debt securities are reported in the consolidated financial statements at an amount less than their historical cost. Total fair value of these investments at September 30, 2014 and 2013 was approximately $75,400,000 and $80,684,000, which is approximately 42% and 45% of the Company s available-for-sale and held-to-maturity investment portfolio. These declines primarily resulted from fluctuations in market interest rates after the purchase.

Based on evaluation of available evidence, including recent changes in market interest rates, credit rating information and information obtained from regulatory filings, management believes the declines in fair value for these securities are temporary.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in either net income or accumulated other comprehensive loss in the period the other-than-temporary impairment is identified.

The following table shows our investments gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at September 30, 2014:

	2014					
	Less Than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available for sale						
Federal agencies	$ 7,101,020	$ 8,028	$ 9,806,750	$ 193,352	$ 16,907,770	$ 201,380
State and municipal obligations	2,592,716	8,212	6,305,786	178,057	8,898,502	186,269
SBA Pools	2,000,000	9,983			2,000,000	9,983
Other asset backed securities			2,018,800	6,424	2,018,800	6,424
Mortgage-backed securities - GSE residential	16,961,754	62,947	23,889,458	785,470	40,851,212	848,417
Total available for sale	28,655,490	89,170	42,020,794	1,163,303	70,676,284	1,252,473
Held to maturity						
Mortgage-backed securities - GSE residential	4,723,234	40,400			4,723,234	40,400
Total temporarily impaired securities	$ 33,378,724	$ 129,570	$ 42,020,794	$ 1,163,303	$ 75,399,518	$ 1,292,873

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September 30, 2014 and 2013

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

	2013					
	Less Than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Federal agencies	$ 14,697,187	$ 293,996	$	$	$ 14,697,187	$ 293,996
State and municipal obligations	12,305,284	609,538	733,997	47,483	13,039,281	657,021
Other asset backed securities			1,990,600	40,339	1,990,600	40,339
Mortgage -backed securities - GSE residential	40,011,050	982,164	10,945,681	224,554	50,956,731	1,206,718
Total temporarily impaired securities	$ 67,013,521	$ 1,885,698	$ 13,670,278	$ 312,376	$ 80,683,799	$ 2,198,074

Federal Agencies, SBA Pools, Other Asset-Backed Securities, and Mortgage-Backed Securities - GSE Residential

The unrealized losses on the Company s investment in federal agencies, SBA pools, other asset-backed securities, and mortgage-backed securities were caused by changes in market interest rates. The Company expects to recover the amortized cost basis over the term of the securities. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at September 30, 2014.

State and Municipal Obligations

The unrealized losses on the Company s investments in securities of state and municipal obligations were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost bases of the investments. Because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at September 30, 2014.

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September 30, 2014 and 2013

Note 4: Loans and Allowance

	2014	2013
Residential real estate loans	$ 142,280,336	$ 148,720,267
Commercial real estate loans	42,375,040	41,021,173
Commercial loans	26,694,117	20,870,103
Home equity/improvement loans	17,159,538	17,623,408
Consumer loans	3,110,628	2,923,833
	231,619,659	231,158,784
Less:		
Undisbursed portion of loans	254,186	399,965
Deferred loan fees and discounts	485,075	528,121
Allowance for loan losses	1,980,170	2,302,824
	2,719,431	3,230,910
Total loans	$ 228,900,228	$ 227,927,874

The risk characteristics of each loan portfolio segment are as follows:

Commercial loans are primarily 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 include a personal guarantee. 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 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 generally 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 more adversely affected by conditions in the real estate markets or in the general economy. The characteristics of properties securing the Company s commercial real estate portfolio are diverse, but with geographic locations almost entirely in the Company s market area. Management monitors and evaluates commercial real estate loans based on collateral, geography and risk grade criteria. In general, the Company avoids financing single purpose projects unless other underwriting factors are present to help mitigate risk. In addition, management tracks the level of owner-occupied commercial real estate versus nonowner-occupied loans.

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Residential real estate, home equity/improvement and consumer loans consist of two segments residential mortgage loans and personal loans. For residential mortgage loans that are secured by 1-4 family residences and are generally owner-occupied, the Company generally establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Home equity loans are typically secured by a subordinate interest in 1-4 family residences, and consumer personal loans are secured by consumer personal assets, such as automobiles or recreational vehicles. Some consumer personal loans are unsecured, such as small installment loans and certain lines of credit. Repayment of these loans is primarily dependent on the personal income of the borrowers, which can be impacted by economic conditions in their market areas, such as unemployment levels. Repayment can also be impacted by changes in property values on residential properties. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

Activity in the allowance for loan losses is as follows:

	2014					
	Residential Real Estate	**Commercial Real Estate**	**Commercial**	**Home Equity/ Improvement**	**Consumer**	**Total**
Beginning Balance	$ 1,525,995	$ 361,419	$ 188,637	$ 196,247	$ 30,526	$ 2,302,824
Provision (credit)	481,833	(74,573)	(29,059)	(7,243)	14,292	385,250
Loans charged off	(604,356)	(28,521)		(61,051)	(27,892)	(721,820)
Recoveries	2,130			528	11,258	13,916
Ending Balance	$ 1,405,602	$ 258,325	$ 159,578	$ 128,481	$ 28,184	$ 1,980,170

	2013					
	Residential Real Estate	**Commercial Real Estate**	**Commercial**	**Home Equity/ Improvement**	**Consumer**	**Total**
Beginning Balance	$ 1,583,094	$ 379,097	$ 137,045	$ 208,917	$ 20,333	$ 2,328,486
Provision (credit)	177,986	(17,678)	51,592	18,619	33,231	263,750
Loans charged off	(235,466)			(31,289)	(36,425)	(303,180)
Recoveries	381				13,387	13,768
Ending Balance	$ 1,525,995	$ 361,419	$ 188,637	$ 196,247	$ 30,526	$ 2,302,824

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September 30, 2014 and 2013

The following tables present the balance in the allowance for loan losses and the recorded investment in loans based on the portfolio segment and impairment method as of September 30, 2014 and 2013:

	September 30, 2014					
	Residential Real Estate	Commercial Real Estate	Commercial	Home Equity/ Improvement	Consumer	Total
Allowance Balances:						
Individually evaluated for impairment	$	$	$	$	$	$
Collectively evaluated for impairment	1,405,602	258,325	159,578	128,481	28,184	1,980,170
Total allowance for loan losses	$ 1,405,602	$ 258,325	$ 159,578	$ 128,481	$ 28,184	$ 1,980,170
Loan Balances:						
Individually evaluated for impairment	$ 2,426,969	$ 631,153	$ 788,949	$ 185,852	$ 8,419	$ 4,041,342
Collectively evaluated for impairment	139,853,367	41,743,887	25,905,168	16,973,686	3,102,209	227,578,317
Total loan balances	$ 142,280,336	$ 42,375,040	$ 26,694,117	$ 17,159,538	$ 3,110,628	$ 231,619,659

	September 30, 2013					
	Residential Real Estate	Commercial Real Estate	Commercial	Home Equity/ Improvement	Consumer	Total
Allowance Balances:						
	$ 241,397	$ 60,890	$	$ 59,186	$	$ 361,473

Individually evaluated for impairment						
Collectively evaluated for impairment	1,284,598	300,529	188,637	137,061	30,526	1,941,351
Total allowance for loan losses	$ 1,525,995	$ 361,419	$ 188,637	$ 196,247	$ 30,526	$ 2,302,824
Loan Balances:						
Individually evaluated for impairment	$ 3,025,710	$ 819,168	$ 45,248	$ 181,246	$ 1,847	$ 4,073,219
Collectively evaluated for impairment	145,694,557	40,202,005	20,824,855	17,442,162	2,921,986	227,085,565
Total loan balances	$ 148,720,267	$ 41,021,173	$ 20,870,103	$ 17,623,408	$ 2,923,833	$ 231,158,784

Management s general practice is to proactively charge down loans individually evaluated for impairment to the fair value of the underlying collateral.

Consistent with regulatory guidance, charge-offs on all loan segments are taken when specific loans, or portions thereof, are considered uncollectible. The Company s policy is to promptly charge these loans off in the period the uncollectible loss is reasonably determined.

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For all loan portfolio segments except 1-4 family residential properties and consumer, the Company promptly charges off loans, or portions thereof, when available information confirms that specific loans are uncollectible based on information that includes, but is not limited to, (1) the deteriorating financial condition of the borrower, (2) declining collateral values, and/or (3) legal action, including bankruptcy, that impairs the borrower s ability to adequately meet its obligations. For impaired loans that are considered to be solely collateral dependent, a partial charge-off is recorded when a loss has been confirmed by an updated appraisal or other appropriate valuation of the collateral.

The Company charges off 1-4 family residential and consumer loans, or portions thereof, when the Company reasonably determines the amount of the loss. The Company adheres to timeframes established by applicable regulatory guidance, which provides for the charge-down of 1-4 family first and junior lien mortgages to the net realizable value, less costs to sell when the loan is 180 days past due, charge-off of unsecured open-end loans when the loan is 180 days past due, and charge-down to the net realizable value when other secured loans are 120 days past due. Loans at these respective delinquency thresholds for which the Company can clearly document that the loan is both well-secured and in the process of collection, such that collection will occur regardless of delinquency status, need not be charged off.

The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the prior three years. Management believes the historical loss experience methodology is appropriate in the current economic environment, as it captures loss rates that are comparable to the current period being analyzed.

The following tables present the credit risk profile of the Company s loan portfolio based on rating category and payment activity as of September 30, 2014 and 2013:

	September 30, 2014					
	Residential Real Estate	**Commercial Real Estate**	**Commercial**	**Home Equity/ Improvement**	**Consumer**	**Total**
Grade:						
Pass (1-4)	$ 140,422,184	$ 42,028,932	$ 25,905,167	$ 17,005,369	$ 3,102,209	$ 228,463,861
Special Mention (5)	398,798	242,304	671,666	61,757	7,824	1,382,349
Substandard (6)	1,459,354	103,804	117,284	92,412	595	1,773,449
Doubtful (7)						
Loss (8)						
Total	$ 142,280,336	$ 42,375,040	$ 26,694,117	$ 17,159,538	$ 3,110,628	$ 231,619,659

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	September 30, 2013					
	Residential Real Estate	**Commercial Real Estate**	**Commercial**	**Home Equity/ Improvement**	**Consumer**	**Total**
Grade:						
Pass (1-4)	$ 146,245,491	$ 40,028,312	$ 20,824,855	$ 17,446,936	$ 2,923,833	$ 227,469,427
Special Mention (5)	439,407	729,577		9,345		1,178,329
Substandard (6)	2,035,369	263,284	45,248	167,127		2,511,028
Doubtful (7)						
Loss (8)						
Total	$ 148,720,267	$ 41,021,173	$ 20,870,103	$ 17,623,408	$ 2,923,833	$ 231,158,784

Internal Risk Categories

Loan grades are numbered 1 through 8. Grades 1 through 4 are considered satisfactory grades. The grade of 5, or Watch or Special Mention, represents loans of lower quality and is considered criticized. The grades of 6, or Substandard, and 7, or Doubtful, refer to assets that are classified. The use and application of these grades by the bank will be uniform and shall conform to the bank s policy.

Prime (1) Loans are of superior quality with excellent credit strength and repayment ability providing a nominal credit risk.

Good (2) Loans are of above average credit strength and repayment ability providing only a minimal credit risk.

Satisfactory (3) Loans of reasonable credit strength and repayment ability providing an average credit risk due to one or more underlying weaknesses.

Acceptable (4) Loans of the lowest acceptable credit strength and weakened repayment ability providing a cautionary credit risk due to one or more underlying weaknesses. New borrowers are typically not underwritten within this classification.

Special Mention (5) A special mention asset has potential weaknesses that deserve management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution s credit position at some future date. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification. Ordinarily, special mention credits have characteristics which corrective management action would remedy.

Substandard (6) Loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful (7) Loans classified as doubtful have all the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of current known facts, conditions and values, highly questionable and improbable.

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Loss (8) Loans classified as loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off even though partial recovery may be affected in the future.

The following tables present the Company s loan portfolio aging analysis as of September 30, 2014 and 2013:

	September 30, 2014						
	30-59 Past Due	60-89 Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Loans > 90 Days and Accruing
Residential real estate	$ 484,469	$	$ 139,735	$ 624,204	$ 141,656,132	$ 142,280,336	$
Commercial real estate					42,375,040	42,375,040	
Commercial			5,979	5,979	26,688,138	26,694,117	
Home equity/improvement	64,910		49,682	114,592	17,044,946	17,159,538	
Consumer	3,080			3,080	3,107,548	3,110,628	
Total loans	$ 552,459	$	$ 195,396	$ 747,855	$ 230,871,804	$ 231,619,659	$

	September 30, 2013						
	30-59 Past Due	60-89 Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Loans > 90 Days and Accruing
Residential real estate	$ 281,570	$ 125,143	$ 683,981	$ 1,090,694	$ 147,629,573	$ 148,720,267	$
Commercial real estate	4,656	81,146		85,802	40,935,371	41,021,173	
Commercial					20,870,103	20,870,103	
Home equity/improvement	42,187	7,948	94,440	144,575	17,478,833	17,623,408	
Consumer	722			722	2,923,111	2,923,833	
Total loans	$ 329,135	$ 214,237	$ 778,421	$ 1,321,793	$ 229,836,991	$ 231,158,784	$

The entire balance of a loan is considered delinquent if the minimum payment contractually required to be made is not received by the specified due date.

The following table presents the Company s nonaccrual loans at September 30, 2014 and 2013:

	2014	2013
Residential real estate	$ 139,735	$ 683,981
Commercial	5,979	
Home equity/improvement	49,682	94,440
Total nonaccrual loans	$ 195,396	$ 778,421

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The following tables present impaired loans for the years ended September 30, 2014 and 2013:

	September 30, 2014				
	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Average Investment in Loans	Interest Income Recognized
Impaired loans without a specific valuation allowance:					
Residential real estate	$ 2,426,969	$ 2,475,469	$	$ 2,589,812	$ 144,344
Commercial real estate	631,153	631,153		739,003	42,151
Commercial	788,949	788,949		283,869	36,286
Home equity/improvement	185,852	213,324		188,163	8,506
Consumer	8,419	8,419		2,407	45
Total impaired loans with no related specific reserve	4,041,342	4,117,314		3,803,254	231,332
Impaired loans with a specific valuation allowance:					
Residential real estate					
Commercial real estate					
Commercial					
Home equity/improvement					
Consumer					
Total impaired loans with an allowance recorded					
Total impaired loans	$ 4,041,342	$ 4,117,314	$	$ 3,803,254	$ 231,332

	September 30, 2013				
	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Average Investment in Loans	Interest Income Recognized
Impaired loans without a specific valuation allowance:					

Residential real estate	$ 2,491,695	$ 2,491,695	$	$ 2,524,388	$ 156,369
Commercial real estate	513,472	513,472		564,312	42,643
Commercial	45,248	45,248		74,293	6,315
Home equity/improvement	94,179	94,179		89,051	19,105
Consumer	1,847	1,847		3,478	149
Total impaired loans with no related specific reserve	3,146,441	3,146,441		3,255,522	224,581
Impaired loans with a specific valuation allowance:					
Residential real estate	534,015	534,015	241,397	248,547	17,568
Commercial real estate	305,696	305,696	60,890	316,777	15,565
Commercial					
Home equity/improvement	87,067	87,067	59,186	81,202	7,799
Consumer					
Total impaired loans with an allowance recorded	926,778	926,778	361,473	646,526	40,932
Total impaired loans	$ 4,073,219	$ 4,073,219	$ 361,473	$ 3,902,048	$ 265,513

Interest income on loans individually classified as impaired is recognized on a cash basis after all past due and current principal payments have been made.

Included in the above impaired loan totals were approximately $572,000 and $1,109,000 of loan modifications meeting the definition of troubled debt restructurings that were accruing interest and performing in accordance with their agreements at September 30, 2014 and 2013, respectively.

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Subsequent payments on nonaccrual loans are recorded as a reduction of principal, and interest income is recorded only after principal recovery is reasonably assured. Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collection of interest or principal. The Company requires a period of satisfactory performance of not less than six months before returning a nonaccrual loan to accrual status.

The following tables present information regarding troubled debt restructurings by class for the years ended September 30, 2014 and 2013.

Newly classified troubled debt restructurings:

	September 30, 2014		
	Number of Loans	Pre-Modification Recorded Balance	Post-Modification Recorded Balance
Home equity/improvement	1	$ 17,235	$ 17,235

	September 30, 2013		
	Number of Loans	Pre-Modification Recorded Balance	Post-Modification Recorded Balance
Residential real estate	1	$ 113,885	$ 113,885

The troubled debt restructurings described above increased the allowance for loan losses by $0 and $20,000 and resulted in charge-offs of $0 and $17,000 during the years ended September 30, 2014 and 2013.

Newly restructured loans by type of modification:

	September 30, 2014			
	Interest Only	Term	Combination	Total Modification
Home equity/improvement	$	$ 17,235	$	$ 17,235

	September 30, 2013			
	Interest Only	Term	Combination	Total Modification
Residential real estate	$	$ 113,885	$	$ 113,885

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There were no troubled debt restructurings modified in the past 12 months that subsequently defaulted for the periods ended September 30, 2014 and 2013.

Note 5: Premises and Equipment

	2014	2013
Land and land improvements	$ 1,536,314	$ 1,373,936
Buildings	9,783,943	9,567,291
Equipment	7,733,491	7,193,259
Total cost	19,053,748	18,134,486
Accumulated depreciation	(13,795,937)	(13,199,738)
Net	$ 5,257,811	$ 4,934,748

Note 6: Deposits

	2014	2013
Noninterest-bearing demand deposits	$ 25,514,862	$ 25,564,485
Interest-bearing demand deposits	106,434,831	98,102,923
Savings deposits	80,844,107	74,938,940
Certificates and other time deposits of $ 100,000 or more	47,026,002	48,149,609
Other certificates and time deposits	94,100,452	102,921,864
	$ 353,920,254	$ 349,677,821

Certificates and other time deposits maturing in years ending September 30:

2015	$ 66,511,410
2016	28,649,115
2017	20,429,562
2018	8,460,793
2019	11,421,608

Thereafter	5,653,966
	$ 141,126,454

Deposits from related parties held by the Company at September 30, 2014 and 2013 totaled $2,448,000 and $2,352,000, respectively.

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Note 7: Short-Term Borrowings

	2014	2013
Securities sold under agreements to repurchase	$ 650,379	$ 897,712

At September 30, 2014 and 2013, the securities sold under agreements to repurchase obligations were secured by investment securities and such collateral is held by a safekeeping agent. The maximum amount of outstanding agreements at any month-end during 2014 and 2013 totaled $1,688,000 and $1,913,000 and the average of such agreements for the years ended September 30, 2014 and 2013 totaled $677,000 and $813,000, respectively. The agreements at September 30, 2014 mature daily.

Note 8: Federal Home Loan Bank Advances

Federal Home Loan Bank advances at September 30, 2014 and 2013 totaled $52,217,000 and $39,164,000 and were at various rates ranging from 0.00% to 4.30% maturing at various dates through August 2022. The Federal Home Loan Bank advances are secured by first mortgage loans totaling $136,310,000. Advances are subject to restrictions or penalties in the event of prepayment.

Maturities in years ending September 30	Amount
2015	$ 4,243,415
2016	1,737,304
2017	5,733,711
2018	21,732,560
2019	12,733,778
Thereafter	6,036,375
	$ 52,217,143

Note 9: Loan Servicing

Mortgage loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balance of mortgage loans serviced for others was $58,654,000 and $62,899,000 at September 30, 2014 and 2013, respectively.

	2014	2013

Mortgage-servicing rights		
Balance, beginning of year	$ 271,291	$ 345,391
Servicing rights capitalized	44,376	83,397
Amortization of servicing rights	(125,552)	(157,497)
Balance, end of year	$ 190,115	$ 271,291

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The fair value of servicing rights subsequently measured using the amortization method was as follows:

	2014	2013
Fair value, beginning of period	$ 508,000	$ 456,000
Fair value, end of period	438,000	508,000

Note 10: Income Tax

	2014	2013
Income tax expense		
Currently payable		
Federal	$ 429,124	$ 34,819
State	(22,393)	183
Deferred		
Federal	21,202	112,657
State	57,593	3,617
Total income tax expense	$ 485,526	$ 151,276
Reconciliation of federal statutory to actual tax expense		
Federal statutory income tax at 34%	$ 1,322,549	$ 944,544
Tax-exempt interest	(561,866)	(621,656)
Nondeductible expenses	2,874	2,936
Effect of state income taxes	23,232	2,508
Cash surrender value	(151,399)	(145,859)
Effect of low income housing credits	(70,454)	(67,045)
Other	(79,410)	35,848
Actual tax expense	$ 485,526	$ 151,276

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A cumulative net deferred tax liability is included in other liabilities. The components of the assets are as follows:

	2014	2013
Assets		
Allowance for loan losses	$ 806,411	$ 813,805
Loan fees	197,544	216,763
Other real estate owned		28,247
Federal and State NOL carryforward	202,977	597,880
Alternative minimum tax and low income housing credits	295,657	223,665
Other	261,534	270,075
Total assets	1,764,123	2,150,435
Liabilities		
Depreciation	159,150	210,485
State income tax	31,275	34,651
FHLB of Indianapolis stock dividend	233,251	235,082
Net unrealized gains on securities available for sale	897,975	344,815
Prepaid expenses	648,197	840,735
Other	179,203	223,750
Total liabilities	2,149,051	1,889,518
Net deferred tax asset (liability) before valuation allowance	(384,928)	260,917
Valuation allowance		
Beginning balance	(216,865)	(128,028)
Changing during the period	13,888	(88,837)
Ending balance	(202,977)	(216,865)
Net deferred asset (liability)	$ (587,905)	$ 44,052

Retained earnings at September 30, 2014 include approximately $8,102,000 for which no deferred income tax liability has been recognized. This amount represents an allocation of income to bad debt deductions as of June 30, 1988 for tax purposes only. Reduction of amounts so allocated for purposes other than tax bad debt losses or adjustments arising from carryback of net operating losses would create income for tax purposes only, which income would be subject to the then current corporate income tax rate. The unrecorded deferred income tax liability on the above amount was approximately $2,755,000 at September 30, 2014.

At September 30, 2014, the Company had credit carryforwards totaling $296,000, which represents alternative minimum tax with no expiration date.

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At September 30, 2014, the Company had state net operating losses totaling $2,495,000 that begin expiring in 2024.

Management believes that the Company will be able to utilize the benefits recorded for federal and state carryforwards within the allotted time periods, except for the amount represented by the valuation allowance. The entire valuation allowance has been recorded for the possible inability to use the state net operating loss carryover.

The Bank s tax years still subject to examination by taxing authorities are years subsequent to 2010.

Note 11: Commitments and Contingent Liabilities

In the normal course of business, there are outstanding commitments and contingent liabilities, such as commitments to extend credit, which are not included in the accompanying consolidated financial statements. The Company s exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit is represented by the contractual or notional amount of those instruments. The Company uses the same credit policies in making such commitments as it does for instruments that are included in the consolidated balance sheets.

Financial instruments whose contract amount represents credit risk at September 30, 2014 and 2013 consisted of commitments to extend credit totaling $85,815,000 and $78,719,000, respectively.

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. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. 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 residential real estate, income-producing commercial properties, or other assets of the borrower.

The Company has employment agreements with three officers, which include provisions for payment to them of three years salary, respectively, in the event of their termination in connection with any change in ownership or control of the Company, other than by agreement. The agreements have terms of three years, which may be extended annually for successive periods of one year.

The Company and subsidiaries are also subject to possible claims and lawsuits which arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate determination of such possible claims or lawsuits will not have a material adverse effect on the consolidated financial position, results of operations and cash flows of the Company.

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Note 12: Dividends and Capital Restrictions

Without prior approval, current regulations allow the Bank to pay dividends to the Company not exceeding net profits (as defined) for the current calendar year to date plus those for the previous two years. The Bank normally restricts dividends to a lesser amount because of the need to maintain an adequate capital structure.

Note 13: Regulatory Capital

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies and are assigned to a capital category. The assigned capital category is largely determined by ratios that are calculated according to the regulations. The ratios are intended to measure capital relative to assets and credit risk associated with those assets and off-balance sheet exposures of the entity. The capital category assigned to an entity can also be affected by qualitative judgments made by regulatory agencies about the risk inherent in the entity s activities that are not part of the calculated ratios.

There are five capital categories defined in the regulations, ranging from well capitalized to critically undercapitalized. Classification of a bank in any of the undercapitalized categories can result in actions by regulators that could have a material effect on a bank s operations. At September 30, 2014, the Bank was categorized as well capitalized and met all subject capital adequacy requirements. There are no conditions or events since September 30, 2014 that management believes have changed the Bank s classification.

The Company s actual and required capital amounts and ratios are as follows:

	2014					
	Actual		Required for Adequate Capital [1]		To Be Well Capitalized [1]	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total risk-based capital [1] (to risk-weighted assets)	$ 53,854,000	22.09%	$ 19,507,000	8.00%	$ 24,384,000	10.00%
Tier 1 risk-based capital [1] (to risk-weighted assets)	51,874,000	21.27%	9,754,000	4.00%	14,630,000	6.00%
Core capital [1] (to adjusted total assets)	51,874,000	11.03%	18,816,000	4.00%	23,521,000	5.00%
Core capital [1] (to adjusted tangible assets)	51,874,000	11.03%	9,408,000	2.00%	NA	NA
Tangible capital [1] (to adjusted total assets)	51,874,000	11.03%	7,056,000	1.50%	NA	NA

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	2013					
	Actual		Required for Adequate Capital [1]		To Be Well Capitalized [1]	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total risk-based capital [1] (to risk-weighted assets)	$ 53,666,000	22.45%	$ 19,121,000	8.00%	$ 23,902,000	10.00%
Tier 1 risk-based capital [1] (to risk-weighted assets)	51,363,000	21.49%	9,561,000	4.00%	14,341,000	6.00%
Core capital [1] (to adjusted total assets)	51,363,000	11.39%	18,036,000	4.00%	22,544,000	5.00%
Core capital [1] (to adjusted tangible assets)	51,363,000	11.39%	9,018,000	2.00%	NA	NA
Tangible capital [1] (to adjusted total assets)	51,363,000	11.39%	6,763,000	1.50%	NA	NA

[1] As defined by Regulatory Agencies

Note 14: Employee Benefit Plans

Prior to August 1, 2007, the Company provided pension benefits for substantially all of its employees through its participation in a pension fund known as the Pentegra Defined Benefit Plan (Pentegra Plan). The Company chose to freeze the Pentegra Plan effective August 1, 2007. The trustees of the Financial Institutions Retirement Fund administer the Pentegra Plan, employer identification number 13-5645888 and plan number 333. This plan operates as a multi-employer plan for accounting purposes and as a multiple-employer plan under the *Employee Retirement Income Security Act of 1974* and the Internal Revenue Code. There are no collective bargaining agreements in place that require contributions to the Pentegra Plan. The Pentegra Plan is a single plan under Internal Revenue Code 413(c) and, as a result, all of the assets stand behind all of the liabilities.

The risks of participating in these multiemployer plans are different from single-employer plans in the following aspects:

1. Assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers.

2. If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.

3. If the Company chooses to stop participating in the multiemployer plan, the Company may be required to pay the plan an amount based on the underfunded status of the plan, referred to as a withdrawal liability.

Pension expense and contributions related to this plan was $300,000 and $325,000 for the years ended September 30, 2014 and 2013. Funding status of the plan as of the beginning of the plan years for 2014 and 2013 (July 1^{st}) was 118.26% and 106.73%, respectively.

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Total contributions to the Pentegra Plan were $136,478,000 and $196,473,000 for the plan years ended June 30, 2014 and 2013, respectively. The Company s contributions to the Pentegra Plan were not more than 5% of the total contributions to the plan. There have been no significant changes that affect the comparability of the 2014 and 2013 contributions.

A profit-sharing plan is maintained for the benefit of substantially all of the Company s employees and allows for both employee and Company contributions. The Company contribution consists of a matching contribution of 100 percent for 2014 and 2013, up to 6 percent of eligible employee compensation. The Company may also contribute an additional discretionary amount to each employee, regardless of participation in the matching program. The Company s contribution to the plan, for the matching program was approximately $211,000 and $226,000 for 2014 and 2013. The Company s contribution for the discretionary program was $0 for 2014 and 2013.

Note 15: Earnings Per Share

For the years ended September 30, 2014 and 2013, no options to purchase shares of common stock were outstanding. Earnings per share (EPS) were computed as follows:

		2014	
	Income	Weighted-Average Shares	Per-Share Amount
Basic Earnings Per Share			
Net income available to common stockholders	$ 3,404,323	2,313,219	$ 1.47
Effect of Dilutive Securities			
Stock options			
Diluted Earnings Per Share			
Income available to common stockholders and assumed conversions	$ 3,404,323	2,313,219	$ 1.47

		2013	
	Income	Weighted-Average Shares	Per-Share Amount

Basic Earnings Per Share			
Net income available to common stockholders	$ 2,626,795	2,357,792	$ 1.11
Effect of Dilutive Securities			
Stock options			
Diluted Earnings Per Share			
Income available to common stockholders and assumed conversions	$ 2,626,795	2,357,792	$ 1.11

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Note 16: Fair Values of Financial Instruments

Fair value 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 measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

Level 1	Quoted prices in active markets for identical assets
Level 2	Observable inputs other than Level 1 prices, such as quoted prices for similar assets; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets
Level 3	Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy.

Available-for-Sale Securities

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. Level 2 securities include U.S. Government agency securities, mortgage-backed securities and CMO s and obligations of state and municipals. Matrix pricing is a mathematical technique widely used in the banking industry to value investment securities without relying exclusively on quoted prices for specific investment securities but rather relying on the investment securities relationship to other benchmark quoted investment securities. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

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The following tables present the fair value measurements of assets recognized in the accompanying consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at September 30, 2014 and 2013:

	2014 Fair Value Measurements Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available for sale				
Federal agencies	$ 19,561,097	$	$ 19,561,097	$
State and municipal obligations	60,172,620		60,172,620	
SBA Pools	2,789,289		2,789,289	
Other asset-backed securities	2,018,800		2,018,800	
Mortgage-backed securities - GSE - residential	85,222,914		85,222,914	
	$ 169,764,720	$	$ 169,764,720	$

	2013 Fair Value Measurements Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)

Available for sale				
Federal agencies	$ 20,428,759	$	$ 20,428,759	$
State and municipal obligations	61,259,621		61,259,621	
SBA Pools	987,409		987,409	
Other asset-backed securities	1,990,600		1,990,600	
Mortgage-backed securities -				
GSE - residential	96,272,354		96,272,354	
	$ 180,938,743	$	$ 180,938,743	$

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Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy.

Collateral-Dependent Impaired Loans, Net of ALLL

The estimated fair value of collateral-dependent impaired loans is based on the appraised fair value of the collateral, less estimated cost to sell. Collateral-dependent impaired loans are classified within Level 3 of the fair value hierarchy.

The Company considers the appraisal or evaluation as the starting point for determining fair value and then considers other factors and events in the environment that may affect the fair value. Appraisals of the collateral underlying collateral-dependent loans are obtained when the loan is determined to be collateral-dependent and subsequently as deemed necessary by the Chief Financial Officer. Appraisals are reviewed for accuracy and consistency by the Chief Financial Officer. Appraisers are selected from the list of approved appraisers maintained by management. The appraised values are reduced by discounts to consider lack of marketability and estimated cost to sell if repayment or satisfaction of the loan is dependent on the sale of the collateral. These discounts and estimates are developed by the Chief Financial Officer comparison to historical results.

Other Real Estate Owned

Other real estate owned is reported at fair value, less cost to sell and is measured using Level 3 inputs within the fair value hierarchy. Level 3 inputs for foreclosed real estate included third-party appraisals adjusted for cost to sell.

The following tables present the fair value measurement of assets at fair value on a nonrecurring basis and the level within the fair value hierarchy in which the fair value measurements fall at September 30, 2014 and 2013.

		2014 Fair Value Measurements Using		
	Fair Value	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**

Impaired loans (collateral dependent)	$ 156,000	$	$	$ 156,000

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		2013 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans (collateral dependent)	$ 950,171	$	$	$ 950,171
Other real estate owned	14,925			14,925

Unobservable (Level 3) Inputs

The following table presents quantitative information about unobservable inputs used in recurring and nonrecurring Level 3 fair value measurements.

	Fair Value at September 30, 2014	Valuation Technique	Unobservable Inputs	Discount
Collateral-dependent impaired loans	$ 156,000	Market comparable properties	Marketability discount	15%

	Fair Value at September 30, 2013	Valuation Technique	Unobservable Inputs	Discount
Collateral-dependent impaired loans	$ 950,171	Market comparable properties	Marketability discount	15-65%
Other real estate owned	14,925	Market comparable properties	Comparability adjustments	40%

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

Cash and Cash Equivalents - The fair value of cash and cash equivalents approximates carrying value.

Interest-Bearing Time Deposits - The fair value of interest-bearing time deposits approximates carrying value.

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Loans and Loans Held for Sale - For both short-term loans and variable-rate loans that reprice frequently, and with no significant change in credit risk, fair values are based on carrying values. The fair value for other loans is estimated using discounted cash flow analyses using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality.

Interest Receivable/Payable - The fair values of interest receivable/payable approximate carrying values.

FHLB Stock - Fair value of FHLB stock is based on the price at which it may be resold to the FHLB.

Deposits - The fair values of noninterest-bearing, interest-bearing demand and savings accounts are equal to the amount payable on demand at the balance sheet date. The carrying amounts for variable-rate, fixed-term certificates of deposit approximate their fair values at the balance sheet date. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on such time deposits.

Short-Term Borrowings - The fair value of short-term borrowings approximates carrying value.

Federal Home Loan Bank Advances - The fair value of these borrowings is estimated using a discounted cash flow calculation, based on current rates for similar advances.

The following table presents estimated fair values of the Company s financial instruments and their related carrying value at year end.

	2014		**2013**	
	Carrying Amount	**Fair Value**	**Carrying Amount**	**Fair Value**
Assets				
Cash and cash equivalents	$ 17,658,180	$ 17,658,180	$ 6,197,988	$ 6,197,988
Interest-bearing time deposits	12,766,000	12,766,000	5,899,000	5,899,000
Investment securities held to maturity	10,984,331	10,951,776		
Loans, including loans held for sale	229,144,878	229,144,878	228,360,874	228,169,874
FHLB stock	4,127,700	4,127,700	4,127,700	4,127,700
Interest receivable	2,510,239	2,510,239	2,477,008	2,477,008
Liabilities				
Deposits	353,920,254	354,807,545	349,677,821	351,267,821
Short-term borrowings	650,379	650,379	897,712	897,712
Federal Home Loan Bank advances	52,217,143	52,795,143	39,163,522	40,404,522
Interest payable	74,094	74,094	81,952	81,952

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Notes to Consolidated Financial Statements

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Note 17: Condensed Financial Information (Parent Company Only)

Presented below is condensed financial information as to financial position, results of operations and cash flows of the Company.

Condensed Balance Sheets

	2014	2013
Assets		
Cash	$ 4,079,446	$ 4,315,965
Investment in subsidiaries	55,984,336	54,425,594
Other assets	1,176,120	14,142
Total assets	$ 61,239,902	$ 58,755,701
Liabilities		
Dividends payable on common stock	$ 462,372	$ 462,858
Other	12,900	370
Total liabilities	475,272	463,228
Stockholders Equity		
Common stock	2,311,858	2,314,288
Retained earnings	56,771,502	55,273,078
Accumulated other comprehensive income	1,681,270	705,107
	60,764,630	58,292,473
Total liabilities and stockholders equity	$ 61,239,902	$ 58,755,701

Condensed Statements of Income

	2014	2013
Income	$ 2,937,500	$ 2,575,000
Expenses	162,416	154,118

Income before distribution in excess of income of subsidiaries and income tax expense	2,775,084	2,420,882
Undistributed income (distribution in excess of income) of subsidiaries	582,839	153,913
Income before income tax	3,357,923	2,574,795
Income tax benefit	(46,400)	(52,000)
Net income	$ 3,404,323	$ 2,626,795

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Condensed Statements of Cash Flows

	2014	2013
Cash flows from operating activities		
Net income	$ 3,404,323	$ 2,626,795
Items not providing cash		
Distributions in excess of income (undistributed income) of subsidiaries	(582,579)	(153,681)
Other adjustments	(149,448)	(1,143)
Net cash provided by operating activities	2,672,296	2,471,971
Cash flows from investing activities - purchase of preferred stock	(1,000,000)	
Cash flows from financing activities		
Stock repurchased	(58,070)	(1,719,023)
Cash dividends	(1,850,745)	(1,897,507)
Net cash used in financing activities	(1,908,815)	(3,616,530)
Net change in cash	(236,519)	(1,144,559)
Cash at beginning of year	4,315,965	5,460,524
Cash at end of year	$ 4,079,446	$ 4,315,965

Note 18: Subsequent Events

Subsequent events have been evaluated through the date of the Independent Auditor s Report, which is the date the consolidated financial statements were available to be issued.

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Consolidated Condensed Balance Sheets

	March 31, 2015 (Unaudited)	September 30, 2014
Assets		
Cash and cash equivalents	$ 22,218,408	$ 17,658,180
Interest-bearing time deposits	10,065,000	12,766,000
Investment securities available for sale	175,404,176	169,764,720
Investment securities held to maturity (fair value of $10,095,187 and $10,951,776)	10,039,346	10,984,331
Mortgage loans held for sale	215,250	244,650
Loans, net of allowance for loan losses of $1,942,782 and $1,980,170	227,816,253	228,900,228
Premises and equipment, net	5,043,062	5,257,811
Federal Home Loan Bank of Indianapolis stock, at cost	3,506,500	4,127,700
Goodwill	2,330,198	2,330,198
Cash surrender value of life insurance	13,802,793	13,603,323
Other assets	6,481,969	5,546,867
Total assets	$ 476,922,955	$ 471,184,008
Liabilities		
NOW and savings deposits	$ 222,308,544	$ 212,793,800
Certificates of deposit	135,983,347	141,126,454
Total deposits	358,291,891	353,920,254
Short-term borrowings	185,679	650,379
Federal Home Loan Bank advances	51,497,385	52,217,143
Other liabilities	4,713,699	3,631,602
Total liabilities	414,688,654	410,419,378
Commitments and Contingencies		
Stockholders Equity		
Preferred stock, $1 par value		
Authorized and unissued - 5,000,000 shares		
Common stock, $1 par value		
Authorized - 7,000,000 shares		
Issued and outstanding - 2,311,858 and 2,311,858 shares	2,311,858	2,311,858
Retained earnings	57,321,400	56,771,502
Accumulated other comprehensive income	2,601,043	1,681,270
Total stockholders equity	62,234,301	60,764,630

Total liabilities and stockholders equity	$ 476,922,955	$ 471,184,008

See Notes to Consolidated Financial Statements

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Peoples Bancorp

Consolidated Condensed Statements of Income

Three and Six Months Ended March 31, 2015 and 2014

	Three Months Ended March 31,		Six Months Ended March 31,	
	2015	**2014**	**2015**	**2014**
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
Interest Income				
Loans	$ 2,546,581	$ 2,700,735	$ 5,150,081	$ 5,436,112
Investment securities	1,078,291	1,157,477	2,119,225	2,262,359
Other interest and dividend income	84,015	74,549	176,513	127,886
	3,708,887	3,932,761	7,445,819	7,826,357
Interest Expense				
Deposits				
NOW and savings deposits	49,285	44,814	103,950	90,534
Certificates of deposit	388,245	417,062	789,113	853,663
Short-term borrowings	375	293	709	689
Federal Home Loan Bank advances	292,093	299,377	589,751	581,743
	729,998	761,546	1,483,523	1,526,629
Net Interest Income	2,978,889	3,171,215	5,962,296	6,299,728
Provision for loan losses	34,500	133,000	69,250	177,500
Net Interest Income After Provision for Loan Losses	2,944,389	3,038,215	5,893,046	6,122,228
Noninterest Income				
Fiduciary activities	179,551	148,605	383,466	304,355
Fees and service charges	386,897	392,014	758,993	768,595
Net realized gains on available-for-sale securities	48,502	102,507	312,457	102,507
Gain on sale of loans	29,091	32,066	43,807	76,901
Cash surrender value	96,869	102,764	199,470	208,397
Other income	159,246	89,677	186,482	97,581
Total other income	900,156	867,633	1,884,675	1,558,336
Noninterest Expenses				
Salaries and employee benefits	1,750,415	1,798,875	3,541,427	3,577,372
Net occupancy expense	255,897	280,616	490,674	533,765
Equipment expense	172,638	160,131	337,309	305,918
Data processing expense	164,300	220,976	315,795	404,840

Deposit insurance expense	60,593	66,000	118,356	124,196
Other expenses	736,629	537,405	1,312,480	1,033,104
Total other expenses	3,140,472	3,064,003	6,116,041	5,979,195
Income Before Income Tax	704,073	841,845	1,661,680	1,701,369
Income tax expense	47,495	96,193	187,039	195,705
Net Income	$ 656,578	$ 745,652	$ 1,474,641	$ 1,505,664
Basic and Diluted Earnings Per Share	$ 0.28	$ 0.32	$ 0.64	$ 0.65
Weighted-Average Shares Outstanding - Basic and Diluted	2,311,858	2,313,788	2,311,858	2,313,912

See Notes to Consolidated Financial Statements

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Peoples Bancorp

Consolidated Condensed Statements of Comprehensive Income

Three and Six Months Ended March 31, 2015 and 2014

(Unaudited)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2015	**2014**	**2015**	**2014**
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
Net Income	$ 656,578	$ 745,652	$ 1,474,641	$ 1,505,664
Other Comprehensive Income				
Change in net unrealized gain on securities available for sale, net of taxes of $384,846, $447,393, $580,058 and $324,732	747,054	868,470	1,125,995	630,363
Less reclassification adjustment for realized gains included in net income, net of taxes of $16,491, $34,852, $106,235 and $34,852	32,011	67,655	206,222	67,655
Total other comprehensive income	715,043	800,815	919,773	562,708
Comprehensive Income	$ 1,371,621	$ 1,546,467	$ 2,394,414	$ 2,068,372

See Notes to Consolidated Financial Statements

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Peoples Bancorp

Consolidated Condensed Statements of Stockholders Equity

Six Months Ended March 31, 2015 (Unaudited)

	Common Stock Outstanding	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balances , September 30, 2014	2,311,858	2,311,858	56,771,502	1,681,270	60,764,630
Net income			1,474,641		1,474,641
Other comprehensive income				919,773	919,773
Cash dividends ($.80 per share)			(924,743)		(924,743)
Repurchase of common stock					
Balances , March 31, 2015	2,311,858	$ 2,311,858	$ 57,321,400	$ 2,601,043	$ 62,234,301

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Peoples Bancorp

Consolidated Condensed Statements of Cash Flows

Six Months Ended March 31, 2015 and 2014

(Unaudited)

	Six Months Ended March 31, 2015	Six Months Ended March 31, 2014
Operating Activities		
Net income	$ 1,474,641	$ 1,505,664
Items not requiring (providing) cash		
Provision for loan losses	69,250	177,500
Depreciation and amortization	290,380	269,929
Investment securities amortization, net	1,032,640	990,720
Loans originated for sale	(1,221,543)	(1,844,900)
Proceeds from sales of loans	1,294,750	2,263,601
Gain on sale of loans	(43,807)	(76,901)
Gain on real estate owned	(69,880)	(50,104)
Accretion of deferred loan fees	(44,297)	(51,380)
Net realized gains on available-for-sale securities	(312,457)	(102,507)
Increase in cash surrender value of life insurance	(199,470)	(208,397)
Change in		
Interest receivable	435,618	330,559
Interest payable	1,159	3,448
Other adjustments	(1,067,377)	(354,537)
Net cash provided by operating activities	1,639,607	2,852,695
Investing Activities		
Net change in interest-bearing time deposits	2,701,000	(1,715,000)
Purchases of securities available for sale	(22,703,514)	(11,455,188)
Purchase of securities held to maturity		(10,269,047)
Proceeds from maturities, call and paydowns of securities available for sale	12,079,422	17,225,243
Proceeds from maturities, call and paydowns of securities held to maturity	897,904	508,817
Proceeds from sales of securities available for sale	5,763,527	1,687,507
Net change in loans	950,801	(6,582,992)
Purchases of premises and equipment	(75,631)	(818,634)
Proceeds from repurchase of FHLB stock	621,200	
Proceeds from sale of foreclosed real estate	423,476	189,629
Net cash provided by (used in) investing activities	658,185	(11,229,665)
Financing Activities		

Net change in		
NOW and savings deposits	9,514,744	8,873,435
Certificates of deposit	(5,143,107)	(3,791,651)
Short -term borrowings	(464,700)	(344,551)
Proceeds from Federal Home Loan Bank advances		16,000,000
Repayment of Federal Home Loan Bank advances	(719,758)	(4,724,444)
Cash dividends	(924,743)	(924,743)
Repurchase of common stock		(12,522)
Net provided by financing activities	2,262,436	15,075,524
Net Change in Cash and Cash Equivalents	4,560,228	6,698,554
Cash and Cash Equivalents, Beginning of Year	17,658,180	6,197,988
Cash and Cash Equivalents, End of Year	$ 22,218,408	$ 12,896,542
Additional Cash Flows Information		
Interest paid	$ 1,482,364	$ 1,523,181
Income tax paid (refund)	(7,528)	
Transfer to other real estate from loans	108,221	362,695

See Notes to Consolidated Financial Statements

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Peoples Bancorp

Notes to Consolidated Condensed Financial Statements

March 31, 2015 and 2014

Note 1: Basis of Presentation

The accounting policies followed in the preparation of the interim consolidated condensed financial statements included in this joint proxy statement/prospectus are consistent with those used in the preparation of annual consolidated financial statements. The interim consolidated condensed financial statements reflect all normal and recurring adjustments, which are necessary, in the opinion of management of Peoples Bancorp (the Company), for a fair statement of results for the interim periods presented. Results for the six months ended March 31, 2015 are not necessarily indicative of the results that may be expected for the year ending September 30, 2015 or any other period.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for the interim financial period and with the instructions generally applicable to a quarterly report on Form 10-Q. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. These consolidated condensed financial statements should be read in conjunction with the audited consolidated financial statements and notes for the year ended September 30, 2014 included in this joint proxy statement/prospectus, beginning at page F-1. The consolidated condensed balance sheet of the Company as of September 30, 2014 has been derived from the audited consolidated balance sheet as of that date.

Note 2: Earnings Per Share

For the three-month and six-month periods ending March 31, 2015 and 2014, no options to purchase shares of common stock were outstanding. Earnings per share were computed as follows:

(Unaudited)	**Three Months Ended March 31, 2015**	**2014**
Basic and Diluted Earnings Per Share		
Net income available to common stockholders	$ 656,578	$ 745,652
Average common shares outstanding for basic and dilutive earnings per share	2,311,858	2,313,788
Basic and diluted earnings per share	$ 0.28	$ 0.32

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(Unaudited)	Six Months Ended March 31, 2015	2014
Basic and Diluted Earnings Per Share		
Net income available to common stockholders	$ 1,474,641	$ 1,505,664
Average common shares outstanding for basic and dilutive earnings per share	2,311,858	2,313,912
Basic and diluted earnings per share	$ 0.64	$ 0.65

Note 3: Investment Securities

(Unaudited) March 31, 2015	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
Federal agencies	$ 30,236,507	$ 143,027	$ 35,200	$ 30,344,334
State and municipal obligations	54,497,802	3,173,404	26,310	57,644,896
SBA Pools	2,746,659	65,944		2,812,603
Other asset backed securities	1,997,185		5,021	1,992,164
Mortgage-backed securities - Government-sponsored entities (GSE) -residential	81,911,316	1,055,342	356,479	82,610,179
Total available for sale	171,389,469	4,437,717	423,010	175,404,176
Held to maturity				
State and municipal obligations	2,038,000			2,038,000
Mortgage-backed securities - Government-sponsored entities (GSE) -residential	8,001,346	62,646	6,805	8,057,187
Total held to maturity	10,039,346	62,646	6,805	10,095,187
Total investment securities	$ 181,428,815	$ 4,500,363	$ 429,815	$ 185,499,363

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	September 30, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
Federal agencies	$ 19,758,680	$ 3,797	$ 201,380	$ 19,561,097
State and municipal obligations	57,466,694	2,892,195	186,269	60,172,620
SBA Pools	2,796,373	2,899	9,983	2,789,289
Other asset backed securities	2,025,224		6,424	2,018,800
Mortgage-backed securities - Government-sponsored entities (GSE) -residential	85,155,037	916,294	848,417	85,222,914
Total available for sale	167,202,008	3,815,185	1,252,473	169,764,720
Held to maturity				
State and municipal obligations	2,160,000			2,160,000
Mortgage-backed securities - Government-sponsored entities (GSE) -residential	8,824,331	7,845	40,400	8,791,776
Total held to maturity	10,984,331	7,845	40,400	10,951,776
Total investment securities	$ 178,186,339	$ 3,823,030	$ 1,292,873	$ 180,716,496

The amortized cost and fair value of securities at March 31, 2015, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

(Unaudited)	March 31, 2015			
	Available for Sale		Held to Maturity	
Maturity Distributions	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Within one year	$ 340,785	$ 341,352	$ 750,000	$ 750,000
One to five years	27,714,374	28,004,102	1,288,000	1,288,000
Five to ten years	33,771,605	35,423,265		
After ten years	22,907,545	24,220,511		
	84,734,309	87,989,230	2,038,000	2,038,000
SBA Pools	2,746,659	2,812,603		
Other asset backed securities	1,997,185	1,992,164		
Mortgage-backed securities - GSE residential	81,911,316	82,610,179	8,001,346	8,057,187
	$ 171,389,469	$ 175,404,176	$ 10,039,346	$ 10,095,187

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Securities with a carrying value of $2,483,000 and $2,426,000 were pledged at March 31, 2015 and September 30, 2014 to secure repurchase agreements. Securities with a carrying value of $9,048,000 and $9,121,000 were pledged at March 31, 2015 and September 30, 2014 to secure certain deposits.

Proceeds from sales of securities available for sale during the six months ended March 31, 2015 and 2014 were approximately $5,764,000 and $1,688,000, respectively. Gross gains of approximately $312,000 and $103,000 were realized on investment transactions for the six months ended March 31, 2015 and 2014, respectively. Gross losses of $0 were realized on investment transactions for the six months ended March 31, 2015 and 2014, respectively.

Certain investments in debt securities are reported in the consolidated financial statements at an amount less than their historical cost. Total fair value of these investments at March 31, 2015 and September 30, 2014 was approximately $38,715,000 and $75,400,000, which is approximately 21% and 42% of the Company s available-for-sale and held-to-maturity investment portfolio. These declines primarily resulted from fluctuations in market interest rates after the purchase.

Based on evaluation of available evidence, including recent changes in market interest rates, credit rating information and information obtained from regulatory filings, management believes the declines in fair value for these securities are temporary.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in either net income or accumulated other comprehensive loss in the period the other-than-temporary impairment is identified.

The following table shows our 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 March 31, 2015:

	(Unaudited)					
	Less Than 12 Months		12 Months or More		Tot al	
Description of Securities	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Available for sale						
Federal agencies	$	$	$ 6,464,800	$ 35,200	$ 6,464,800	$ 35,200
State and municipal obligations			1,608,276	26,310	1,608,276	26,310
Other asset backed securities			1,992,164	5,021	1,992,164	5,021
Mortgage-backed securities - GS E residential	6,262,847	33,057	20,314,790	323,422	26,577,637	356,479
Total available for sale	6,262,847	33,057	30,380,030	389,953	36,642,877	423,010
Held to maturity						
Mortgage-backed securities - GS E residential			2,072,326	6,805	2,072,326	6,805
Total temporarily impaired securities	$ 6,262,847	$ 33,057	$ 32,452,356	$ 396,758	$ 38,715,203	$ 429,815

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The following table shows our investments gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at September 30, 2014:

	Less Than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available for sale						
Federal agencies	$ 7,101,020	$ 8,028	$ 9,806,750	$ 193,352	$ 16,907,770	$ 201,380
State and municipal obligations	2,592,716	8,212	6,305,786	178,057	8,898,502	186,269
SBA Pools	2,000,000	9,983			2,000,000	9,983
Other asset backed securities			2,018,800	6,424	2,018,800	6,424
Mortgage-backed securities - GSE residential	16,961,754	62,947	23,889,458	785,470	40,851,212	848,417
Total available for sale	28,655,490	89,170	42,020,794	1,163,303	70,676,284	1,252,473
Held to maturity						
Mortgage-backed securities - GSE residential	4,723,234	40,400			4,723,234	40,400
Total temporarily impaired securities	$ 33,378,724	$ 129,570	$ 42,020,794	$ 1,163,303	$ 75,399,518	$ 1,292,873

Federal Agencies, SBA Pools, Other Asset-Backed Securities, and Mortgage-Backed Securities - GSE Residential

The unrealized losses on the Company s investment in federal agencies, SBA pools, other asset- backed securities, and mortgage-backed securities were caused by changes in market interest rates. The Company expects to recover the amortized cost basis over the term of the securities. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company does not consider those investments to be other-than- temporarily impaired at March 31, 2015.

State and Municipal Obligations

The unrealized losses on the Company s investments in securities of state and municipal obligations were caused by interest rate changes. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost bases of the investments. Because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at March 31, 2015.

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Note 4: Loans and Allowance

	March 31, 2015 (Unaudited)	September 30, 2014
Residential real estate loans	$ 140,858,304	$ 142,280,336
Commercial real estate loans	46,212,114	42,375,040
Commercial loans	22,515,128	26,694,117
Home equity/improvement loans	17,589,980	17,159,538
Consumer loans	3,229,155	3,110,628
	230,404,681	231,619,659
Less :		
Undisbursed portion of loans	170,722	254,186
Deferred loan fees and dis counts	474,924	485,075
Allowance for loan losses	1,942,782	1,980,170
	2,588,428	2,719,431
Total loans	$ 227,816,253	$ 228,900,228

The risk characteristics of each loan portfolio segment are as follows:

Commercial loans are primarily 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 include a personal guarantee. 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 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 generally 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 more adversely affected by conditions in the real estate markets or in the general economy. The characteristics of properties securing the Company s commercial real estate portfolio are diverse, but with geographic locations almost entirely in the Company s market area. Management monitors and evaluates commercial real estate loans based on collateral, geography and risk grade criteria. In general, the Company avoids financing single purpose projects unless other underwriting factors are present to help mitigate risk. In addition, management tracks the level of owner-occupied commercial real estate versus nonowner-occupied loans.

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Residential real estate, home equity/improvement and consumer loans consist of two segments residential mortgage loans and personal loans. For residential mortgage loans that are secured by 1-4 family residences and are generally owner-occupied, the Company generally establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Home equity loans are typically secured by a subordinate interest in 1-4 family residences, and consumer personal loans are secured by consumer personal assets, such as automobiles or recreational vehicles. Some consumer personal loans are unsecured, such as small installment loans and certain lines of credit. Repayment of these loans is primarily dependent on the personal income of the borrowers, which can be impacted by economic conditions in their market areas, such as unemployment levels. Repayment can also be impacted by changes in property values on residential properties. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

Activity in the allowance for loan losses is as follows:

	Three Months Ended March 31, 2015 (Unaudited)					
	Residential Real Estate	Commercial Real Estate	Commercial	Home Equity/ Improvement	Consumer	Total
Beginning Balance	$ 1,340,050	$ 281,655	$ 164,734	$ 136,730	$ 31,197	$ 1,954,366
Provision (credit)	(331)	26,937	(2,479)	5,632	4,741	34,500
Loans charged-off	(39,956)				(10,431)	(50,387)
Recoveries	1,289				3,014	4,303
Ending Balance	$ 1,301,052	$ 308,592	$ 162,255	$ 142,362	$ 28,521	$ 1,942,782

	Six Months Ended March 31, 2015 (Unaudited)					
	Residential Real Estate	Commercial Real Estate	Commercial	Home Equity/ Improvement	Consumer	Total
Beginning Balance	$ 1,405,602	$ 258,325	$ 159,578	$ 128,481	$ 28,184	$ 1,980,170
Provision (credit)	(35,912)	71,267	2,677	27,881	3,337	69,250
Loans charged-off	(70,638)	(21,000)		(14,000)	(5,000)	(110,638)
Recoveries	2,000				2,000	4,000
Ending Balance	$ 1,301,052	$ 308,592	$ 162,255	$ 142,362	$ 28,521	$ 1,942,782

	Three Months Ended March 31, 2014 (Unaudited)					
	Residential Real Estate	Commercial Real Estate	Commercial	Home Equity/ Improvement	Consumer	Total
Beginning Balance	$ 1,587,063	$ 299,797	$ 136,759	$ 178,878	$ 29,674	$ 2,232,171
Provision (credit)	162,091	(59,610)	21,958	7,706	855	133,000
Loans charged-off	(339,981)			(61,052)	(6,338)	(407,371)

Recoveries					3,500	3,500
Ending Balance	$ 1,409,173	$ 240,187	$ 158,717	$ 125,532	$ 27,691	$ 1,961,300

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	Six Months Ended March 31, 2014 (Unaudited)					
	Residential Real Estate	Commercial Real Estate	Commercial	Home Equity/ Improvement	Consumer	Total
Beginning Balance	$ 1,525,995	$ 361,419	$ 188,637	$ 196,247	$ 30,526	$ 2,302,824
Provision (credit)	332,709	(121,232)	(29,920)	(9,663)	5,606	177,500
Loans charged-off	(449,531)			(61,052)	(14,517)	(525,100)
Recoveries					6,076	6,076
Ending Balance	$ 1,409,173	$ 240,187	$ 158,717	$ 125,532	$ 27,691	$ 1,961,300

The following tables present the balance in the allowance for loan losses and the recorded investment in loans based on the portfolio segment and impairment method as of March 31, 2015 and September 30, 2014:

	March 31, 2015 (Unaudited)					
	Residential Real Estate	Commercial Real Estate	Commercial	Home Equity/ Improvement	Consumer	Total
Allowance Balances:						
Individually evaluated for impairment	$	$	$	$	$	$
Collectively evaluated for impairment	1,301,052	308,592	162,255	142,362	28,521	1,942,782
Total allowance for loan losses	$ 1,301,052	$ 308,592	$ 162,255	$ 142,362	$ 28,521	$ 1,942,782
Loan Balances:						
Individually evaluated for impairment	$ 2,426,969	$ 631,153	$ 788,949	$ 185,852	$ 8,419	$ 4,041,342
Collectively evaluated for impairment	138,431,335	45,580,961	21,726,179	17,404,128	3,220,736	226,363,339
Total loan balances	$ 140,858,304	$ 46,212,114	$ 22,515,128	$ 17,589,980	$ 3,229,155	$ 230,404,681

	September 30, 2014					
	Residential Real Estate	Commercial Real Estate	Commercial	Home Equity/ Improvement	Consumer	Total
Allowance Balances:						

Individually evaluated for impairment	$	$	$	$	$	$
Collectively evaluated for impairment	1,405,602	258,325	159,578	128,481	28,184	1,980,170
Total allowance for loan losses	$ 1,405,602	$ 258,325	$ 159,578	$ 128,481	$ 28,184	$ 1,980,170
Loan Balances:						
Individually evaluated for impairment	$ 2,426,969	$ 631,153	$ 788,949	$ 185,852	$ 8,419	$ 4,041,342
Collectively evaluated for impairment	139,853,367	41,743,887	25,905,168	16,973,686	3,102,209	227,578,317
Total loan balances	$ 142,280,336	$ 42,375,040	$ 26,694,117	$ 17,159,538	$ 3,110,628	$ 231,619,659

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Management s general practice is to proactively charge down loans individually evaluated for impairment to the fair value of the underlying collateral.

Consistent with regulatory guidance, charge-offs on all loan segments are taken when specific loans, or portions thereof, are considered uncollectible. The Company s policy is to promptly charge these loans off in the period the uncollectible loss is reasonably determined.

For all loan portfolio segments except 1-4 family residential properties and consumer, the Company promptly charges off loans, or portions thereof, when available information confirms that specific loans are uncollectible based on information that includes, but is not limited to, (1) the deteriorating financial condition of the borrower, (2) declining collateral values, and/or (3) legal action, including bankruptcy, that impairs the borrower s ability to adequately meet its obligations. For impaired loans that are considered to be solely collateral dependent, a partial charge-off is recorded when a loss has been confirmed by an updated appraisal or other appropriate valuation of the collateral.

The Company charges off 1-4 family residential and consumer loans, or portions thereof, when the Company reasonably determines the amount of the loss. The Company adheres to timeframes established by applicable regulatory guidance, which provides for the charge-down of 1-4 family first and junior lien mortgages to the net realizable value, less costs to sell when the loan is 180 days past due, charge-off of unsecured open-end loans when the loan is 180 days past due, and charge-down to the net realizable value when other secured loans are 120 days past due. Loans at these respective delinquency thresholds for which the Company can clearly document that the loan is both well-secured and in the process of collection, such that collection will occur regardless of delinquency status, need not be charged off.

The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the prior three years. Management believes the historical loss experience methodology is appropriate in the current economic environment, as it captures loss rates that are comparable to the current period being analyzed.

The following tables present the credit risk profile of the Company s loan portfolio based on rating category and payment activity as of March 31, 2015 and September 30, 2014:

			March 31, 2015 (Unaudited)			
	Residential Real Estate	**Commercial Real Estate**	**Commercial**	**Home Equity/ Improvement**	**Consumer**	**Total**
Grade:						
Pass (1-4)	$ 138,916,110	$ 45,985,589	$ 21,782,946	$ 17,463,043	$ 3,228,934	$ 227,376,622
Special Mention (5)	502,550	139,187	512,425	58,386		1,212,548
Substandard (6)	1,439,644	87,338	219,757	68,551	221	1,815,511
Doubtful (7)						
Loss (8)						
Total	$ 140,858,304	$ 46,212,114	$ 22,515,128	$ 17,589,980	$ 3,229,155	$ 230,404,681

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	September 30, 2014					
	Residential Real Estate	Commercial Real Estate	Commercial	Home Equity/ Improvement	Consumer	Total
Grade:						
Pass (1-4)	$ 140,422,184	$ 42,028,932	$ 25,905,167	$ 17,005,369	$ 3,102,209	$ 228,463,861
Special Mention (5)	398,798	242,304	671,666	61,757	7,824	1,382,349
Substandard (6)	1,459,354	103,804	117,284	92,412	595	1,773,449
Doubtful (7)						
Loss (8)						
Total	$ 142,280,336	$ 42,375,040	$ 26,694,117	$ 17,159,538	$ 3,110,628	$ 231,619,659

Internal Risk Categories

Loan grades are numbered 1 through 8. Grades 1 through 4 are considered satisfactory grades. The grade of 5, or Watch or Special Mention, represents loans of lower quality and is considered criticized. The grades of 6, or Substandard, and 7, or Doubtful, refer to assets that are classified. The use and application of these grades by the Company will be uniform and shall conform to the Company s policy.

Prime (1) Loans are of superior quality with excellent credit strength and repayment ability providing a nominal credit risk.

Good (2) Loans are of above average credit strength and repayment ability providing only a minimal credit risk.

Satisfactory (3) Loans of reasonable credit strength and repayment ability providing an average credit risk due to one or more underlying weaknesses.

Acceptable (4) Loans of the lowest acceptable credit strength and weakened repayment ability providing a cautionary credit risk due to one or more underlying weaknesses. New borrowers are typically not underwritten within this classification.

Special Mention (5) A special mention asset has potential weaknesses that deserve management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution s credit position at some future date. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification. Ordinarily, special mention credits have characteristics which corrective management action would remedy.

Substandard (6) Loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful (7) Loans classified as doubtful have all the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of current known facts, conditions and values, highly questionable and improbable.

Loss (8) Loans classified as loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off even though partial recovery may be affected in the future.

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The following tables present the Company s loan portfolio aging analysis as of March 31, 2015 and September 30, 2014:

	March 31, 2015 (Unaudited)						
	30-59 Past Due	60-89 Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Loans > 90 Days and Accruing
Residential real estate	$ 153,858	$	$ 375,317	$ 529,175	$ 140,329,129	$ 140,858,304	$
Commercial real estate					46,212,114	46,212,114	
Commercial	308,851			308,851	22,206,277	22,515,128	
Home equity/improvement	13,308	1,184	34,604	49,096	17,540,884	17,589,980	
Consumer		221		221	3,228,934	3,229,155	
Total loans	$ 476,017	$ 1,405	$ 409,921	$ 887,343	$ 229,517,338	$ 230,404,681	$

	September 30, 2014						
	30-59 Past Due	60-89 Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Loans > 90 Days and Accruing
Residential real estate	$ 484,469	$	$ 139,735	$ 624,204	$ 141,656,132	$ 142,280,336	$
Commercial real estate					42,375,040	42,375,040	
Commercial			5,979	5,979	26,688,138	26,694,117	
Home equity/improvement	64,910		49,682	114,592	17,044,946	17,159,538	
Consumer	3,080			3,080	3,107,548	3,110,628	
Total loans	$ 552,459	$	$ 195,396	$ 747,855	$ 230,871,804	$ 231,619,659	$

The entire balance of a loan is considered delinquent if the minimum payment contractually required to be made is not received by the specified due date.

The following table presents the Company s nonaccrual loans at:

	March 31, 2015 (Unaudited)	September 30, 2014
Residential real estate	$ 375,317	$ 139,735
Commercial		5,979
Home equity/improvement	34,604	49,682

Total nonaccrual loans	$ 409,921	$ 195,396

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The following tables present information regarding impaired loans as of:

	March 31, 2015 (Unaudited)		
	Recorded Balance	Unpaid Principal Balance	Specific Allowance
Impaired loans without a specific valuation allowance:			
Residential real estate	$ 2,467,842	$ 2,516,343	$
Commercial real estate	635,911	635,911	
Commercial	732,182	732,182	
Home equity/improvement	169,678	197,149	
Consumer	221	221	
Total impaired loans	$ 4,005,834	$ 4,081,806	$

	September 30, 2014		
	Recorded Balance	Unpaid Principal Balance	Specific Allowance
Impaired loans without a specific valuation allowance:			
Residential real estate	$ 2,426,969	$ 2,475,469	$
Commercial real estate	631,153	631,153	
Commercial	788,949	788,949	
Home equity/improvement	185,852	213,324	
Consumer	8,419	8,419	
Total impaired loans	$ 4,041,342	$ 4,117,314	$

	Three Months Ended March 31,				Six Months Ended March 31,			
	2015		2014		2015		2014	
	Average Investment in Impaired Loans	Interest Income Recognized	Average Investment in Impaired Loans	Interest Income Recognized	Average Investment in Impaired Loans	Interest Income Recognized	Average Investment in Impaired Loans	Interest Income Recognized
	(Unaudited)		(Unaudited)		(Unaudited)		(Unaudited)	
Impaired loans without a specific valuation allowance:								
Residential real estate	$ 2,422,387	$ 29,579	$ 2,594,338	$ 36,086	$ 2,423,914	$ 59,157	$ 2,707,280	$ 72,172
	622,930	9,290	730,044	10,538	625,671	18,580	790,601	21,075

Commercial real estate								
Commercial	746,023	10,432	45,701	9,072	760,332	20,865	45,550	18,143
Home equity/improvement	175,295	3,117	191,889	2,126	178,814	6,234	188,341	4,253
Consumer	111		884	11	74		1,205	23
Total impaired loans	$ 3,966,746	$ 52,418	$ 3,562,856	$ 57,833	$ 3,988,805	$ 104,836	$ 3,732,977	$ 115,666

Interest income on loans individually classified as impaired is recognized on a cash basis after all past due and current principal payments have been made.

Subsequent payments on nonaccrual loans are recorded as a reduction of principal, and interest income is recorded only after principal recovery is reasonably assured. Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no

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longer any reasonable doubt as to the timely collection of interest or principal. The Company requires a period of satisfactory performance of not less than six months before returning a nonaccrual loan to accrual status.

There were no troubled debt restructurings for the three and six month periods ended March 31, 2015 and 2014.

There were no troubled debt restructurings modified in the past 12 months that subsequently defaulted for the three and six month periods ended March 31, 2015 and 2014.

Note 5: Fair Values of Financial Instruments

Fair value 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 measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets

Level 3 Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy.

Available-for-Sale Securities

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. Level 2 securities include U.S. Government agency securities, mortgage- backed securities and CMO s and obligations of state and municipals. Matrix pricing is a mathematical technique widely used in the banking industry to value investment securities without relying exclusively on quoted prices for specific investment securities but rather relying on the investment securities relationship to other benchmark quoted investment securities. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

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The following tables present the fair value measurements of assets recognized in the accompanying consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2015 and September 30, 2014:

	March 31, 2015 (Unaudited) Fair Value Measurements Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available for sale				
Federal agencies	$ 30,344,334	$	$ 30,344,334	$
State and municipal obligations	57,644,896		57,644,896	
SBA Pools	2,812,603		2,812,603	
Other asset-backed securities	1,992,164		1,992,164	
Mortgage-backed securities - GSE - residential	82,610,179		82,610,179	
	$ 175,404,176	$	$ 175,404,176	$

	September 30, 2014 Fair Value Measurements Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available for sale				
Federal agencies	$ 19,561,097	$	$ 19,561,097	$
State and municipal obligations	60,172,620		60,172,620	
SBA Pools	2,789,289		2,789,289	
Other asset-backed securities	2,018,800		2,018,800	
Mortgage-backed securities - GSE - residential	85,222,914		85,222,914	

$ 169,764,720	$	$ 169,764,720	$

There were no nonrecurring fair value measurements at March 31, 2015 and September 30, 2014.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

Cash and Cash Equivalents - The fair value of cash and cash equivalents approximates carrying value.

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Interest-Bearing Time Deposits - The fair value of interest-bearing time deposits approximates carrying value.

Loans and Loans Held for Sale - For both short-term loans and variable-rate loans that reprice frequently, and with no significant change in credit risk, fair values are based on carrying values. The fair value for other loans is estimated using discounted cash flow analyses using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality.

Interest Receivable/Payable - The fair values of interest receivable/payable approximate carrying values.

FHLB Stock - Fair value of FHLB stock is based on the price at which it may be resold to the

FHLB.

Deposits - The fair values of noninterest-bearing, interest-bearing demand and savings accounts are equal to the amount payable on demand at the balance sheet date. The carrying amounts for variable-rate, fixed-term certificates of deposit approximate their fair values at the balance sheet date. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on such time deposits.

Short-Term Borrowings - The fair value of short-term borrowings approximates carrying value.

Federal Home Loan Bank Advances - The fair value of these borrowings is estimated using a discounted cash flow calculation, based on current rates for similar advances.

The following table presents estimated fair values of the Company s financial instruments and their related carrying value at March 31, 2015 and September 30, 2014.

	March 31, 2015		**September 30, 2014**	
	Carrying Amount	**Fair Value**	**Carrying Amount**	**Fair Value**
Assets				
Cash and cash equivalents	$ 22,218,408	$ 22,218,408	$ 17,658,180	$ 17,658,180
Interest-bearing time deposits	10,065,000	10,065,000	12,766,000	12,766,000
Investment securities held to maturity	10,039,346	10,095,187	10,984,331	10,951,776
Loans, including loans held for sale	228,031,503	228,247,503	229,144,878	229,144,878
FHLB stock	3,506,500	3,506,500	4,127,700	4,127,700
Interest receivable	2,068,232	2,068,232	2,510,239	2,510,239
Liabilities				
Deposits	358,291,891	359,421,891	353,920,254	354,807,545
Short-term borrowings	185,679	185,679	650,379	650,379
Federal Home Loan Bank advances	51,497,385	52,784,000	52,217,143	52,795,143
Interest payable	75,253	75,253	74,094	74,094

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Appendix A

AGREEMENT AND PLAN OF MERGER

This Agreement and Plan of Merger (this **Agreement**) is dated to be effective as of the 18th day of February, 2015, by and between Horizon Bancorp, an Indiana corporation (**Horizon**), and Peoples Bancorp, an Indiana corporation (**Peoples**).

Witnesseth:

WHEREAS, Horizon is an Indiana corporation registered as a bank holding company under the federal Bank Holding Company Act of 1956, as amended (the **BHC Act**), with its principal office located in Michigan City, Indiana; and

WHEREAS, Peoples is an Indiana corporation registered as a savings and loan holding company under the Home Owners Loan Act of 1933, as amended (the **HOLA**), with its principal office located in Auburn, Indiana; and

WHEREAS, Horizon and Peoples seek to affiliate through a corporate reorganization whereby Peoples will merge with and into Horizon, and thereafter or simultaneously therewith, Peoples Federal Savings Bank of DeKalb County, a federally chartered stock savings bank and wholly-owned subsidiary of Peoples (**Peoples Bank**), will be merged with and into Horizon Bank, National Association, a national banking association and wholly-owned subsidiary of Horizon (**Horizon Bank**); and

WHEREAS, the Boards of Directors of each of the parties hereto have determined that it is in the best interests of their respective corporations and their respective shareholders to consummate the merger provided for herein and have approved this Agreement, authorized its execution and designated this Agreement a plan of reorganization and a plan of merger; and

NOW, THEREFORE, in consideration of the foregoing premises, the representations, warranties, covenants and agreements herein contained and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties hereby make this Agreement and prescribe the terms and conditions of the merger of Peoples with and into Horizon, and the mode of carrying such merger into effect as follows:

ARTICLE I.

THE MERGER

1.01 **The Merger**.

(a) **General Description**. Upon the terms and subject to the conditions of this Agreement, at the Effective Time (as defined in Article IX hereof), Peoples shall merge with and into and under the Articles of Incorporation of Horizon (the **Merger**). Horizon shall survive the Merger (sometimes hereinafter referred to as the **Surviving Corporation**) and shall continue its corporate existence under the laws of the State of Indiana pursuant to the provisions of and with the effect provided in the Indiana Business Corporation Law (the **IBCL**), as amended.

(b) **Name, Officers and Directors**. The name of the Surviving Corporation shall be Horizon Bancorp. Its principal office shall be located at 515 Franklin Street, Michigan City, Indiana 46360. The officers of Horizon serving at the Effective Time shall continue to serve as the officers of the Surviving Corporation, until such time as their successors shall have been duly elected and have qualified or until their earlier resignation, death or removal from office. The directors of the Surviving Corporation following the Effective Time shall be those individuals serving as directors of Horizon at the Effective Time, until such time as their successors have been duly elected and have qualified or until their earlier resignation, death, or removal as a director, subject to Section 6.09 hereof.

(c) **Articles of Incorporation and Bylaws**. The Articles of Incorporation and Bylaws of Horizon in existence at the Effective Time shall remain the Articles of Incorporation and Bylaws of the Surviving Corporation following the Effective Time, until such Articles of Incorporation and Bylaws shall be further amended as provided by applicable law.

(d) **Effect of the Merger**. At the Effective Time, the title to all assets, real estate and other property owned by Peoples shall vest in Surviving Corporation as set forth in Indiana Code Section 23-1-40-6, as amended, without reversion or impairment. At the Effective Time, all liabilities of Peoples shall become liabilities of the Surviving Corporation as set forth in Indiana Code Section 23-1-40-6, as amended.

(e) **Integration**. At the Effective Time and subject to the terms and conditions of this Agreement, the parties hereto currently intend to effectuate, or cause to be effectuated, the Merger, pursuant to a Plan of Merger, substantially in the form attached hereto as Exhibit 1.01(e). The parties agree to cooperate and to take all reasonable actions prior to or following the Effective Time, including executing all requisite documentation, as may be reasonably necessary to effect the Merger in accordance with the terms and conditions hereof.

1.02 **Reservation of Right to Revise Structure**. At Horizon s election, the Merger may alternatively be structured so that (a) Peoples is merged with and into any other direct or indirect wholly-owned subsidiary of Horizon or (b) any direct or indirect wholly-owned subsidiary of Horizon is merged with and into Peoples; *provided, however*, that no such change shall (1) alter or change the amount or kind of the Merger Consideration (as hereinafter defined) or the treatment of the holders of common stock, $1.00 par value per share, of Peoples (the **Peoples Common Stock**), (2) prevent the parties from obtaining the opinions of counsel referred to in Sections 7.01(h) and 7.02(h) or otherwise cause the transaction to fail to qualify for the tax treatment described in Section 1.03, or (3) materially impede or delay consummation of the transactions contemplated by this Agreement. In the event of such an election, the parties agree to execute an appropriate amendment to this Agreement (to the extent such amendment only changes the method of effecting the business combination and does not substantively affect this Agreement or the rights and obligations of the parties or their respective shareholders) in order to reflect such election.

1.03 **Tax Free Reorganization**. Horizon and Peoples intend for the Merger to qualify as a reorganization within the meaning of Section 368(a) and related sections of the Internal Revenue Code of 1986, as amended (the **Code**), and that this Agreement shall constitute a plan of reorganization for purposes of Sections 354 and 361 of the Code, and agree to cooperate and to take such actions as may be reasonably necessary to assure such result.

1.04 **Absence of Control**. Subject to any specific provisions of the Agreement, it is the intent of the parties to this Agreement that neither Horizon nor Peoples by reason of this Agreement shall be deemed (until consummation of the transactions contemplated here) to control, directly or indirectly, the other party or any of its respective Subsidiaries (as such term is defined below) and shall not exercise or be deemed to exercise, directly or indirectly, a controlling influence over the management or policies of such other party or any of its respective Subsidiaries.

1.04 **Bank Merger**. The parties will cooperate and use reasonable best efforts to effect the merger of Peoples Bank with and into Horizon Bank (the **Bank Merger**) at the Effective Time of the Merger. At the effective time of the Bank Merger, the separate corporate existence of Peoples Bank will terminate. Horizon Bank will be the surviving bank and will continue its corporate existence under applicable law. The Articles of Association of Horizon Bank, as then in effect, will be the Articles of Association of the surviving bank, the Bylaws of Horizon Bank, as then in effect, will be the Bylaws of the surviving bank, and the Board of Directors and officers of Horizon Bank will continue as the Board of Directors and officers of the surviving bank, subject to Section 6.09 hereof.

1.06 **Dissenters Rights**. Notwithstanding anything to the contrary contained in this Agreement, to the extent appraisal rights are available to holders of Peoples Common Stock pursuant to the provisions of any applicable Law (as hereinafter defined in Section 3.05(a), including Chapter 44 of the IBCL, any shares of Peoples Common Stock held by a Person (as hereinafter defined in Section 2.04(f) who objects to the Merger, whose shares were not voted in favor of the Merger and who complies with and satisfies all of the provisions of the applicable Law concerning the rights of such Person to dissent from the Merger and to require appraisal of such Person s shares and who has not withdrawn such objection or waived such rights prior to the Effective Time (collectively with respect to all such Peoples shareholders, the **Dissenting Shares**), shall not be converted pursuant to Section 2.01, but shall become the right to receive such consideration as may be determined to be due the holder of such Dissenting Shares pursuant to applicable Law; *provided, however*, that each Dissenting Share held by a Person at the Effective Time who shall, after the Effective Time, withdraw the demand for appraisal or lose the right of appraisal, in either case pursuant to applicable Law, shall be deemed to have been converted, as of the Effective Time, into the right to receive the consideration as is determined in accordance with Article II.

ARTICLE II.

MANNER AND BASIS OF EXCHANGE OF STOCK

2.01 **Merger Consideration**. Subject to the terms and conditions of this Agreement, at the Effective Time, each share of Peoples Common Stock issued and outstanding immediately prior to the Effective Time (other than Dissenting Shares, shares held as treasury stock of Peoples and shares held directly or indirectly by Horizon, except shares held in a fiduciary capacity or in satisfaction of a debt previously contracted, if any) shall become and be converted into the right to receive in accordance with this Article (collectively, the **Merger Consideration**): (i) 0.95 shares of Horizon common stock (the **Exchange Ratio**) (as adjusted in accordance with the terms of this Agreement), without par value (the Horizon Common Stock), and (ii) $9.75 in cash (the aggregate cash consideration to be paid in the Merger is referred to herein as the **Cash Consideration**); *provided, however*, the Peoples stockholders owning less than 100 shares of Peoples Common Stock as of the Effective Time will only be entitled to receive $33.14 per share in cash and will not be entitled to receive any Horizon Common Stock.

2.02 **Anti-Dilution Adjustments**. If Horizon changes (or establishes a record date for changing) the number of shares of Horizon Common Stock issued and outstanding prior to the Effective Time by way of a stock split, stock dividend, or similar transaction with respect to the outstanding Horizon Common Stock, and the record date therefor shall be prior to the Effective Time, the Exchange Ratio shall be adjusted so the shareholders of Peoples at the Effective Time shall receive, in the aggregate, such number of shares of Horizon Common Stock representing the same percentage of the outstanding shares of Horizon Common Stock as would have been represented by the number of shares of Horizon Common Stock the shareholders of Peoples would have received if any of the foregoing actions had not occurred. No adjustment shall be made under this Section 2.02 solely as a result of Horizon changing its cash dividend levels or issuing additional shares of Horizon Common Stock provided it receives value for such shares or such shares are issued in connection with a Horizon employee benefit plan or similar plan.

2.03 **Fractional Shares**. Notwithstanding any other provision in this Agreement, no fractional shares of Horizon Common Stock and no certificates or scrip therefor, or other evidence of ownership thereof, will be issued in the Merger; instead, Horizon shall pay to each holder of Peoples Common Stock who otherwise would be entitled to a fractional share of Horizon Common Stock an amount in cash (without interest) determined by multiplying such fraction by the average of the daily closing sales prices of a share of Horizon s common stock, rounded to the nearest cent, during the fifteen (15) consecutive trading days immediately preceding the second business day prior to the Closing Date; *provided, however*, that closing sales prices shall only be used for days during which such shares are actually traded on the NASDAQ Global Market.

2.04 **Exchange Procedures**.

(a) At and after the Effective Time, each certificate representing outstanding shares of Peoples Common Stock (other than Dissenting Shares) shall represent only the right to receive the Merger Consideration in accordance with the terms of this Agreement.

(b) At or prior to the Effective Time, Horizon shall reserve a sufficient number of shares of Horizon Common Stock to be issued as part of the Merger Consideration. As promptly as practicable after the Effective Time, but in no event more than five (5) business days thereafter, Horizon shall mail to each holder of Peoples Common Stock a letter of transmittal providing instructions as to the transmittal to Horizon of certificates representing shares of

Peoples Common Stock and the issuance of shares of Horizon Common Stock in exchange therefor pursuant to the terms of this Agreement.

(c) Horizon shall cause a certificate representing that number of whole shares of Horizon Common Stock that each holder of Peoples Common Stock has the right to receive pursuant to Section 2.01 and a check in the amount of such holder s proportionate share of the Cash Consideration and any cash in lieu of fractional shares or dividends or distributions which such holder shall be entitled to receive, if any, to be delivered to such shareholder upon delivery to Horizon of certificates representing such shares of Peoples Common Stock (**Old Certificates**) (or bond or other indemnity satisfactory to Horizon if any of such certificates are lost, stolen or destroyed) owned by such shareholder accompanied by a properly completed and executed letter of transmittal, in the form and substance satisfactory to Horizon. No interest will be paid on any Merger Consideration that any such holder shall be entitled to receive pursuant to this Article II upon such delivery.

(d) No dividends or other distributions on Horizon Common Stock with a record date occurring after the Effective Time shall be paid to the holder of any unsurrendered Old Certificate representing shares of Peoples Common Stock converted in the Merger into the right to receive shares of Horizon Common Stock until the holder thereof surrenders such Old Certificates in accordance with this Section 2.04. After becoming so entitled in accordance with this Section 2.04, the record holder thereof also shall be entitled to receive any such dividends or other distributions, without any interest thereon, which theretofore had become payable with respect to shares of Horizon Common Stock such holder had the right to receive upon surrender of the Old Certificate.

(e) The stock transfer books of Peoples shall be closed immediately upon the Effective Time and from and after the Effective Time there shall be no transfers on the stock transfer records of Peoples of any shares of Peoples Common Stock. If, after the Effective Time, Old Certificates are presented to Horizon, they shall be canceled and exchanged for the Merger Consideration deliverable in respect thereof pursuant to this Agreement in accordance with the procedures set forth in this Section 2.04.

(f) Horizon shall be entitled to rely upon Peoples stock transfer books to establish the identity of those individuals, partnerships, corporations, trusts, joint ventures, organizations or other entities (each, a **Person**) entitled to receive the Merger Consideration, which books shall be conclusive with respect thereto. In the event of a dispute with respect to ownership of stock represented by any Old Certificate, Horizon shall be entitled to deposit any Merger Consideration represented thereby in escrow with an independent third party selected by Horizon and thereafter be relieved from any and all liability with respect to any claims thereto.

(g) If any Old Certificate shall have been lost, stolen, or destroyed, upon the making of an affidavit of that fact by the Person claiming such Old Certificate to be lost, stolen, or destroyed and, if required by Horizon, the posting by such Person of a bond or other indemnity satisfactory to Horizon as indemnity against any claim that may be made against it with respect to such Old Certificate, Horizon will issue in exchange for such affidavit of lost, stolen, or destroyed Old Certificate, the Merger Consideration deliverable in respect thereof pursuant to Section 2.01 hereof.

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(h) Notwithstanding anything in this Agreement to the contrary, at the Effective Time, all shares of Peoples Common Stock that are held as treasury stock of Peoples or owned by Horizon (other than shares held in a fiduciary capacity or in satisfaction of a debt previously contracted) shall be cancelled and shall cease to exist, and no stock of Horizon or other consideration shall be exchanged therefor.

(i) Notwithstanding the foregoing, no party hereto shall be liable to any former holder of Peoples Common Stock for any amount properly delivered to a public official pursuant to applicable abandoned property, escheat or similar laws.

ARTICLE III.

REPRESENTATIONS AND WARRANTIES OF PEOPLES

On or prior to the date hereof, Peoples has delivered to Horizon a schedule (the **Peoples Disclosure Schedule**) setting forth, among other things, items th