Northumberland Bancorp

Consolidated Financial Statements

December 31, 2017 and 2016

Northumberland Bancorp

Contents

Northumberland Bancorp

245 Front Street • P.O. Box 271 • Northumberland, PA 17857
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March 22, 2018

To our Stockholders:

The year 2017 was exciting in that we spent much of the year developing a strategic plan focused on growing our Company. This growth is designed to first enhance profitability and second allow the Company to cover the costs of enhancements to the Bank's management structure, costs of regulatory requirements and ongoing information technology needs. Behind this growth is a belief that there has not been a better time in recent memory for us to take advantage of a healthy, growing economy along with the recent reduction in the number of banks serving the Central Susquehanna Valley.

Net income declined to $1,970,000 in 2017 from $2,866,000. Of the decline of $896,000, $569,000 was due to the write-down of net deferred tax assets. The tax legislation passed by Congress in late December 2017 reduced the statutory tax rate from 34% to 21% required this one-time non-cash accounting adjustment. The remainder of the decrease was a result of the staff additions needed to support our growth, as well as, staff to support the increased regulatory compliance needs.

Net interest income grew $621,000. The Bank's tax equivalent net interest margin remained steady at 3.11%. Non-interest income declined $122,000 primarily due to the impact of security gains in 2016 moving to a security loss in 2017. Non-interest expense increased $812,000, primarily due to the increased salaries and benefits noted previously, as well as, continued expenses associated with the Consent Order disclosed in Note 2 to the following Consolidated Financial Statements.

From a balance sheet perspective, total loans increased $21,315,000 from December 31, 2016 or 7.1%. This increase was primarily due to the growth in commercial loans. Deposits increased to $453,376,000 or 2.4% from 2016. Credit quality remained strong.

The Company and the Bank continue to be well capitalized. Tier One Capital of the Bank was 10.31%, compared to 10.33% in 2016. Common Equity Tier One Capital, Tier One Risk Based Capital and Total Risked based capital were 18.31%, 18.31% and 19.34%, compared to the same ratios in 2016 of 18.57%, 18.57% and 19.59%, respectively. The decline reflects the growth of the Bank coupled with the growth in the commercial and residential real estate loan portfolio. Past due loans increased to $3,756,000 or 1.17% of total loans in 2017, compared to $3,222,000 or 1.07% of total loans in 2016, and remains at a very low level.

Organizationally, the Bank has completed the planned enhanced management structure. Robert Crane joined the Bank in August 2017, as SVP & Chief Financial Officer. He joins J. Todd Troxell, EVP & Chief Operating Officer, Mark Ritter, EVP of Wealth Management and Lisa Hassinger, SVP of Compliance and Risk Management. This structure adds to the Bank's depth of management to address the needs of the Bank going forward.

The Company continues to enhance its electronic services deliveries. In 2017, we implemented a new internet banking product, as well as, SecureLock Equip to provide additional security for our debit card holders. In 2018, we have signed agreements to provide Remote Deposit Capture for our commercial banking customers, as well as, Zelle (a person to person) payment solution.

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In 2017, the Company welcomed two new directors to the board, Chad Geise and Adam Purdy. They come from families that have deep roots in the Central Susquehanna Valley and offer additional skill sets to the Board of Directors.

We thank you, our valued stockholders, directors, officers and employees for your dedication, support and contributions to the Company's growth and success during the year.

J. Donald Steele, Jr.
Chairman and President

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Independent Auditor’s Report

Board of Directors and Stockholders
Northumberland Bancorp
Northumberland, Pennsylvania

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Northumberland Bancorp and subsidiary, which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Northumberland Bancorp and subsidiary as of December 31, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter Regarding Consent Order

As discussed in Note 2, The Northumberland National Bank, the wholly-owned subsidiary of Northumberland Bancorp, has entered into a Stipulation and Consent to Issuance of a Consent Order with the Comptroller of the Currency of the United States of America and Northumberland Bancorp adopted a resolution at the request of the Federal Reserve Bank of Philadelphia ("FRB"). Our opinion is not modified with respect to this matter.

BDO USA, LLP

Harrisburg, Pennsylvania
March 22, 2018

Consolidated Financial Statements

Northumberland Bancorp

Consolidated Balance Sheets

(amounts in thousands except share and per share data)

December 31,		**2017**		2016
Assets				
Cash and due from banks	**$**	**5,619**	$	6,604
Interest-bearing deposits in other banks		**7,928**		7,644
Total cash and cash equivalents		**13,547**		14,248
Investment securities available-for-sale		**145,125**		149,666
Investment securities held-to-maturity (fair value of $648 and $1,686)		**650**		1,692
Total investment securities		**145,775**		151,358
Restricted stock, at cost		**3,806**		3,505
Loans held for sale		**1,353**		1,493
Loans		**321,516**		300,201
Less allowance for loan losses		**2,910**		2,778
Net loans		**318,606**		297,423
Premises and equipment		**9,361**		9,780
Bank-owned life insurance		**11,237**		9,525
Accrued interest and other assets		**4,204**		4,826
Total Assets	**$**	**507,889**	$	492,158
Liabilities and Stockholders' Equity				
Liabilities				
Deposits:				
Noninterest-bearing demand	**$**	**78,221**	$	73,621
Interest-bearing demand		**164,393**		169,555
Savings		**82,661**		81,318
Time deposits		**128,101**		118,136
Total deposits		**453,376**		442,630
Short-term borrowings		**3,000**		-
Accrued interest and other liabilities		**2,645**		1,677
Total Liabilities		**459,021**		444,307
Stockholders' Equity				
Common stock, par value $0.10; 5,000,000 shares authorized, 1,502,500 shares issued and 1,328,358 shares outstanding		**150**		150
Capital surplus		**3,832**		3,832
Retained earnings		**50,304**		48,778
Accumulated other comprehensive loss		**(3,118)**		(2,603)
		51,168		50,157
Treasury stock, at cost (174,142 shares)		**(2,248)**		(2,248)
Total Northumberland Bancorp stockholders' equity		**48,920**		47,909
Noncontrolling interest		**(52)**		(58)
Total Stockholders' Equity		**48,868**		47,851
Total Liabilities and Stockholders' Equity	**$**	**507,889**	$	492,158

See accompanying notes to consolidated financial statements.

Northumberland Bancorp

Consolidated Statements of Income

(amounts in thousands except share and per share data)

Years Ended December 31,		**2017**		2016
Interest and Dividend Income				
Interest and fees on loans:				
Taxable	**$**	**13,601**	$	12,844
Tax-exempt		**264**		259
Interest on interest-bearing deposits in other banks		**103**		47
Interest and dividends on investment securities:				
Taxable		**1,736**		1,247
Tax-exempt		**991**		1,247
Dividends		**176**		176
Total Interest and Dividend Income		**16,871**		15,820
Interest Expense				
Deposits		**2,832**		2,409
Short-term borrowings		**7**		-
Total Interest Expense		**2,839**		2,409
Net interest income		**14,032**		13,411
Provision for Loan Losses		**227**		208
Net Interest Income After Provision for Loan Losses		**13,805**		13,203
Noninterest Income				
Service charges on deposit accounts		**1,125**		1,044
Trust services income		**674**		611
Investment securities (losses) gains, net		**(31)**		163
Gain on sale of loans		**633**		797
Earnings on bank-owned life insurance		**268**		266
Other income		**810**		720
Total Noninterest Income		**3,479**		3,601
Noninterest Expense				
Salaries and employee benefits		**7,331**		6,738
Occupancy expense, net		**790**		757
Equipment expense		**937**		868
Professional fees		**1,058**		1,254
Data processing		**913**		845
Shares tax		**435**		377
Federal deposit insurance expense		**289**		376
Reimbursements to customers		**227**		36
Other expense		**2,165**		2,082
Total Noninterest Expense		**14,145**		13,333
Income before income taxes		**3,139**		3,471
Income Taxes		**1,163**		591
Net Income		**1,976**		2,880
Net income attributable to noncontrolling interest		**6**		14
Net Income Attributable to Northumberland Bancorp	**$**	**1,970**	$	2,866
Earnings Per Share	**$**	**1.48**	$	2.16
Weighted-Average Shares Outstanding		**1,328,358**		1,328,358

See accompanying notes to consolidated financial statements.

Northumberland Bancorp

Consolidated Statements of Comprehensive Income

(amounts in thousands)

Years Ended December 31,		**2017**		2016
Net Income	**$**	**1,976**	$	2,880
Other Comprehensive Loss				
Change in unrealized holding (gains) losses on investment securities available-for-sale		**176**		(1,678)
Tax effect		**(60)**		573
Reclassification adjustment for investment securities (gains) losses recognized in net income		**31**		(163)
Tax effect		**(10)**		55
Change in unrecognized pension costs		**(211)**		(147)
Tax effect		**72**		50
Other Comprehensive Loss, Net of Tax		**(2)**		(1,310)
Comprehensive income before noncontrolling interest		**1,974**		1,570
Less: net income attributable to noncontrolling interest		**6**		14
Comprehensive Income	**$**	**1,968**	$	1,556

See accompanying notes to consolidated financial statements.

Northumberland Bancorp

Consolidated Statements of Stockholders' Equity

(amounts in thousands except per share data)

	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Noncontrolling Interest	Total
Balance, December 31, 2015	$ 150	$ 3,832	$ 46,815	$ (1,293)	$ (2,248)	$ (72)	$ 47,184
Net income	-	-	2,866	-	-	14	2,880
Other comprehensive loss	-	-	-	(1,310)	-	-	(1,310)
Dividends declared ($0.68 per share)	-	-	(903)	-	-	-	(903)
Balance, December 31, 2016	150	3,832	48,778	(2,603)	(2,248)	(58)	47,851
Net income	-	-	1,970	-	-	6	1,976
Other comprehensive loss	-	-	-	(2)	-	-	(2)
Reclassification of Certain Tax Effects	-	-	513	(513)	-	-	-
Dividends declared ($0.72 per share)	-	-	(957)	-	-	-	(957)
Balance, December 31, 2017	**$ 150**	**$ 3,832**	**$ 50,304**	**$ (3,118)**	**$ (2,248)**	**$ (52)**	**$ 48,868**

See accompanying notes to consolidated financial statements.

Northumberland Bancorp

Consolidated Statements of Cash Flows
(amounts in thousands)

Years Ended December 31,		**2017**		2016
Cash Flows from Operating Activities				
Net income	**$**	**1,976**	$	2,880
Adjustments to reconcile net income to net cash provided by operating activities:				
Provision for loan losses		**227**		208
Depreciation, amortization, and accretion, net		**1,714**		1,631
Proceeds from sale of loans held for sale		**22,194**		26,103
Gain on sale of loans		**(633)**		(797)
Originations of residential loans held for sale		**(21,422)**		(25,506)
Investment securities gains (losses), net		**31**		(163)
Deferred income tax expense		**276**		217
Earnings on bank-owned life insurance		**(268)**		(266)
Write-down of other real estate owned		**-**		14
Increase in accrued interest receivable		**(185)**		(22)
Decrease (increase) in accrued interest payable		**13**		(2)
Other, net		**1,308**		(2,022)
Net Cash Provided by Operating Activities		**5,231**		2,275
Cash Flows from Investing Activities				
Investment securities available-for-sale:				
Proceeds from sales		**14,483**		29,294
Proceeds from maturities or redemptions		**20,807**		20,856
Purchases		**(31,617)**		(52,926)
Investment securities held-to-maturity:				
Proceeds from maturities or redemptions		**1,015**		1,446
Purchases		**-**		(4)
Increase in loans, net		**(21,460)**		(13,652)
Purchases of premises and equipment, net		**(204)**		(260)
Purchases of restricted stock		**(528)**		(470)
Redemptions of restricted stock		**227**		265
Purchase of bank-owned life insurance		**(1,444)**		-
Proceeds from sale of other real estate owned		**-**		335
Net Cash Used in Investing Activities		**(18,721)**		(15,116)
Cash Flows from Financing Activities				
Net increase in deposits		**10,746**		16,293
Net increase in short term borrowed funds		**3,000**		-
Cash dividends paid		**(957)**		(903)
Net Cash Provided by Financing Activities		**12,789**		15,390
(Decrease) increase in cash and cash equivalents		**(701)**		2,549
Cash and Cash Equivalents, Beginning Of Year		**14,248**		11,699
Cash and Cash Equivalents, End Of Year	**$**	**13,547**	$	14,248

1. Summary of Significant Accounting Policies

A summary of significant accounting and reporting policies applied in the presentation of the accompanying consolidated financial statements follows:

Nature of Operations and Basis of Presentation

Northumberland Bancorp (the "Company") is a Pennsylvania corporation and is registered under the Bank Holding Company Act. The Company was organized as the holding company of its wholly owned subsidiary, The Northumberland National Bank (the "Bank"). The Bank is a nationally chartered commercial bank located in Northumberland, Pennsylvania. The Bank's service area includes portions of Northumberland, Snyder, Union, and Montour counties in Pennsylvania. The Company and the Bank derive substantially all of their income from banking and bank-related services, which include interest earnings on commercial, commercial mortgage, residential real estate, and consumer loan financing as well as interest earnings on investment securities and deposit and trust services to their customers. The Bank has a subsidiary, NNB Financial Services, which sells financial and insurance products. The Company is supervised by the Federal Reserve Board, while the Bank is subject to regulation and supervision by the Office of the Comptroller of the Currency.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, the Bank. Intercompany activity has been eliminated in consolidation.

The consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles and with general practice within the banking industry. In preparing the financial statements, management is required to make certain estimates and assumptions that affect the reported amounts of assets and liabilities as of the consolidated balance sheet date and revenues and expenses for the period. Actual results could differ significantly from those estimates.

Investment Securities

Investment securities are classified at the time of purchase, based on management's intention and ability, as securities held-to-maturity or securities available-for-sale. Debt securities acquired with the intent and ability to hold to maturity are stated at cost adjusted for amortization of premium and accretion of discount that are computed using the level yield method and recognized as adjustments of interest income. Certain other debt securities have been classified as available-for-sale to serve principally as a source of liquidity. Unrealized holding gains and losses for available-for-sale securities are reported as a separate component of stockholders' equity, net of tax, until realized. Realized securities gains and losses are computed using the specific identification method. Interest and dividends on investment securities are recognized as income when earned.

Securities are periodically reviewed for other-than-temporary impairment based upon a number of factors including, but not limited to, the length of time and extent to which the market value has been less than cost, the financial condition of the underlying issuer, the ability of the issuer to meet contractual obligations, the likelihood of the security's ability to recover any decline in its market value, and whether or not the Company intends to sell the security or whether it's more likely than not that the Company would be required to sell the security before its anticipated recovery in market value. A decline in value that is considered to be other than temporary is recorded as a loss within noninterest income in the consolidated statements of income.

Federal Home Loan Bank Stock

The Bank is a member of the Federal Home Loan Bank ("FHLB") of Pittsburgh and, as such, is required to maintain a minimum investment in stock of the FHLB that varies with the level of advances outstanding with the FHLB, as well as a minimum level of mortgages in the Mortgage Partnership Finance (“MPF”) program. The stock is bought from and sold to the FHLB based upon its $100 par value. The stock does not have a readily determinable fair value and as such is classified as restricted stock, carried at cost.

Loans Held for Sale and Loans Serviced

Loans held for sale are carried at the lower of cost or fair value, as determined on an aggregate basis. Gains and losses on sales of loans held for sale are recognized on settlement dates and are determined by the difference between the sale proceeds and the carrying value of loans. All sales are made with limited recourse. Loans held for sale were $1,353,000 and $1,493,000 at December 31, 2017 and 2016, respectively. At December 31, 2017 and 2016, the amounts of loans serviced by the Company for the benefit of others were $128,121,000 and $123,739,000, respectively. These loans are not included in the Company’s consolidated balance sheet.

Mortgage Servicing Rights ("MSRs")

The Company has agreements for the express purpose of selling loans in the secondary market. The Company maintains servicing rights for certain loans. Originated MSRs are recorded by allocating total costs incurred between the loan and servicing rights based on their relative fair values. MSRs are amortized in proportion to the estimated servicing income over the estimated life of the servicing portfolio. Annually, the Company performs an impairment review of the MSRs and recognizes impairment through a valuation account. No impairment was recognized in 2017 or 2016. MSRs are a component of other assets on the consolidated balance sheets. The balance of loan servicing assets was $831,000 and $893,000 at December 31, 2017 and 2016, respectively.

Loans

Loans originated with the intention to hold to maturity are reported at their principal amount, net of unearned income and the allowance for loan losses. Interest income on all loans is recognized on an accrual basis. Nonrefundable loan fees and certain direct costs are deferred and amortized over the life of the loans using the interest method. The amortization is reflected as an interest yield adjustment, and the deferred portion of the net fees and costs is reflected as part of the loan balance. Accrual of interest is discontinued when, in the opinion of management, reasonable doubt exists as to the collectability of additional interest. Loans are returned to accrual status when past-due interest is collected and the collection of principal is probable.

Allowance for Loan Losses

The allowance for loan losses represents the amount that management estimates is adequate to provide for probable losses inherent in its loan portfolio. The allowance method is used in providing for loan losses. Accordingly, all loan losses are charged to the allowance, and all recoveries are credited to it. The allowance for loan losses is established through a provision for loan losses charged to operations. The provision for loan losses is based on management's periodic evaluation of individual loans, economic factors, past loan loss experience, changes in the composition and volume of the portfolio, and other relevant factors. The estimates used in determining the adequacy of the allowance for loan losses, including the amounts and timing of future cash flows expected on impaired loans, are particularly susceptible to changes in the near term.

Impaired loans are commercial and commercial real estate loans for which it is probable the Company will not be able to collect all amounts due according to the contractual terms of the loan agreement. The Company individually evaluates such loans for impairment and does not aggregate loans by major risk classifications. The definition of "impaired loans" is not the same as the definition of "nonaccrual loans," although the two categories overlap. The Company may choose to place a loan on nonaccrual status due to payment delinquency or uncertain collectability, while not classifying the loan as impaired if the loan is not a commercial or commercial real estate loan. Factors considered by management in determining impairment include payment status and collateral value. The amount of impairment for these types of impaired loans is determined by the difference between the present value of the expected cash flows related to the loan, using the original interest rate, and its recorded value, or as a practical expedient in the case of collateralized loans, the difference between the fair value of the collateral and the recorded amount of the loans. When foreclosure is probable, impairment is measured based on the fair value of the collateral.

Mortgage loans on one-to-four family properties and all consumer loans are large groups of smaller-balance homogeneous loans and are measured for impairment collectively. Loans that experience insignificant payment delays, which are defined as 90 days or less, generally are not classified as impaired. Management determines the significance of payment delays on a case-by-case basis taking into consideration all circumstances surrounding the loan and the borrower including the length of the delay, the borrower's prior payment record, and the amount of shortfall in relation to the principal and interest owed.

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

Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful lives of the assets, which range from 3 to 20 years for furniture, fixtures, and equipment and 15 to 50 years for buildings and leasehold improvements. Expenditures for maintenance and repairs are charged against income as incurred. Costs of major additions and improvements are capitalized.

Real Estate Owned

Real estate owned acquired in settlement of foreclosed loans is carried as a component of other assets at fair value minus estimated cost to sell. Prior to foreclosure, the estimated collectible value of the collateral is evaluated to determine whether a partial charge-off of the loan balance is necessary. After transfer to real estate owned, any subsequent write-downs are charged against other operating expenses. Direct costs incurred in the foreclosure process and subsequent holding costs incurred on such properties are recorded as expenses of current operations.

Bank Owned Life Insurance

The Company invests in bank owned life insurance ("BOLI") as a source of funding for employee benefit expenses. BOLI involves the purchasing of life insurance by the bank on a select group of employees. The Company is the owner and beneficiary of the policies. This life insurance investment is carried at the cash surrender value of the underlying policies. Income from the increase in cash surrender value of the policies or from death benefits realized is included in other income on the consolidated statements of income.

Advertising Costs

Advertising costs are expensed as the costs are incurred. Advertising expenses amounted to $122,000 and $121,000 for 2017 and 2016, respectively.

Income Taxes

The Company and the Bank file a consolidated federal income tax return. Deferred tax assets or liabilities are computed based on the difference between the financial statement and income tax basis of assets and liabilities using the enacted marginal tax rates. Deferred income tax expenses or benefits are based on the changes in the deferred tax asset or liability from period to period.

On December 22, 2017, the Tax Cuts and Jobs Act (the "Act") was signed into law resulting in a reduction in the Company's federal income tax rate to 21% from 34% effective January 1, 2018.

In February 2018, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2018-02, Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which would require entities to reclassify from accumulated other comprehensive income (AOCI) to retained earnings the effects of the change in the federal tax rate under the Act on deferred amounts that were originally recorded in other comprehensive income. The amount of the reclassification would exclude the effects of any valuation allowance previously charged to income from continuing operations. The Company has chosen to early adopt this ASU which resulted in a reclassification of $513,000 from AOCI to retained earnings in the consolidated financial statements.

Employee Benefit Plans

The Bank has a noncontributory defined benefit pension plan that covers all eligible employees. Benefits are based upon years of service, the employee's compensation, and age at retirement. The Bank's contribution is actuarially determined and is intended to meet the current and projected obligations of the plan. The Bank has a noncontributory defined contribution plan that covers all eligible employees.

Trust Assets and Income

Assets held by the Bank in a fiduciary or agency capacity for its customers are not included in the accompanying financial statements, since such items are not assets of the Bank. The fair value of trust assets under administration were $117,963,000 and $128,902,000 as of December 31, 2017 and 2016, respectively. In accordance with banking industry practice, trust services income is recognized on the cash basis and is not materially different than if it was reported on the accrual basis.

Comprehensive Income

The Company is required to present comprehensive income and its components in a full set of general-purpose financial statements for all periods presented. Other comprehensive income (loss) is comprised of net unrealized holding gains or losses on its available-for-sale investment securities as well as changes in unrecognized pension cost.

Earnings Per Share

The Company currently maintains a simple capital structure; therefore, there are no dilutive effects on earnings per share. As such, earnings per share are calculated using the weighted-average number of shares outstanding for the periods.

Cash Flow Information

The Company has defined cash and cash equivalents as those amounts included in the consolidated balance sheet captions "cash and due from banks," and "interest-bearing deposits in other banks," with original maturities of 90 days or less (in thousands):

	2017	2016
Cash paid during the year for:		
Interest	**$ 2,826**	$ 2,411
Income taxes	**250**	300
Noncash investing transactions:		
Transfer of loans to real estate owned	**57**	50

Reclassification of Comparative Amounts

Certain comparative amounts for the prior year have been reclassified to conform to current-year classifications. Such reclassifications had no effect on stockholders' equity or net income.

2. OCC Consent Order and Federal Reserve Bank Resolution

On May 5, 2016, The Northumberland National Bank ("Bank"), the wholly owned subsidiary of Northumberland Bancorp, entered into a Stipulation and Consent to the Issuance of a Consent Order ("Order") with the Comptroller of the Currency of the United States of America, through its national bank examiners and other staff of the Office of the Comptroller of the Currency ("OCC"), which has supervisory authority over the Bank. In entering into the Order, the Bank did not concede to the findings or admit to any of the assertions therein. However, as a result of the Order, the Bank is considered under OCC regulations to be in a "troubled condition," meaning primarily that the Bank must seek the OCC's advance consent to hiring certain executive officers or adding directors, to entering into agreements with Bank officers which provide for "golden parachute" payments, and to making "golden parachute" payments, and that the Bank is not eligible to receive expedited consideration of certain actions for which it must seek the OCC's advance approval, such as opening a new branch office.

The provisions of the Order are summarized below. The full text of the Order has been published by the OCC on its website (www.occ.gov). The actions to be taken by the Bank's Board of Directors ("Board"), as a result of the Order, were required to be taken within time periods specified in the Order and, in some cases, must be taken periodically on an ongoing basis. The Board intends to fully comply with all the requirements of the Order.

Compliance Committee. The Board was required to appoint and maintain a Compliance Committee of at least three directors, whose main function is to monitor and report to the OCC on the Bank's compliance with the Order. The Compliance Committee was established on the day that the Order was issued and continues to meet at least monthly.

Board Supervision and Competent Management. The Order requires the Board to ensure that the Bank has competent and effective full-time management in place for all executive officer positions at the Bank. The Board is also required to evaluate corporate governance processes and management supervision in light of the Bank's condition, to establish, at least annually, the objectives it will use to measure the effectiveness of the Bank's executive officers, to perform an annual independent written performance appraisal for each of the Bank's executive officers, including the President, after identifying any deficiency in an officer's performance as a result of the annual performance appraisal to identify what corrective action is required to address the deficiency and ensure the Bank implements and adheres to such corrective action, and to develop and thereafter maintain and update a written Board and management succession program that identifies the Bank's future management requirements and promotes the retention and continuity of competent and experienced management and board members.

Cross Trading Remediation. The Order required the Board to adopt policies, procedures, and controls for the crossing of buy and sell orders for securities on a fair and equitable basis to the parties to the transaction, where permissible under applicable law. With respect to cross trades which the Trust Department conducted at par value between 2002 and 2014, the Bank was required to adhere to the cross-trade Reimbursement Plan previously submitted to the OCC and to not make any changes to the Reimbursement Plan without submitting a request to and receiving a written determination of no supervisory objection from the OCC. The Bank has substantially completed the Reimbursement Plan.

Forensic Investigation Findings. The Order requires the Board to periodically report on the Bank's progress in addressing the concerns identified in the Bank's forensic investigation of past Trust Department activities, and the Bank continues to do so.

Account Administration. The Order required the Board to submit to the OCC for a written determination of no supervisory objection written policies and procedures for the proper administration of fiduciary and custody accounts.

Investment Management Processes. The Order required the Board to submit a written investment management program to the OCC for a written determination of no supervisory objection. Additionally, the Board must ensure the Bank's engagement of any third party to assist the Bank with its investment management program is consistent with the OCC's guidance on third party engagements.

Asset Management Governance and Controls. The Order required the Board to adopt a program to ensure effective oversight and controls for trust department operations, after submitting the program to the OCC and obtaining an indication of no objection. Additionally, the Bank's internal audit function must periodically test and verify that the Bank is adhering to the program and that it remains effective and is functioning as designed.

Asset Management Fees and Earnings. The Order requires the Board to adopt fee schedules that cover all accounts administered by the Trust Department. The Bank was required to enter into account agreements implementing the new fee schedule and giving the Bank the appropriate authority to manage trust accounts by September 30, 2017, and management believes that the re-contracting process will be complete by March 31, 2018. Additionally, the Board must adopt and ensure the Bank implements and thereafter adheres to a process for reviewing all accounts administered by the trust department to ensure such accounts are charged fees in accordance with the fee schedules developed pursuant to the Order.

Fiduciary Audit. The Order required the Board to adopt a revised Fiduciary Audit Program that complies with OCC regulations and to ensure that the Bank adheres to the new Program.

Bank Secrecy Act/Anti-Money Laundering Internal Controls. The Order required the Board to adopt and ensure that the Bank implements and thereafter adheres to a revised Bank Secrecy Act/Anti-Money Laundering ("BSA/AML") written compliance program that covers the Bank's Trust Department. Additionally, the Board must ensure the Bank's ongoing compliance with the Bank Secrecy Act, that the Bank reviews and updates its BSA/AML customer risk rating process and methodology for Trust Department customers and accounts in accordance with the Federal Financial Institutions Examination Council ("FFIEC") BSA/AML Examination Manual and other applicable regulatory guidance, that the Bank reviews and updates, in accordance with the FFIEC BSA/AML Examination Manual and other applicable regulatory guidance, its risk-based processes to obtain and analyze appropriate customer due diligence information for Trust Department customers and accounts at the time of account opening and on an ongoing basis, and effectively use the information in monitoring account activity, and investigating suspicious or unusual activity, that the Bank develops, implements, and thereafter adheres to suspicious activity monitoring policies, procedures and processes to ensure the Bank's timely and effective identification and review of potential suspicious activity involving customer relationships and accounts administered by the trust department, and the Bank's compliance with reporting requirements, and that the Bank has an effective risk-based BSA/AML independent testing function to ensure the Bank's adherence to effective BSA/AML internal controls for trust department customers and accounts, including evaluation of the Bank's BSA/AML risk assessment, and customer due diligence, enhanced due diligence and suspicious activity monitoring processes for trust customers and accounts.

Violations of Law. The Order requires the Board to immediately take all necessary steps to ensure that Bank management corrects each violation of law, rule or regulation recently cited by the OCC and to adopt, implement, and thereafter ensure Bank adherence to specific procedures to which incorporate internal control systems and education of employees regarding laws, rules and regulations applicable to their areas of responsibility.

On December 6, 2016, the directors of the Company adopted a resolution at the request of the Federal Reserve Bank of Philadelphia ("FRB"). In the resolution, the directors committed to addressing concerns raised by the FRB with respect to the same issues which were the subject of the OCC's Consent Order and to providing regular progress reports to the FRB on the Company's progress. The Company intends to fully comply with all the requirements of the resolution.

In connection with the OCC Consent Order and the resolution adopted at the request of the FRB, including the related investigation, the Company incurred professional fees of $277,000 and $562,000 for 2017 and 2016, respectively, and made or accrued reimbursements to customers of $227,000 in 2017 and $36,000 in 2016.

3. Investment Securities

The amortized cost and fair values of investment securities are as follows (in thousands):

December 31, 2017	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Obligations of states and political subdivisions	$ 56,758	$ 269	$ (518)	$ 56,509
Mortgage-backed securities in government sponsored entities	89,444	99	(1,129)	88,414
	146,202	368	(1,647)	144,923
Equity securities in financial institutions	167	35	-	202
Total	$ 146,369	$ 403	$ (1,647)	$ 145,125

December 31, 2016		Amortized Cost		Gross Unrealized Gains		Gross Unrealized Losses		Fair Value
Available-for-sale:								
Obligations of states and political subdivisions	$	58,619	$	266	$	(759)	$	58,126
Mortgage-backed securities in government sponsored entities		92,330		124		(1,119)		91,335
		150,949		390		(1,878)		149,461
Equity securities in financial institutions		167		38		-		205
Total	$	151,116	$	428	$	(1,878)	$	149,666

December 31, 2017		Amortized Cost		Gross Unrealized Gains		Gross Unrealized Losses		Fair Value
Held-to-maturity:								
Obligations of states and political subdivisions	**$**	**650**	**$**	**-**	**$**	**(2)**	**$**	**648**
Total	**$**	**650**	**$**	**-**	**$**	**(2)**	**$**	**648**

December 31, 2016		Amortized Cost		Gross Unrealized Gains		Gross Unrealized Losses		Fair Value
Held-to-maturity:								
Obligations of states and political subdivisions	$	1,692	$	-	$	(6)	$	1,686
Total	$	1,692	$	-	$	(6)	$	1,686

The following tables show the Company's gross unrealized losses and fair value, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position, at December 31, 2017 and 2016 (in thousands).

December 31, 2017	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-sale:						
Obligations of states and political subdivisions	**$ 16,652**	**$ (183)**	**$ 8,842**	**$ (335)**	**$ 25,494**	**$ (518)**
Mortgage-backed securities in government sponsored entities	**27,686**	**(296)**	**47,007**	**(833)**	**74,693**	**(1,129)**
Total	**$ 44,338**	**$ (479)**	**$ 55,849**	**$ (1,168)**	**$ 100,187**	**$ (1,647)**
Held-to-maturity:						
Obligations of states and political subdivisions	**$ 641**	**$ (2)**	**$ -**	**$ -**	**$ 641**	**$ (2)**
Total	**$ 641**	**$ (2)**	**$ -**	**$ -**	**$ 641**	**$ (2)**

December 31, 2016	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-sale:						
Obligations of states and political subdivisions	$ 29,352	$ (759)	$ -	$ -	$ 29,352	$ (759)
Mortgage-backed securities in government sponsored entities	35,616	(681)	39,393	(438)	75,009	(1,119)
Total	$ 64,968	$ (1,440)	$ 39,393	$ (438)	$ 104,361	$ (1,878)
Held-to-maturity:						
Obligations of states and political subdivisions	$ 647	$ (2)	$ 784	$ (4)	$ 1,431	$ (6)
Total	$ 647	$ (2)	$ 784	$ (4)	$ 1,431	$ (6)

The Company reviews its unrealized loss positions quarterly and has asserted that at December 31, 2017 and 2016, the declines outlined in the above tables represent temporary declines and the Company does not intend to sell and does not believe it will be required to sell these securities before recovery of their cost basis, which may be at maturity. There were 184 and 198 positions that were temporarily impaired at December 31, 2017 and 2016, respectively. The Company has concluded that the unrealized losses disclosed above are not other than temporary but are the result of interest rate changes, sector credit ratings changes, or issuer-specific ratings changes that are not expected to result in the noncollection of principal and interest during the period.

The amortized cost and fair value of debt securities at December 31, 2017, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties (in thousands).

	Available-for-Sale		Held-to-Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	**$ 7,599**	**$ 7,577**	**$ 396**	**$ 395**
Due after one year through five years	**73,611**	**73,076**	**247**	**246**
Due after five years through ten years	**49,274**	**48,625**	**-**	**-**
Due after ten years	**15,718**	**15,645**	**7**	**7**
Total	**$ 146,202**	**$ 144,923**	**$ 650**	**$ 648**

Proceeds from the sales of available-for-sale securities during 2017 amounted to $14,483,000 resulting in gross gains and gross losses of $65,000 and $(96,000), respectively. Proceeds from the sales of available-for-sale securities during 2016 amounted to $29,294,000 resulting in gross gains and gross losses of $187,000 and $(24,000), respectively.

Investment securities with fair values of $74,196,000 and $66,577,000 at December 31, 2017 and 2016, respectively, were pledged to secure public deposits and other purposes as required by law.

4. Loans

Major classifications of loans are summarized as follows (in thousands):

	2017	2016
Commercial	**$ 63,179**	$ 64,568
Commercial real estate	**70,614**	53,699
Residential real estate	**183,536**	177,454
Consumer	**4,187**	4,480
	321,516	300,201
Less allowance for loan losses	**2,910**	2,778
Net Loans	**$ 318,606**	$ 297,423

The Company grants residential, commercial, and consumer loans to customers throughout its trade area, which is concentrated in North Central Pennsylvania. Although the Company has a diversified loan portfolio at December 31, 2017 and 2016, a substantial portion of its debtors' ability to honor their loan agreements is dependent upon the economic stability of its immediate trade area.

5. Allowance for Loan Losses

Changes in the allowance for loan losses by portfolio segment are as follows (in thousands):

December 31, 2017	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Beginning Balance	**$ 671**	**$ 284**	**$ 1,483**	**$ 40**	**$ 300**	**$ 2,778**
Charge-offs	**(5)**	**-**	**(71)**	**(32)**	**-**	**(108)**
Recoveries	**11**	**-**	**1**	**1**	**-**	**13**
Provision	**(103)**	**215**	**52**	**36**	**27**	**227**
Ending Balance	**$ 574**	**$ 499**	**$ 1,465**	**$ 45**	**$ 327**	**$ 2,910**

December 31, 2016	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Beginning Balance	$ 722	$ 331	$ 1,382	$ 39	$ 200	$ 2,674
Charge-offs	(3)	-	(86)	(18)	-	(107)
Recoveries	-	-	2	1	-	3
Provision	(48)	(47)	185	18	100	208
Ending Balance	$ 671	$ 284	$ 1,483	$ 40	$ 300	$ 2,778

Management has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and losses inherent in the loan portfolio. For purposes of determining the allowance for loan losses, the Company has segmented certain loans in the portfolio by product type. Loans are segmented into the following pools: commercial, commercial real estate loans, residential real estate loans, and consumer loans. Historical loss percentages for each risk category are calculated and used as the basis for calculating allowance allocations. These historical loss percentages are calculated over a two-year period during 2017 and a two-year period during 2016 for all portfolio segments. Certain qualitative factors are then added to the historical allocation percentage to apply the adjusted factor to nonclassified loans. The following qualitative factors are analyzed for each portfolio segment and are adjusted based upon relevant changes within the portfolio:

- Levels of and trends in delinquencies
- Trends in volume and terms
- Trends in credit quality ratings
- Changes in management and lending staff
- Economic trends
- Concentrations of credit

In addition, regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses and may require the Bank to recognize additions to the allowance based on their judgments about information available to them at the time of their examination, which may not be currently available to management. Based on management's comprehensive analysis of the loan portfolio, management believes the current level of the allowance for loan losses is adequate.

The total allowance reflects management's estimate of loan losses inherent in the loan portfolio at the consolidated balance sheet date. The Company considers the allowance for loan losses of $2,910,000 and $2,778,000 adequate to cover loan losses inherent in the loan portfolio at December 31, 2017 and 2016, respectively. The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment evaluation method as of December 31, 2017 and 2016 (in thousands):

December 31, 2017	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses:						
Individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -
Collectively evaluated for impairment	574	499	1,465	45	327	2,910
Total	$ 574	$ 499	$ 1,465	$ 45	$ 327	$ 2,910
Loans:						
Individually evaluated for impairment	$ 1,005	$ -	$ 141	$ -	$ -	$ 1,146
Collectively evaluated for impairment	62,174	70,614	183,395	4,187	-	320,370
Total	$ 63,179	$ 70,614	$ 183,536	$ 4,187	$ -	$ 321,516

December 31, 2016	Commercial	Commercial Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses:						
Individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -
Collectively evaluated for impairment	671	284	1,483	40	300	2,778
Total	$ 671	$ 284	$ 1,483	$ 40	$ 300	$ 2,778
Loans:						
Individually evaluated for impairment	$ 1,313	$ -	$ 78	$ -	$ -	$ 1,391
Collectively evaluated for impairment	63,255	53,699	177,376	4,480	-	298,810
Total	$ 64,568	$ 53,699	$ 177,454	$ 4,480	$ -	$ 300,201

Credit Quality Information

The Company's internally assigned grades are as follows:

Pass loans are protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral. There are five sub-grades within the pass category to further distinguish the loan.

Special Mention loans are loans for which a potential weakness or risk exists, which could cause a more serious problem if not corrected.

Substandard loans have a well-defined weakness based on objective evidence and are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected.

Doubtful loans have all the weaknesses inherent in a substandard asset. In addition, these weaknesses make collection or liquidation in full highly questionable and improbable, based on existing circumstances.

Loss loans are considered uncollectible, or of such value that continuance as an asset is not warranted.

The following tables represent credit exposures by internally assigned grades for the years ended December 31, 2017 and 2016. The grading analysis estimates the capability of the borrower to repay the contractual obligations of the loan agreements as scheduled or at all. The Company's internal credit risk grading system is based on experiences with similarly graded loans (in thousands).

December 31, 2017	Obligations of States and Political Subdivisions	Other Commercial Loans	Loans for Investment Properties	Other Commercial Real Estate Loans	Total
Pass	**$ 15,553**	**$ 43,531**	**$ 27,970**	**$ 42,188**	**$ 129,242**
Special Mention					
Substandard	**-**	**4,095**	**243**	**213**	**4,551**
Doubtful	**-**	**-**	**-**	**-**	**-**
Loss	**-**	**-**	**-**	**-**	**-**
Ending Balance	**$ 15,553**	**$ 47,626**	**$ 28,213**	**$ 42,401**	**$ 133,793**

December 31, 2016	Obligations of States and Political Subdivisions	Other Commercial Loans	Loans for Investment Properties	Other Commercial Real Estate Loans	Total
Pass	$ 17,247	$ 44,789	$ 24,383	$ 29,276	$ 115,695
Special Mention	-	-	-	-	-
Substandard	-	2,532	40	-	2,572
Doubtful	-	-	-	-	-
Loss	-	-	-	-	-
Ending Balance	$ 17,247	$ 47,321	$ 24,423	$ 29,276	$ 118,267

The following tables present performing and nonperforming residential real estate and consumer loans based on payment activity for the years ended December 31, 2017 and 2016. Payment activity is reviewed by management on a monthly basis to determine how loans are performing. Loans are considered to be nonperforming when they become 90 days past due or are placed on nonaccrual (in thousands).

December 31, 2017	First Mortgages	Home Equity Loans	Consumer	Total
Performing	**$ 155,874**	**$ 27,067**	**$ 4,187**	**$ 187,128**
Nonperforming	**574**	**21**	**-**	**595**
Total	**$ 156,448**	**$ 27,088**	**$ 4,187**	**$ 187,723**

December 31, 2016	First Mortgages	Home Equity Loans	Consumer	Total
Performing	$ 149,182	$ 27,408	$ 4,479	$ 181,069
Nonperforming	840	24	1	865
Total	$ 150,022	$ 27,432	$ 4,480	$ 181,934

Following are tables which include an aging analysis of the recorded investment of past-due loans as of December 31, 2017 and 2016 (in thousands):

December 31, 2017	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater	Total Past Due	Current	Total
Commercial:						
Obligations of states and political subdivisions	**$ -**	**$ -**	**$ -**	**$ -**	**$ 15,553**	**$ 15,553**
Other commercial loans	**17**	**-**	**-**	**17**	**47,609**	**47,626**
Commercial real estate:						
Loans for investment property	**-**	**-**	**163**	**163**	**28,050**	**28,213**
Other commercial real estate loans	**34**	**-**	**-**	**34**	**42,367**	**42,401**
Residential mortgage loans:						
First mortgages	**2,268**	**219**	**761**	**3,248**	**153,200**	**156,448**
Home equity loans	**154**	**33**	**40**	**227**	**26,861**	**27,088**
Consumer	**65**	**1**	**1**	**67**	**4,120**	**4,187**
Total	**$ 2,538**	**$ 253**	**$ 965**	**$ 3,756**	**$ 317,760**	**$ 321,516**

December 31, 2016	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater	Total Past Due	Current	Total
Commercial:						
Obligations of states and political subdivisions	$ -	$ -	$ -	$ -	$ 17,247	$ 17,247
Other commercial loans	129	-	189	318	47,081	47,321
Commercial real estate:						
Loans for investment property	-	-	40	40	24,383	24,423
Other commercial real estate loans	37	-	-	37	29,239	29,276
Residential mortgage loans:						
First mortgages	1,446	204	935	2,585	147,359	150,022
Home equity loans	75	82	51	208	27,224	27,432
Consumer	30	3	1	34	4,446	4,480
Total	$ 1,717	$ 289	$ 1,216	$ 3,222	$ 296,979	$ 300,201

Impaired Loans

Management evaluates commercial loans and commercial real estate loans which are 90 days or more past due and considers them to be impaired. Loans rated substandard or doubtful are also evaluated for impairment. These loans are analyzed to determine whether it is probable that all amounts will not be collected according to the contractual terms of the loan agreement. If management determines that the value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees, or costs and unamortized premium or discount), impairment is recognized through an allowance estimate or a charge-off to the allowance.

The following tables include the recorded investment and unpaid principal balances for impaired loans with the associated allowance amount, if applicable, as of and for the years ending December 31 (in thousands):

December 31, 2017	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial:					
Other commercial loans	**$ 1,005**	**$ 1,005**	**$ -**	**$ 1,081**	**$ -**
Commercial real estate:					
Loans for investment properties	**-**	**-**	**-**	**-**	**-**
Residential real estate:					
First mortgages	**141**	**141**	**-**	**117**	**-**
With an allowance recorded:					
Commercial:					
Other commercial loans	**-**	**-**	**-**	**-**	**-**
Commercial real estate:					
Loans for investment properties	**-**	**-**	**-**	**-**	**-**
Residential mortgage loans:					
First mortgages	**-**	**-**	**-**	**-**	**-**
Total	**$ 1,146**	**$ 1,146**	**$ -**	**$ 1,198**	**$ -**

December 31, 2016	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial:					
Other commercial loans	$ 1,313	$ 1,313	$ -	$ 1,339	$ -
Commercial real estate:					
Loans for investment properties	-	-	-	-	-
Residential real estate:					
First mortgages	78	78	-	91	-
With an allowance recorded:					
Commercial:					
Other commercial loans	-	-	-	-	-
Commercial real estate:					
Loans for investment properties	-	-	-	-	-
Residential mortgage loans:					
First mortgages	-	-	-	-	-
Total	$ 1,391	$ 1,391	$ -	$ 1,430	$ -

Nonaccrual Loans

Loans are considered for nonaccrual status upon 90 days delinquency. When a loan is placed in nonaccrual status, previously accrued but unpaid interest is deducted from interest income.

The following tables present loans that are on nonaccrual status and that are 90 days delinquent and still accruing interest by portfolio segment as of December 31 (in thousands):

December 31, 2017	Nonaccrual	Past Due 90 Days or More and Still Accruing
Commercial:		
Obligations of states and political subdivisions	**$ -**	**$ -**
Other commercial loans	**1,005**	**-**
Commercial real estate:		
Loans for investment properties	**-**	**-**
Other commercial real estate loans		
Residential mortgage loans:		
First mortgages	**574**	**590**
Home equity loans	**21**	**40**
Consumer loans	**-**	**1**
	$ 1,600	**$ 631**

December 31, 2016	Nonaccrual	Past Due 90 Days or More and Still Accruing
Commercial:		
Obligations of states and political subdivisions	$ -	$ -
Other commercial loans	1,313	-
Commercial real estate:		
Loans for investment properties	40	-
Other commercial real estate loans	-	-
Residential mortgage loans:		
First mortgages	279	589
Home equity loans	27	22
Consumer loans	-	1
	$ 1,659	$ 612

Interest income on nonaccrual loans not recognized during 2017 and 2016 was $96,000 and $101,000, respectively.

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

Troubled debt restructurings (TDR) may be designated as performing or non-performing. A TDR may be designated as performing if the loan has demonstrated sustained performance under the modified terms. The period of sustained performance may include the periods prior to modification if prior performance met or exceeded the modified terms. For non-performing restructured loans, the loan will remain on non-accrual status until the borrower demonstrates a sustained period of performance, generally six consecutive months of payments. The Bank had $141,000 and $268,000 in total performing restructured loans as of December 31, 2017 and 2016, respectively. During the year ended December 31, 2017 and 2016, the Bank did not have any loans classified as troubled debt restructurings that subsequently defaulted.

The following table reflects information regarding the Bank's troubled debt restructurings at December 31, 2017 and 2016 (in thousands):

	2017		2016	
	Modification of Payment and Other Terms		Modification of Payment and Other Terms	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
Commercial	**-**	**$ -**	1	$ 190
Residential real estate	**5**	**141**	4	78
Total	**5**	**$ 141**	5	$ 268

6. Premises and Equipment

Major classifications of premises and equipment are summarized as follows (in thousands):

December 31,	**2017**	2016
Land and improvements	**$ 1,458**	$ 1,458
Buildings and improvements	**9,984**	9,973
Furniture, fixtures and equipment	**4,411**	4,281
	15,853	15,712
Less accumulated depreciation	**6,492**	5,932
Total	**$ 9,361**	$ 9,780

Depreciation expense for the years ended December 31, 2017 and 2016 was $623,000 and $652,000, respectively.

7. Deposits

The components of deposits at December 31, 2017 and 2016 are as follows (in thousands):

	2017	2016
Demand, noninterest-bearing	**$ 78,221**	$ 73,621
Demand, interest-bearing	**68,535**	59,786
Savings	**82,661**	81,318
Money Market Accounts	**95,858**	109,769
Time, $250 and over	**25,145**	22,961
Time, other	**102,956**	95,175
Total	**$ 453,376**	$ 442,630

Time deposits and their remaining maturities at December 31, 2017 are as follows (in thousands):

Year Ending December 31,	
2018	$ 35,109
2019	29,644
2020	38,914
2021	18,295
2022	6,065
Thereafter	74
	$ 128,101

8. Short-Term Borrowings

Borrowings at December 31, 2017 and 2016 consisted of the following short-term notes with the Federal Home Loan Bank (dollars in thousands):

Maturity Date	Interest Rate	2017	2016
January 2, 2018	**1.54%**	**$ 3,000**	$ -
Total		**$ 3,000**	$ -

9. Income Taxes

The provision for income taxes consists of (in thousands):

		2017		2016
Current	$	887	$	374
Deferred		276		217
Total	$	1,163	$	591

The tax effects of deductible and taxable temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities, respectively, at December 31 are as follows:

		2017		2016
Deferred tax assets:				
Allowance for loan losses	$	565	$	870
Accrued pension obligation		573		856
Unrealized loss on investment securities		256		500
Alternative minimum tax credit		201		201
Other		178		268
Total gross deferred tax assets		1,773		2,695
Deferred tax liabilities:				
Premises and equipment		267		477
Investment accretion		2		4
Prepaid pension costs		262		622
Loan origination fees and costs		80		114
Other		37		60
Total gross deferred tax liabilities		648		1,277
Net Deferred Tax Asset	$	1,125	$	1,418

No valuation allowance was established at December 31, 2017 and 2016, in view of the Company's ability to carryback to taxes paid in previous years and certain tax strategies, coupled with the anticipated future taxable income as evidenced by the Company's earnings potential. Deferred tax assets are included in accrued interest and other assets and deferred tax liabilities are included in accrued interest and other liabilities on the balance sheet.

The following is a reconciliation of the federal statutory rate and the Company's effective income tax rate for the years ended December 31 (dollars in thousands):

	2017			2016		
	Amount	% of Pretax Income		Amount	% of Pretax Income	
Provision at statutory rate	**$ 1,067**	**34.0**	**%**	$ 1,171	34.0	%
Effect of tax-exempt income	**(426)**	**(13.6)**		(603)	(17.5)	
Nondeductible interest expense	**22**	**0.7**		21	0.5	
Revaluation of certain deferred tax assets and liabilities	**569**	**18.1**				
Other	**(69)**	**(2.2)**		2	-	
Actual Tax Expense and Effective Rate	**$ 1,163**	**37.0**	**%**	$ 591	17.0	%

On December 22, 2017, H.R.1, commonly known as the Tax Cuts and Jobs Act (the "Act"), was signed into law. The Act includes several provisions that will affect the Company's federal income tax expense, including reducing the federal income tax rate to 21% from 34% effective January 1, 2018. As a result of the rate reduction, the Company is required to re-measure, through income tax expense in the period of enactment, the deferred tax assets and liabilities using the enacted rate at which these items are expected to be recovered or settled. The re-measurement of the Company's net deferred tax asset resulted in additional 2017 deferred income tax expense of $569,000.

The Company prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Benefits from tax positions should be recognized in the financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority that would have full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be derecognized in the first subsequent financial reporting period in which that threshold is no longer met.

There is currently no liability for uncertain tax positions and no known unrecognized tax benefits. The Company recognizes, when applicable, interest and penalties related to unrecognized tax benefits in the provision for income taxes in the consolidated statements of income. With few exceptions, the Company is no longer subject to U.S. federal or state income tax examinations by tax authorities for years before 2013.

10. Commitments and Contingencies

In the normal course of business, the Company makes various commitments that are not reflected in the accompanying consolidated financial statements. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The Company's exposure to credit loss in the event of nonperformance by the other parties to the financial instruments is represented by the contractual amounts as disclosed. Losses, if any, are charged to the allowance for loan losses. The Company minimizes its exposure to credit loss under these commitments by subjecting them to credit approval, review procedures, and collateral requirements as deemed necessary.

The off-balance sheet commitments consisted of the following (in thousands):

	2017	2016
Commitments to extend credit	$ 64,264	$ 66,419
Standby letters of credit	5,563	6,367

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the loan agreement. These commitments are composed primarily of available commercial lines of credit and mortgage loan commitments. The Company uses the same credit policies in making loan commitments and conditional obligations as it does for on-balance sheet instruments. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, as deemed necessary, is based upon management's credit evaluation in compliance with the Company's lending policy guidelines. Customers use credit commitments to ensure funds will be available for working capital purposes, for capital expenditures, and to ensure access to funds at specified terms and conditions.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Performance letters of credit represent conditional commitments issued by the Company to guarantee the performance of a customer to a third party. These instruments are issued primarily to support bid- or performance-related contracts. The coverage period for these instruments is typically a one-year period with an annual renewal option subject to prior approval by management. Fees earned from the issuance of these letters are recognized over the coverage period. For secured letters of credit, the collateral is typically company deposit instruments or customer business assets.

As discussed in Note 2, the Bank entered into a Consent Order with the OCC and the Company adopted a resolution at the request of the FRB and incurred costs in connection therewith, including professional fees and reimbursements to customers.

11. Pension Plan

The Bank sponsors a defined benefit pension plan covering substantially all employees and officers. The Plan calls for benefits to be paid to eligible employees at retirement, based primarily upon years of service with the Bank and compensation rates during employment. The Bank's funding policy is to make annual contributions, if needed, based upon the funding formula developed by the plan's actuary.

The following table sets forth the obligation and funded status as of December 31 (in thousands):

	2017	2016
Change in benefit obligation:		
Benefit obligation at beginning of year	**$ 10,853**	$ 9,613
Service cost	**814**	786
Interest cost	**441**	420
Change in assumptions	**1,181**	293
Actuarial loss (gains)	**(85)**	109
Benefits paid	**(422)**	(368)
Benefit obligation at end of year	**12,782**	10,853
Change in plan assets:		
Fair value of plan assets at beginning of year	**10,191**	8,899
Actual return on plan assets	**1,560**	860
Employer contribution	**-**	800
Benefits paid	**(422)**	(368)
Fair value of plan assets at end of year	**11,329**	10,191
Funded Status, included in Other Liabilities	**$ (1,453)**	$ (662)

	2017	2016
Amounts recognized in accumulated other comprehensive loss consist of:		
Net loss	**$ 2,729**	$ 2,518
Total	**$ 2,729**	$ 2,518

The accumulated benefit obligation for the defined benefit pension plan was $10,713,000 and $9,059,000 at December 31, 2017 and 2016, respectively.

Components of Net Periodic Benefit Cost

		2017		2016
Net periodic pension cost:				
Service cost	$	814	$	786
Interest cost		441		420
Expected return on plan assets		(771)		(707)
Amortization of net loss		97		101
Net Periodic Benefit Cost	$	581	$	600

The estimated net loss for the defined benefit pension plan that will be amortized from accumulated other comprehensive loss into net periodic benefit cost over the next fiscal year is $102,000.

Assumptions

The weighted-average assumptions used to determine benefit obligations at December 31:

	2017		2016	
Discount rate	3.59	%	4.14	%
Rate of compensation increase	4.00		4.00	

The weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:

	2017		2016	
Discount rate	4.14	%	4.35	%
Expected long-term return on plan assets	8.00		8.00	
Rate of compensation increase	4.00		4.00	

The long-term rate of return on plan assets gives consideration to returns currently being earned on plan assets, as well as future rates expected to be returned.

Plan Assets

The Bank's defined benefit pension plan weighted-average asset allocations at December 31 by asset category are as follows:

	2017		2016	
Asset category:				
Mutual funds	73.69	%	70.14	%
Corporate bonds	22.95		26.39	
U.S. government agency securities	2.07		2.29	
Cash and cash equivalents	1.29		1.18	
Total	100.00	%	100.00	%

The Bank believes that the Plan's risk and liquidity position are, in large part, a function of the asset class mix. The Bank desires to utilize a portfolio mix that results in a balanced investment strategy. The investment objective for the defined benefit pension plan is to maximize total return with tolerance for average to slightly above average risk. Asset allocation strongly favors mutual funds.

The following table sets forth by level, within the fair value hierarchy, the plan's assets at fair value as of December 31, 2017 and 2016 (in thousands):

December 31, 2017	Level I	Level II	Level III	Total
Assets:				
Cash and cash equivalents	**$ 146**	**$ -**	**$ -**	**$ 146**
U.S. government agency securities	**-**	**235**	**-**	**235**
Corporate bonds	**-**	**2,600**	**-**	**2,600**
Mutual funds	**8,348**	**-**	**-**	**8,348**
Total Assets at Fair Value	**$ 8,494**	**$ 2,835**	**$ -**	**$ 11,329**

December 31, 2016	Level I	Level II	Level III	Total
Assets:				
Cash and cash equivalents	$ 120	$ -	$ -	$ 120
U.S. government agency securities	-	233	-	233
Corporate bonds	-	2,690	-	2,690
Mutual funds	7,148	-	-	7,148
Total Assets at Fair Value	$ 7,268	$ 2,923	$ -	$ 10,191

Cash Flows

Due to the funding position of the Plan, and the current interest rate environment, the Bank does not expect to make a contribution to its defined benefit pension plan in 2018.

The following benefit payments that reflect expected future service, as appropriate, are expected to be paid (in thousands):

	Pension Benefits
2018	$ 258
2019	272
2020	328
2021	378
2022 through 2027	3,193

12. Accumulated Other Comprehensive Loss

The following tables present the changes in accumulated other comprehensive loss by component net of tax for the years ended December 31, 2017 and 2016 (in thousands):

	Unrealized Gains (Losses) on Available-for-Sale Securities	Unrecognized Pension Costs	Total
Balance as of December 31, 2015	$ 271	$ (1,564)	$ (1,293)
Other comprehensive loss before reclassification	(1,105)	(31)	(1,136)
Amount reclassified from accumulated other comprehensive loss	(108)	(66)	(174)
Total other comprehensive loss	(1,213)	(97)	(1,310)
Balance as of December 31, 2016	(942)	(1,661)	(2,603)
Other comprehensive loss before reclassification	**116**	**(74)**	**42**
Amount reclassified from accumulated other comprehensive loss	**20**	**(64)**	**(44)**
Total other comprehensive loss	**136**	**(138)**	**(2)**
Reclassification of stranded tax effects	**(158)**	**(355)**	**(513)**
Balance as of December 31, 2017	**$ (964)**	**$ (2,154)**	**$ (3,118)**

The following table presents significant amounts reclassified out of each component of accumulated other comprehensive loss for the years ended December 31, 2017 and 2016 (in thousands):

	Amount Reclassified from Accumulated Other Comprehensive Loss		Affected Line Item in the Statement Where Net Income is Presented
	2017	2016	
Unrealized gains on available-for-sale securities:			
	$ 31	$ (163)	Investment securities gains, net
	(11)	55	Income taxes
	$ 20	$ (108)	Net of tax
Unrecognized pension costs:			
	$ 97	$ 100	Salaries and employee benefits
	(33)	(34)	Income tax
	$ 64	$ 66	Net of tax

13. Regulatory Matters

Cash and Due from Banks

The Bank is required to maintain average cash reserve balances in vault cash or with the Federal Reserve Bank. The amount of these restricted cash reserve balances at December 31, 2017 and 2016 was $-0-.

Loans

Federal law prevents the Company from borrowing from the Bank unless the loans are secured by specific collateral. Further, such secured loans are limited in amount to 10 percent of the Bank's common stock and capital surplus.

Dividends

The Bank is subject to a dividend restriction that generally limits the amount of dividends that can be paid by a national bank. Prior approval of the Office of the Comptroller of the Currency ("OCC") is required if the total of all dividends declared by a national bank in any calendar year exceeds net profits, as defined for the year, combined with its retained net profits for the two preceding calendar years less any required transfers to surplus. Using this formula, the amount available for payment of dividends by the Bank in 2018, without approval of the OCC, is approximately $2,997,000 plus 2018 net profits retained up to the date of the dividend declaration.

Capital Requirements

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet the minimum capital requirements can initiate certain mandatory and possibly additional discretionary-actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk-weightings and other factors.

Information presented for December 31, 2017 and 2016, reflects the Basel III capital requirements that became effective January 1, 2015 for the Bank. Prior to January 1, 2015, the Bank was subject to capital requirements under Basel I. Under these capital requirements and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk-weightings and other factors.

The risk-based capital rules adopted effective January 1, 2015 require that banks and holding companies maintain a "capital conservation buffer" of 250 basis points in excess of the "minimum capital ratio." The minimum capital ratio is equal to the prompt corrective action adequately capitalized threshold ratio. The capital conservation buffer is being phased in over a four year period that began January 1, 2016, with a required buffer of 0.625% of risk weighted assets for 2016, 1.25% for 2017, 1.875% for 2018, and 2.5% for 2019 and thereafter. Failure to maintain the required capital conservation buffer will result in limitations on capital distributions and on discretionary bonuses to executive officers.

Effective January 1, 2017, the capital levels required for the Bank to avoid these limitations were as follows:

- Common Equity Tier 1 capital ratio of 5.75%
- Tier 1 risk based capital ratio of 7.25%
- Total risk based capital ratio of 9.25%

As of December 31, 2017, the Bank had a conservation buffer greater than 2.5%.

In addition to the capital requirements, the Federal Deposit Insurance Corporation Improvement Act ("FDICIA") established five capital categories ranging from "well capitalized" to "critically undercapitalized." Should any institution fail to meet the requirements to be considered "adequately capitalized," it would become subject to a series of increasingly restrictive regulatory actions.

As of December 31, 2017 and 2016, the OCC categorized the Bank as well-capitalized under the regulatory framework for prompt corrective action. To be classified as a well-capitalized financial institution, Common equity Tier 1, Total risk-based, Tier I risk-based, and Tier I leverage capital ratios must be at least 6.5 percent, 10 percent, 6 percent, and 5 percent, respectively.

The Company's actual capital ratios are presented in the following table that shows the Company met all regulatory capital requirements. The capital position of the Bank does not differ significantly from the Company's capital position (dollars in thousands).

December 31, 2017	Actual		For Capital Adequacy Purposes		To be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Common equity Tier 1 (total risk-weighted assets)	**$ 51,867**	**18.31%**	**$ 12,745≥**	**≥4.5%**	**$ 18,410≥**	**≥ 6.5%**
Total capital (to risk-weighted assets)	**54,777**	**19.34%**	**22,658≥**	**≥8.0%**	**28,323≥**	**≥10.0%**
Tier I capital (to risk-weighted assets)	**51,867**	**18.31%**	**11,329≥**	**≥4.0%**	**16,994≥**	**≥ 6.0%**
Tier I capital (to average assets)	**51,867**	**10.31%**	**20,124≥**	**≥4.0%**	**25,155≥**	**≥ 5.0%**

December 31, 2016	Actual		For Capital Adequacy Purposes		To be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Common equity Tier 1 (total risk-weighted assets)	$ 50,332	18.57%	$ ≥12,200	≥4.5%	$ ≥17,622	≥ 6.5%
Total capital (to risk-weighted assets)	53,110	19.59%	≥21,688	≥8.0%	≥27,110	≥10.0%
Tier I capital (to risk-weighted assets)	50,332	18.57%	≥10,844	≥4.0%	≥16,266	≥ 6.0%
Tier I capital (to average assets)	50,332	10.33%	≥19,497	≥4.0%	≥24,372	≥ 5.0%

14. Fair Value Measurements

The following disclosures show the hierarchal disclosure framework associated with the level of pricing observations utilized in measuring assets and liabilities at fair value. The three broad levels of pricing observations are as follows:

Level I: Quoted prices are available in active markets for identical assets or liabilities as of the reported date.

Level II: Pricing inputs are other than the quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these assets and liabilities includes items for which quoted prices are available but traded less frequently and items that are fair-valued using other financial instruments, the parameters of which can be directly observed.

Level III: Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

This hierarchy requires the use of observable market data when available.

The following tables present the assets measured on a recurring basis on the consolidated balance sheets at their fair value as of December 31, 2017 and 2016, by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement (in thousands).

December 31, 2017	Level I	Level II	Level III	Total
Assets measured on a recurring basis:				
Investment securities available-for-sale:				
Obligations of states and political subdivisions	**$ -**	**$ 56,509**	**$ -**	**$ 56,509**
Mortgage-backed securities in government-sponsored entities	**-**	**88,414**	**-**	**88,414**
Equity securities in financial institutions	**202**	**-**	**-**	**202**
Total	**$ 202**	**$ 144,923**	**$**	**$ 145,125**

December 31, 2016	Level I	Level II	Level III	Total
Assets measured on a recurring basis:				
Investment securities available-for-sale:				
Obligations of states and political subdivisions	$ -	$ 58,126	$ -	$ 58,126
Mortgage-backed securities in government-sponsored entities	-	91,335	-	91,335
Equity securities in financial institutions	205	-	-	205
Total	$ 205	$ 149,461	$ -	$ 149,666

15. Fair Value of Financial Instruments

The fair values at December 31 of the Company's financial instruments are as follows (in thousands):

December 31, 2017	Carrying Value	Fair Value	Level I	Level II	Level III
Financial assets:					
Cash and cash equivalents	**$ 13,547**	**$ 13,547**	**$ 13,547**	**$ -**	**$ -**
Investment securities:					
Available-for-sale	**145,125**	**145,125**	**202**	**144,923**	**-**
Held-to-maturity	**650**	**641**	**-**	**641**	**-**
Loans held for sale	**1,353**	**1,353**	**1,353**	**-**	**-**
Net loans	**318,606**	**317,506**	**-**	**317,506**	**-**
Restricted stock	**3,806**	**3,806**	**-**	**3,806**	**-**
Mortgage servicing rights	**831**	**831**	**-**	**831**	**-**
Accrued interest receivable	**1,593**	**1,593**	**1,593**	**-**	**-**
Financial liabilities:					
Deposits	**$ 453,376**	**$ 436,292**	**$ -**	**$ 436,292**	**$ -**
Borrowings	**3,000**	**2,999**	**-**	**2,999**	**-**
Accrued interest payable	**111**	**111**	**111**	**-**	**-**

December 31, 2016	Carrying Value	Fair Value	Level I	Level II	Level III
Financial assets:					
Cash and cash equivalents	$ 14,248	$ 14,248	$ 14,248	$ -	$ -
Investment securities:					
Available-for-sale	149,666	149,666	205	149,461	-
Held-to-maturity	1,692	1,686	-	1,686	-
Loans held for sale	1,493	1,493	1,493	-	-
Net loans	297,423	300,218	-	300,218	-
Restricted stock	3,505	3,505	-	3,505	-
Mortgage servicing rights	893	893	-	893	-
Accrued interest receivable	1,408	1,408	1,408	-	-
Financial liabilities:					
Deposits	$ 442,630	$ 427,148	$ -	$ 427,148	$ -
Accrued interest payable	98	98	98	-	-

Financial instruments are defined as cash, evidence of ownership interest in an entity, or a contract that creates an obligation or right to receive or deliver cash or another financial instrument from/to a second entity on potentially favorable or unfavorable terms.

Fair value is defined as the amount at which a financial instrument could be exchanged in a current transaction between willing parties other than in a forced or liquidation sale. If a quoted market price is available for a financial instrument, the estimated fair value would be calculated based upon the market price per trading unit of the instrument.

If no readily available market exists, the fair value estimates for financial instruments should be based upon management's judgment regarding current economic conditions, interest rate risk, expected cash flows, future estimated losses, and other factors as determined through various option pricing formulas. As many of these assumptions result from judgments made by management based upon estimates that are inherently uncertain, the resulting estimated fair values may not be indicative of the amount realizable in the sale of a particular financial instrument. In addition, changes in assumptions on which the estimated fair values are based may have a significant impact on the resulting estimated fair values.

As certain assets, such as deferred tax assets and premises and equipment, are not considered financial instruments, the estimated fair value of financial instruments would not represent the full value of the Company.

The Company employed simulation modeling in determining the estimated fair value of financial instruments for which quoted market prices were not available based upon the following assumptions:

Cash and Cash Equivalents, Loans Held for Sale, Regulatory Stock, Accrued Interest Receivable, and Accrued Interest Payable

The fair value is equal to the current carrying value.

Investment Securities

The fair market value of investment securities is equal to the available quoted market price. If no quoted market price is available, fair value is estimated using the quoted market price for similar securities. Fair values for certain corporate bonds were determined utilizing discounted cash flow models, due to the absence of a current market to provide reliable market quotes for the instruments.

Loans

Fair value is estimated by discounting future cash flows using current market inputs at which loans with similar terms and qualities would be made to borrowers of similar credit quality. Where quoted market prices were available, primarily for certain residential mortgage loans, such market rates were utilized as estimates for fair value.

Mortgage Servicing Rights

The fair value for mortgage servicing rights is estimated by discounting contractual cash flows and adjusting for prepayment estimates. Discount rates are based upon rates generally charged for such loans with similar characteristics.

Demand, savings, and money market deposit accounts are valued at the amount payable on demand as of year-end.

Deposits

The fair values disclosed for demand deposits (interest and noninterest checking, savings and money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (their carrying amounts). The fair values of certificates of deposit are based on the discounted value of contractual cash flows. The discount rates are estimated using rates currently offered for similar instruments with similar remaining maturities.

Borrowings

Fair values of borrowings are estimated using discounted cash flow analysis, based on quoted prices for new borrowings with similar credit risk characteristics, terms and remaining maturity. These prices obtained from this active market represent a market value that is deemed to represent the transfer price if the liability were assumed by a third party.

Commitments to Extend Credit and Commercial Letters of Credit

These financial instruments are generally not subject to sale, and estimated fair values are not readily available.

The carrying value, represented by the net deferred fee arising from the unrecognized commitment or letter of credit, and the fair value, determined by discounting the remaining contractual fee over the term of the commitment using fees currently charged to enter into similar agreements with similar credit risk, are not considered material for disclosure. The contractual amounts of unfunded commitments and letters of credit are presented in Note 8.

16. Related Party Transactions

Certain officers, directors and other related parties have loans and conduct other transactions with the Bank. Deposits of related parties totaled $1,815,000 and $1,771,000 at December 31, 2017 and 2016, respectively. The aggregate dollar amount of loans to related parties, along with an analysis of the activity for December 31, 2017 and 2016 are as follows (in thousands):

	2017	2016
Balance, beginning	**$ 987**	$ 698
Additions	**698**	631
Repayments	**100**	391
Reclassification	**-**	49
Balance, ending	**$ 1,585**	$ 987

17. Employment Agreements

The Company entered into three-year employment agreements with certain members of management, which includes minimum annual salary commitments and change of control provisions. Upon resignation after a change in the control of the Company, as defined in the agreement, the individual will receive monetary compensation in the amount set forth therein. The agreements include covenant not-to-compete provisions and are subject to limitations as discussed in Note 2.

18. Subsequent Events

Management has reviewed events occurring through March 22, 2018, the date the financial statements were available to be issued and no subsequent events occurred requiring accrual or disclosure.