2018 ANNUAL REPORT

STRENGTH
THROUGH INDEPENDENCE

LITITZ PA

JBT'S NEWEST LOCATION ADDS FINANCIAL STRENGTH TO A GROWING COMMUNITY

Since our founding in 1873, Jonestown Bank & Trust Co. has focused on building long-term relationships with clients, working to add financial **strength** to their lives.

As an **independent** community bank, we have been able to be more flexible when creating financial solutions that help businesses and individuals – a valuable advantage.

Clients appreciate that we are strong with our **community** involvement, too. We proudly live, work and volunteer here.

As JBT continues to strengthen as a **local bank**, our directors, management and staff will continue to do everything possible to help enhance the communities we serve.

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jbt Bank on a Smile.

BOARD OF DIRECTORS

Richard J. Newmaster, Jr. CPA
Chairman
Director since 2004

Chief Financial Officer, Lebanon Seaboard Corp.

Jeffrey L. Bohn
Vice Chairman
Director since 1987

Former Owner & President, JP Donmoyer, Inc.

Executive Director, Shining Light Ministries

Edward L. Anspach
Second Vice Chairman and Secretary
Director since 1987

President, Anspach Autos

Troy A. Peters
Director since 2016

President and Chief Executive Officer, Jonestown Bank & Trust Co.

Lloyd A. Deaven, Jr.
Director since 1998

President, Patriot Auto Parts (retired)

Edwin C. Hostetter II CPA CGMA
Director since 2013

Vice President of Finance & Chief Financial Officer, SSM Group, Inc.

Brian R. Miller
Director since 2015

Insurance Agency Principal, Richard S. Miller, Inc.

Larry P. Minnich
Director since 2013

Operations Manager, Children's Heart Group, Milton S. Hershey Medical Center (retired); COO, Central Medical Ambulance Svcs.; Mayor, Borough of Cleona

Sallie A. Neuin
Director since 2009

Lebanon County Treasurer; Lebanon County Tax Claim Director

Eric A. Trainer
Director since 2011

Co-owner/Operator, Trainer's Midway Diner; Quality Inn at Midway; Microtel Inn & Suites–Hamburg; Pappy T's Pub & Lounge–Hamburg

Glenn T. Wenger
Director since 2008

President, Wengers of Myerstown; Chairman, Ag Industrial, Inc.; President, JK&B Inc.

EXECUTIVE OFFICERS

Troy A. Peters
President
Chief Executive Officer

C. William Roth
Chief Financial Officer

Edward T. Martel, Jr.
Chief Operating Officer

Timothy D. Gingrich
Chief Information Officer

Theresa L. Resanovich
Chief Trust Officer

Richard M. Rollman
Chief Lending Officer

LETTER TO SHAREHOLDERS

Richard J. Newmaster, Jr.
Chairman

Troy A. Peters
President
Chief Executive Officer

Dear Shareholders of Jonestown Bank & Trust Co.,

Your Bank had an outstanding year that included record earnings, substantial investment in the future, and expansion. The Bank produced a net income of $4,845,000, an 8% increase over the prior year and earnings per share of $2.07, a 7.25% increase over 2017. Return on average assets finished at 0.84% and return on average equity was 9.62%. Our core business results were strong, and we benefited from the Tax Cuts and Jobs Act which reduced the corporate income tax rate.

Deposits

We began the year with a focus on deposit generation as we ended the previous year with a loan-to-deposit ratio of 107.09%. We had a need to fund our loan growth with reasonably priced deposits and borrowings. The rate environment was dynamic as we experienced four Federal Open Market Committee rate hikes during the year, moving the fed funds target rate range from 1.25–1.50% to 2.25–2.50%. This is the first time we have seen four rate increases in one year since 2006, and it was on the heels of three increases in 2017. Although the competition for deposits began to heat-up, we were able to grow deposits at a level of 8.25% or $38 million. This was beyond our targeted expectations. This growth can be attributed to a number of factors, including our enhanced product set and the focus of our employees to build and execute tactics that gather deposit dollars.

We also had success entering a market that few banks have, and that is banking marijuana-related businesses in the Commonwealth of Pennsylvania. With the legalization of medical marijuana, we saw an opportunity to support businesses in this industry with banking services. After much research and investment into appropriate systems to fulfill the tracking and monitoring expectations for banking this industry, we entered it and have benefitted from that decision. We finished the year with over $13 million of deposits in this segment, and we see an opportunity for more client relationships in the future.

Another deposit generating strategy was expanding our branch footprint. In March, we opened our fourteenth location, this one in Lititz. Although our Grand Opening event plans were delayed by inclement spring weather, this office proved to be very successful in its first nine months. In fact, it is off to the best start of any office we have opened in the past ten years. During the course of the year, we generated over $11 million in new deposit business and added 254 new households. Opening the Lititz office filled in our branch network in northern Lancaster County between our existing Ephrata and Manheim locations. This market has been a focus for us and has helped contribute to our overall growth. In total, we now maintain active relationships with 27,811 clients with 45,378 accounts. This represents a 3.80% growth rate over the prior year.

SMILE Center

To support our client and employee growth, we relocated many of our support departments to a building located at 100 N. Harris St. in Cleona. We call this building our SMILE Center. Aside from our growth, this move was precipitated by three flooding events in our Cleona branch and operations building during the past dozen years which created an unacceptable business-interruption risk. Since moving into this leased space, we have realized greater synergy between work groups. Going forward, it will also house our training department designed to prepare our existing and future workforce to better deliver our signature *Bank on a Smile®* service.

Lending

Loan growth for the year finished at 2.90%. Although this growth rate was below our expectations, we experienced several large payoffs as the result of bond financings, the sale of completed projects, and finding solutions to problem credits. In fact, we booked over $160 million in loans during the year that

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after routine pay-downs and the special payoffs previously referenced, resulted in $14 million net growth. Our commercial and indirect lending businesses lead the way in loan generation.

Credit Quality

We continued to see improvement in our overall credit quality. Total delinquencies and non-accrual loans are at their lowest levels in two years. Our improvement is related to both increased management expertise and attention that we achieved through enhancement of our credit administration department and systematic movement through the credit cycle. The provision for loan losses during the year was $856,000 versus $1,450,000 in the prior year. This reduction was largely related to our limited loan growth.

Regulatory Relief

As an industry we experienced some well needed regulatory relief. In May, the president signed into law the Economic Growth, Regulatory Relief and Consumer Protection Act (S.2155). This carefully crafted Act includes common sense improvements to the nation's financial rules that will allow community banks, like ours, to better serve our clients and communities. It is an important first step in rolling back some of the overreaching regulations that strangled growth and that have been hurting consumers for the past 8 years. It will open doors for more creditworthy borrowers and businesses, and it will contribute to economic growth and job creation. After the final rules are written, we hope to see substantial improvements in lending regulations, capital rules, and required government reporting.

Stock Activity

There was a substantial increase in our stock activity in 2018. We traded a high of 114,087 shares for a total dollar volume of $2.97 million with an average price of $26.03. The number of shares traded represented a 26% increase versus the prior year and accounted for 4.73% of our outstanding shares. The 52 week high and low was $30.00 and $23.70 respectively.

In July, the Bank announced a common stock offering with intentions of issuing up to 233,010 new shares at a price of $25.75 for an aggregate of $6,000,000. The Board of Directors determined that market conditions were favorable to augment our capital position and support the Bank's continued growth projections. Existing shareholders enjoy pre-emptive rights, giving them the ability to purchase new shares before shares are open to new investors. The pre-emptive rights offering period ran from July 16 to September 14, and accounted for 22,707 new shares, raising equity of $584,705.25. After the pre-emptive rights period, we offered shares through a community offering. During the community offering, 47,557 shares were issued for $1,224,618.50. In total, we issued 70,264 shares to 116 investors and raised $1.80 million in new capital. Unfortunately, the stock market went through a fourth quarter correction and dampened the appetite of many investors for equity investments. So, although our timing could have been better, we were very encouraged by the participation and feedback we received relative to the offering from the communities we serve.

It was very evident that many in our community are supportive of the Bank and appreciative of what we do to economically support our markets. We remain in a strong capital position with total capital to risk weighted assets of 12.50%, compared to a regulatory guideline of 10% for well-capitalized institutions. We remind shareholders that they can participate in our dividend reinvestment and stock purchase plan on a quarterly basis as a convenient way to increase their JNES holdings.

Strength Through Independence

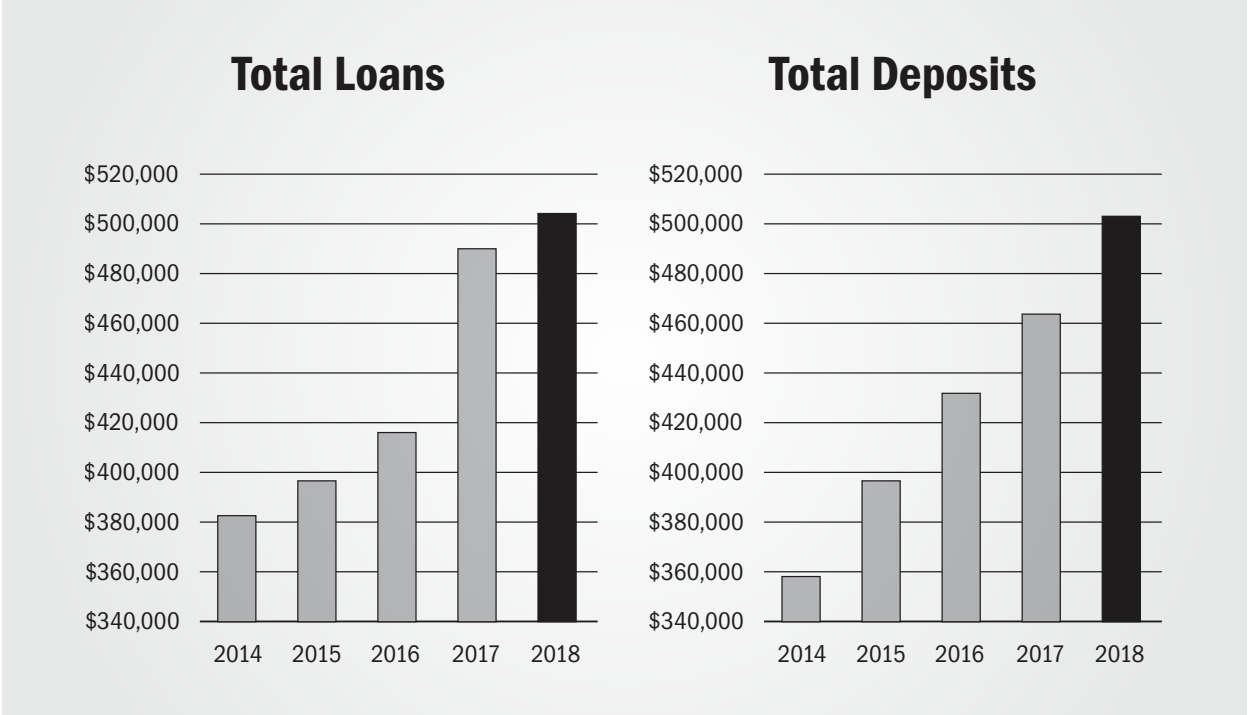
We continue to believe that there is a bright future ahead with many opportunities for JBT. The course that we have stayed true to for the past 146 years as an independent community bank is a differentiator for us now more than ever. We appreciate your business, investment, and support. We will continue to work hard every day to earn it. *Thank you!*

Richard J. Newmaster, Jr.
Chairman

Troy A. Peters
President
Chief Executive Officer

FINANCIAL HIGHLIGHTS

(Dollars in thousands, except per share amounts)	**2018**	2017	Change
Results of Operations			
Net interest income	**19,815**	17,954	10.4%
Provision for loan losses	**856**	1,450	-41.0%
Net income	**4,845**	4,487	8.0%
Per Share Data			
Basic earnings	**2.07**	1.93	7.3%
Book value	**22.36**	20.93	6.8%
Financial Condition at Year-end			
Assets	**588,729**	575,610	2.3%
Deposits	**502,452**	464,166	8.2%
Loans Receivable, net	**505,466**	491,231	2.9%
Allowance for loan loss	**5,855**	5,853	0.0%
Stockholders' equity	**53,903**	48,831	10.4%
Financial ratios			
Return on average assets	**0.84%**	0.83%	1.2%
Return on average equity	**9.62%**	9.49%	1.4%
Total capital to risk weighted assets	**12.50%**	11.88%	5.2%



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INDEPENDENT AUDITOR'S REPORT

Board of Directors and Shareholders
Jonestown Bank & Trust Co.

We have audited the accompanying financial statements of Jonestown Bank & Trust Co., which comprise the balance sheets as of December 31, 2018 and 2017, and the related statements of income, comprehensive income, stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of these 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 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 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Jonestown Bank & Trust Co. as of December 31, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

EFFECT OF ADOPTING NEW ACCOUNTING STANDARDS

As discussed in Note 1 to the financial statements, in 2018 the entity adopted new accounting guidance issued by the Financial Accounting Standards Board (FASB) related to revenue from contracts with customers, recognition and measurement of financial assets and liabilities, and the presentation of pension service costs.

Our opinion is not modified with respect to these matters.

Smith Elliott Kearns & Company, LLC

Chambersburg, Pennsylvania
February 26, 2019

Balance Sheets

(Dollars in thousands, except per share amounts)	December 31, 2018	December 31, 2017
ASSETS		
Cash and due from banks	$ 3,355	$ 2,769
Interest bearing deposits in other banks	10,519	10,528
Securities available for sale	40,565	41,747
Securities held to maturity, fair value of $844 and $853	843	851
Loans	511,321	497,084
Less allowance for loan losses	5,855	5,853
Net loans	505,466	491,231
Restricted investment in bank stock	1,734	2,965
Foreclosed assets	533	737
Premises and equipment	8,801	7,547
Investment in life insurance	12,734	12,450
Accrued interest receivable	1,817	1,641
Other assets	2,362	3,144
TOTAL ASSETS	$ 588,729	$ 575,610
LIABILITIES		
Deposits:		
Non-interest-bearing	50,145	48,267
Interest-bearing	452,307	415,899
Total deposits	502,452	464,166
Short-term debt	-	23,221
Long-term debt	26,420	33,704
Subordinated debt	3,000	3,000
Accrued interest payable and other liabilities	2,954	2,688
TOTAL LIABILITIES	$ 534,826	$ 526,779
STOCKHOLDERS' EQUITY		
Preferred stock, no par value; $1,000 per share liquidation preference; 4,000,000 shares authorized; no shares issued and outstanding	-	-
Common stock, par value $2.00; 6,000,000 shares authorized; issued and outstanding 2,411,064 and 2,332,566 on December 31, 2018 and December 31, 2017	4,822	4,665
Surplus	6,944	5,074
Retained earnings	43,206	40,046
Accumulated other comprehensive (loss)	(1,069)	(954)
TOTAL STOCKHOLDERS' EQUITY	$ 53,903	$ 48,831
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 588,729	$ 575,610

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

Statements of Income

(Dollars in thousands, except per share amounts)	Years Ended December 31, 2018	2017
INTEREST INCOME		
Loans receivables, including fees	$ 23,063	$ 19,700
Securities:		
Taxable	575	593
Tax-exempt	284	320
Other	376	226
Total interest income	$ 24,298	$ 20,839
INTEREST EXPENSE		
Deposits	3,503	1,926
Short-term borrowings	242	44
Interest on subordinated debt	165	165
Long-term debt	573	750
Total interest expense	$ 4,483	$ 2,885
NET INTEREST INCOME	19,815	17,954
Provision for loan losses	856	1,450
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	$ 18,959	$ 16,504
OTHER INCOME		
Trust income	337	425
Service charges on deposit accounts	2,097	1,925
Automated teller machine and internet banking fees	193	209
Mortgage banking activities	393	434
Earnings on investment in life insurance	285	383
Other	183	462
Total other income	$ 3,488	$ 3,838
OTHER EXPENSE		
Salaries and employee benefits	8,842	7,732
Outsourcing services	1,783	1,559
Occupancy	1,211	942
Equipment and data processing	631	508
Marketing	498	437
ATM processing fees	430	417
Pennsylvania bank shares tax	461	433
Federal deposit insurance assessment	311	329
Net (gain) loss on foreclosed assets	68	15
Other	2,433	2,021
Total other expense	$ 16,668	$ 14,393
Income before income taxes	5,779	5,949
Federal income taxes	934	1,462
NET INCOME	$ 4,845	$ 4,487
EARNINGS PER SHARE	$ 2.07	$ 1.93
WEIGHTED-AVERAGE SHARES OUTSTANDING	2,345,065	2,328,038

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

Statements of Comprehensive Income

(Dollars in thousands, except per share amounts)	Years Ended December 31, 2018	2017
Net Income	$ 4,845	$ 4,487
Unrealized gains (losses) on securities:		
Unrealized holding gains (losses) arising during the year	(240)	301
Reclassification adjustment for (gains) realized in net income	-	-
Tax effect	50	(102)
Net unrealized gains (losses) on securities	(190)	199
Defined benefit pension plan:		
Change in benefit obligations and plan assets	95	(47)
Tax effect	(20)	16
Net change in defined benefit pension plan	75	(31)
Other comprehensive income (loss)	(115)	168
Total comprehensive income	$ 4,730	$ 4,655

Statements of Stockholders' Equity

(Dollars in thousands, except per share amounts)	Years Ended December 31, 2018 and 2017				
	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2016	$ 4,645	4,877	$ 36,984	$ (965)	$ 45,541
Issuance of common stock through:					
Dividend reinvestment plan (9,887 shares)	20	197	-	-	217
Comprehensive income:					
Net income		-	4,487	-	4,487
Other comprehensive income, net of taxes	-	-	-	168	168
Adjustment due to tax rate change	-	-	157	(157)	-
Cash dividends declared ($.68 per share)	-	-	(1,582)	-	(1,582)
Balance, December 31, 2017	$ 4,665	$ 5,074	$ 40,046	$ (954)	$ 48,831
Issuance of common stock through:					
Dividend reinvestment plan (8,234 shares)	16	202	-	-	218
Common stock offering (70,264 shares)	141	1,668			1,809
Comprehensive income:					
Net income		-	4,845	-	4,845
Other comprehensive loss, net of taxes	-	-	-	(115)	(115)
Cash dividends declared ($.72 per share)	-	-	(1,685)	-	(1,685)
Balance, December 31, 2018	$ 4,822	$ 6,944	$ 43,206	$ (1,069)	$ 53,903

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

Statements of Cash Flows

(Dollars in thousands)	Years Ended December 31, 2018	2017
OPERATING ACTIVITIES		
Net income	$ 4,845	$ 4,487
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for loan losses	856	1,450
Provision for depreciation and amortization	608	514
Net amortization of securities premiums and discounts	334	397
Net amortization of deferred loan fees	(720)	(2,810)
Deferred income taxes	166	500
Loss on disposal of property and equipment	15	17
Loss on foreclosed assets	68	15
(Gain) on sale of loans, net	(272)	(315)
Proceeds from sales of loans	9,854	9,307
Loans originated for sale	(9,582)	(8,607)
Earnings on investment in Bank-owned life insurance, net	(285)	(283)
Increase (decrease) in accrued interest receivable and other assets	517	(424)
Increase (decrease) in accrued interest payable and other liabilities	223	(14)
Net cash provided by operating activities	6,627	4,234
INVESTING ACTIVITIES		
Proceeds from maturities and principal repayments		
Securities held to maturity	8	12
Securities available for sale	4,398	4,543
Purchase of securities available for sale	(3,788)	-
Net (increase) in loans	(15,246)	(74,110)
Redemption (purchase) of restricted bank stock	1,231	(1,455)
Purchase of premises and equipment	(1,786)	(3,911)
Proceeds from sale of foreclosed assets	1,010	899
Purchase of bank owned life insurance	-	(886)
Net cash used for investing activities	(14,173)	(74,908)
FINANCING ACTIVITIES		
Net increase in deposits	38,286	31,452
Net increase (decrease) in short-term borrowings	(23,221)	17,221
Proceeds from debt	-	25,000
Repayment of long term debt	(7,284)	(5,570)
Proceeds from the issuance of common stock	2,027	217
Dividends on common stock	(1,685)	(1,582)
Net cash provided by financing activities	8,123	66,738
Increase (decrease) in cash and cash equivalents	577	(3,936)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	13,297	17,233
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 13,874	$ 13,297
Cash paid during the year for:		
Interest	$ 4,451	$ 2,826
Taxes	350	1,265
Noncash investing transactions:		
Loans Transferred to Foreclosed Assets	$ 875	$ 1,267

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

1. Summary of Significant Accounting Policies

Nature of Operations

The Jonestown Bank & Trust Co. (the "Bank") operates under a state bank charter and provides full banking services, including trust services. As a state bank, the Bank is subject to regulation of the Pennsylvania Department of Banking and Securities and the Federal Deposit Insurance Corporation. The area served by the Bank is principally Lebanon County and northern Lancaster County, Pennsylvania.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, mortgage servicing rights, deferred tax valuation allowances, pension liability, and the determination of impairment of restricted investment in Bank stock and of other-than-temporary impairment of securities.

Presentation of Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks with original maturities of 90 days or less, if any.

Securities

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

Bonds, notes, and debentures for which the Bank has the positive intent and ability to hold to maturity are reported at cost, adjusted for premiums and discounts that are recognized in interest income using the interest method over the terms of the securities.

Management determines the appropriate classification of debt securities at the time of purchase and reevaluates such designation as of each Balance Sheet date.

Securities are evaluated on a periodic basis to determine whether a decline in their value is other than temporary. For debt securities, management considers whether the present value of cash flow expected to be collected is less than the security's amortized cost basis (the difference defined as the credit loss), the magnitude and duration of the decline, the reasons underlying the decline, and the Bank's intent to sell the security or whether it is more likely than not that the Bank would be required to sell the security before its anticipated recovery in market value, to determine whether the loss in value is other than temporary. Once a decline in value is determined to be other than temporary, if the Bank does not intend to sell the security, and it is more likely than not that it will not be required to sell the security before recovery of the security's amortized cost basis, the charge to earnings is limited to the amount of credit loss. Any remaining difference between fair value and amortized cost (the difference defined as the non-credit portion) is recognized in other comprehensive income, net of applicable taxes. Otherwise, the entire difference between fair value and amortized cost is charged to earnings.

1. Summary of Significant Accounting Policies (Continued)

Restricted Investments in Bank Stock

Restricted investments in bank stock, which represent required investments in the common stock of correspondent banks, are carried at cost and as of December 31, 2018 and 2017 consist of the common stock of the Federal Home Loan Bank ("FHLB") of Pittsburgh and Atlantic Community Bankers Bank ("ACBB"). Federal law requires a member institution of the FHLB to hold stock of its district FHLB according to a predetermined formula. As of December 31, 2018 and 2017, the recorded investment in restricted bank stock is $1,734,000 and $2,965,000, respectively.

Management evaluates the restricted stock for impairment at least annually, or more frequently, if necessary. Management's determination of whether these investments are impaired is based on their assessment of the ultimate recoverability of their cost rather than by recognizing temporary declines in value.

Loans Held for Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income. There were no loans held for sale at December 31, 2018 and no loans held for sale at December 31, 2017.

Mortgage loans held for sale are generally sold with the mortgage-servicing rights retained by the Bank; however, the Bank does sell some mortgage loans with servicing released. The carrying value of mortgage loans sold is reduced by the cost allocated to the associated mortgage-servicing rights. Gains or losses on sales of mortgage loans are recognized based on the difference between the selling price and the carrying value of the related mortgage loans sold.

Loans Receivable

The Bank grants mortgage, commercial, and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans throughout Lebanon County, Pennsylvania. The ability of the Bank's debtors to honor their contracts is dependent upon the real estate and general economic conditions in this area.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff generally are stated at their outstanding unpaid principal balances, net of any deferred fees or costs on originated loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the yield (interest income) of the related loans. The Bank is generally amortizing these amounts over the contractual life of the loan.

The accrual of interest for all loan segments, except for consumer loans, is discontinued when the contractual payment of principal or interest has become 90 days past due, unless the credit is well-secured and in the process of collection or management has serious doubts about further collectability of principal or interest, even though the loan is currently performing. Consumer loans are charged-off on or before they become 90 days past due. When a loan is placed on nonaccrual status, unpaid interest credited to income in the current year is reversed and unpaid interest accrued in prior years is charged against the allowance for loan losses. Interest received on nonaccrual loans generally is either applied against principal or reported as interest income, according to management's judgment as to the collectability of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time, and the ultimate collectability of the total contractual principal and interest is no longer in doubt. Loan delinquencies for all loan segments are determined based on contractual terms of the loans.

1. Summary of Significant Accounting Policies (Continued)

Loans Receivable (Continued)

The Bank segregates its loan portfolio into segments with varying risk characteristics. Commercial loans include loans to businesses for general commercial purposes and include permanent and short-term working capital, machinery and equipment financing, and may be either in the form of lines of credit, demand, or term loans. Some commercial and industrial loans may be unsecured to higher rated customers, but the majority of these loans are secured by the borrower's accounts receivable, inventory and machinery and equipment and in many loans, the collateral also includes the business real estate or the business owner's personal real estate or assets. Commercial loans have credit exposure since they are more susceptible to risk of loss during a downturn in the economy as borrowers may have greater difficulty in meeting their debt service requirements and the value of the collateral may decline.

Commercial real estate loans consist of owner occupied and non-owner occupied commercial real estate loans. Owner occupied commercial real estate loans are generally dependent upon the successful operation of the borrower's business, with the cash flows generated from the business being the primary source of repayment of the loan. If the business suffers a downturn in sales or profitability, the borrower's ability to repay the loan could be in jeopardy, which could increase the risk of loss. Non-owner occupied and multi-family commercial real estate loans and non-owner occupied residential loans are dependent on the borrower's ability to generate a sufficient level of occupancy to produce rental income that exceeds debt service requirements and operating expenses. Lower occupancy or lease rates may result in a reduction in cash flows, which may affect the ability of the borrower to meet debt service requirements, and may result in lower collateral values, which represents a higher inherent risk than owner-occupied commercial loans.

Commercial real estate construction loans consist of 1-4 family residential construction and commercial and land development loans. The risk of loss on these loans is contingent on the assessment of the property's value at the completion of the project, which should exceed the property's construction costs. A number of factors can negatively affect the project during the construction phase such as cost overruns, delays in completing the project, competition, and real estate market conditions which may change based on the supply of similar properties in the area. If the collateral value at the completion of the project is not sufficient to cover the outstanding loan balance, repayment of the loan would potentially need to rely on other repayment sources, including the guarantors of the project or other collateral securing the loan.

Residential real estate loans include fixed-rate and adjustable first lien mortgage loans with the underlying 1-4 family owner-occupied residential property securing the loan. Risk exposure is mitigated somewhat through the evaluation of the credit worthiness of the borrower, including credit scores and debt-to-income ratios, and limits on the loan-to-value ratios based on collateral values.

Home equity lines of credit represent a slightly higher risk than residential real estate first liens, as these loans can be first or second liens on residential family owner occupied residential property, but there are loan-to-value limits on the value of the real estate taken as collateral. The credit worthiness of the borrower is considered, including credit scores and debt-to-income ratios.

Consumer indirect automobile and other consumer loans' credit risk are mitigated through evaluation of the credit worthiness of the borrower through credit scores and debt-to-income ratios, and if secured, the collateral value of the assets. However, these loans can be unsecured or secured by assets that may depreciate quickly or may fluctuate and represent a greater risk than 1-4 family residential loans. Indirect automobile loans represent some risk as the initiation of the credit process begins with a consumer and dealer at the point of purchase with the Bank then approving or denying the credit based on the consumer's credit worthiness.

Allowance for Loan Losses

Management establishes the allowance for loan losses based upon its evaluation of the pertinent factors underlying the types and quality of loans in the portfolio. All commercial loans and commercial real estate loans are reviewed on a regular basis with a focus on larger loans along with loans which have experienced past payment or financial deficiencies. All commercial loans and commercial real estate loans which are 90 days or more past due are selected for impairment testing.

1. Summary of Significant Accounting Policies (Continued)

Allowance for Loan Losses (Continued)

These loans are analyzed to determine if they are "impaired," which means that it is probable that all amounts will not be collected according to the contractual terms of the loan agreement. All commercial loans that are delinquent 90 days and residential mortgage loans that are 120 days delinquent and are placed on nonaccrual status are evaluated for impairment on an individual basis. The remaining loans are evaluated for impairment as groups of loans with similar risk characteristics. The Bank allocates allowances based on the factors described below, which conform to the Bank's asset classification policy. In reviewing risk within the Bank's loan portfolio, management has determined there to be several different risk categories within the loan portfolio. The allowance for loan losses consists of amounts applicable to: (i) the commercial loan portfolio; (ii) the commercial real estate portfolio; (iii) the consumer loan portfolio (indirect and other); (iv) the loans secured by residential real estate portfolio; and (v) home equity lines of credit. Factors considered in this process include general loan terms, collateral, and availability of historical data to support the analysis. Historical loss percentages for each risk category are calculated and used as the basis for calculating allowance allocations based on the last twelve quarters of historical losses. Certain qualitative factors are then added to the historical allocation percentage to get the total factor to be applied to non-classified loans. The following qualitative factors are analyzed:

- Trends in delinquency
- Underlying loan collateral value factors
- Trends in risk ratings
- Economic trends
- Concentrations of credit risk
- Lending policies and procedures
- Quality of loan review
- External factors (competition, legal, regulatory)
- Experience, depth and ability of lending management/staff
- Nature and volume of the portfolio and terms of loans
- Special mention and substandard trends
- Factors unique to home equity lines of credit, indirect loans, education loans

The Bank analyzes its loan portfolio each quarter to determine the appropriateness of its allowance for loan losses. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for losses on loans. Such agencies 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. Because of these factors, management's estimate of credit losses inherent in the loan portfolio and the related allowance may change in the near term. However, the amount of the change that is reasonably possible cannot be estimated.

Loan Charge-off Policies

Consumer and residential real estate loans are generally fully or partially charged down to the fair value of collateral securing the asset when the loan is 120 days past due unless the loan is in the process of collection. On all other loans, the primary factors considered by management in determining charge-offs include payment status and collateral value but could also include debt service coverage, financial health of the borrower, and other external factors that could impact the ability of the borrower to repay the loan.

Servicing

Servicing assets are recognized as separate assets when rights are acquired through the sale of loans. Capitalized servicing rights are reported in other assets and are amortized as a reduction of noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans. Servicing assets are evaluated for impairment based upon the fair value of the rights as compared with amortized cost. Impairment is

1. Summary of Significant Accounting Policies (Continued)

Servicing (Continued)

determined by stratifying rights by predominant characteristics, such as interest rates and terms. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. Impairment is recognized through a valuation allowance for an individual stratum, to the extent that fair value is less than the capitalized amount for the stratum.

Foreclosed Assets

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value less cost to sell at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets. Residential real estate in the process of foreclosure was $717,000 and $752,000 at December 31, 2018 and 2017, respectively. Residential real estate held as other real estate owned and included in foreclosed assets on the balance sheets was $433,000 and $358,000 at December 31, 2018 and 2017, respectively. Commercial real estate held as other real estate was $0 and $196,000 at December 31, 2018 and 2017, respectively. Other foreclosed assets were $100,000 and $183,000 at December 31, 2018 and 2017, respectively.

Bank Premises and Equipment

Land is carried at cost. Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed principally on the straight-line method over the estimated useful lives of the related assets, ranging from 3 to 40 years.

Transfers of Financial Assets

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

Investment in Life Insurance

The Bank invests in split-dollar 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 chosen group of employees. The Bank is the owner and the Bank and employee's beneficiary are beneficiaries 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 is included in other income on the income statement. Some of the BOLI policies have a post-retirement death benefit. The liability for this benefit was $794,000 and $724,000 at December 31, 2018 and 2017, respectively. The expense related to the liability for future benefits of the Bank's split-dollar bank-owned life insurance was approximately $69,000 and $61,000 for the years ended December 31, 2018 and 2017, respectively.

Trust Assets

Assets held by the Bank in a fiduciary capacity for customers are not included in the financial statements, since such items are not assets of the Bank. Trust income is reported on the accrual method.

Income Taxes

Deferred taxes are provided on the liability method, whereby deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely

1. Summary of Significant Accounting Policies (Continued)

Income Taxes (Continued)

than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. The Bank follows generally accepted accounting principles, which provides guidance on accounting for uncertainty in income taxes recognized in a Bank's financial statements. The Bank's policy is to charge penalties and interest to income tax expense as incurred. The Bank's federal and state tax returns are subject to examination by the Internal Revenue Service and state tax authorities, generally for a period of three years after the returns are filed.

Revenue Recognition

On January 1, 2018 the company adopted ASU 2014-09 *Revenue from contract with customers* (topic 606). All of the Company's revenue from contracts with customers within the scope of ASC 606 is recognized within noninterest income in the statements of income. Consistent with ASC 606, noninterest income covered by this guidance is recognized as services are transferred to our customers in an amount that reflects the consideration we expect to be entitled to in exchange for those services. Adoption of ASC 606 did not result in a change to the accounting for any in-scope revenue streams.

Interest income – It Is generated from various sources, including loans outstanding and investments, and is recognized on an accrual basis according to loan agreements, securities contracts or other such written contracts. These revenues are outside the scope of ASC 606.

Trust Department Income - Consists of income earned from Investment & Trust Services, Estate Settlement Income and Investment Brokerage Income. The Company receives fees for Investment and Trust Services based on the market value of the assets managed. Investment & Trust accounts are assessed a quarterly fee charged to client accounts, tiered and based primarily on the market value. These fees are based on a fixed fee schedule. Estate income is received and recognized upon completion of estate settlement in accordance with the fixed fee schedule. Investment brokerage services are provided through a third-party service provider. The Company receives commissions from the provider monthly, based on customer activity and is recognized by the company monthly.

Service Charges on Deposit Accounts, Automated Teller Machine and Internet Banking Fees – The Company earns fees from its deposit customers for transaction-based, account maintenance, and overdraft services. Transaction-based fees, which include services such as ATM use fees, internet banking fees, stop payment charges, and ACH fees, are recognized at the time the transaction is executed as that is the point in time the Company fulfills the customer's request. Account maintenance fees, which relate primarily to monthly maintenance, are earned over the course of a month, representing the period over which the Company satisfies the performance obligation. Overdraft fees are recognized at the point in time that the overdraft occurs. Service charges on deposits are withdrawn from the customer's account balance.

Interchange Income – The Company earns interchange fees from debit/credit cardholder transactions conducted through the Discover payment network. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder.

Mortgage Banking Activity – Income consists of gains on mortgages sold to FHLB and servicing of sold loans. Income is recognized on the date of the sale. FHLB also pays a monthly fee to service the mortgages for them compensating the bank for collecting monthly payments on the loan and providing customer service on the loans.

Earnings on Investments in Life Insurance - Increases in the cash surrender value of life insurance are not within the scope of ASC 606.

Gain/Losses on Sales of OREO – The Company records a gain or loss on the sale of OREO when control of the property transfers to the buyer, which generally occurs at the time of an executed deed. If the Company finances

1. Summary of Significant Accounting Policies (Continued)

Revenue Recognition (Continued)

the sale of OREO to the buyer, the Company assesses whether the buyer is committed to perform their obligations under the contract and whether collectability of the transaction price is probable. Once these criteria are met, the OREO asset is derecognized and the gain or loss on the sale is recorded upon the transfer of control of the property to the buyer. In determining the gain or loss on the sale, the Company adjusts the transaction price and related gain (loss) on sale if a significant financing component is present.

Other – these are comprised primarily of merchant card fees, credit card fees, wire transfer fees, and rental of safe deposit boxes. Merchant card fees represent fees the Bank earns from a third party for enrolling a customer in the processor's program. Credit card fees represent a fee earned by the Bank for a successful referral to a card-issuing company. All of these fees are transaction based and are recognized at the time of the transaction except for safe deposit fees which are recorded annually as received for rental of the box for one year.

The following table presents our non-interest income disaggregated by revenue source. Overdraft fees on checking, other service charges on deposit accounts and interchange on deposit accounts are combined in the Statements of Income under service charges on deposit accounts.

(Dollars in 000s)	December 31, 2018	December 31, 2017
Trust income	$ 337	$ 425
Overdraft fees on checking	1,080	1017
Other service charges on deposit accounts	72	57
Interchange fees on debit card	945	851
Automated teller machine and internet banking fees	193	209
Mortgage banking activity	393	434
Earning on investments in life insurance	285	383
Other	183	462
	$ 3,488	$ 3,838

Advertising

Advertising costs are expensed as incurred. The Bank's expenditures on advertising were $498,000 and $437,000 for the years ended December 31, 2018 and 2017, respectively.

Off-Balance Sheet Financial Instruments

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

Earnings per Share

Basic earnings per share represent net income available to common shareholders divided by the weighted-average number of shares outstanding during the period. Dividends on preferred stock are deducted from net income in calculating earnings per common share.

Comprehensive Income

Accounting principles generally accepted in the United States of America require that recognized revenue, expenses, gains, and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities and unrecognized gains and losses, prior service costs, and transition assets or obligations for defined benefit pension plans are reported as a separate component of the equity section of the Balance Sheets, such items, along with net income, are components of comprehensive income.

1. Summary of Significant Accounting Policies (Continued)

Change in Accounting Principles

On December 22, 2017, the U.S. federal government enacted the "Tax Cuts and Jobs Act of 2017" (TCJA). As a result of the newly enacted tax laws and rates, in accordance with generally accepted accounting principles, the bank remeasured their future tax benefits and liabilities using the newly enacted tax rates. Generally accepted accounting principles requires that the effect of tax law and rate changes be recognized in income tax from continuing operations, even if the deferred tax asset or liability originally related to items recognized in Accumulated Other Comprehensive Income (AOCI). Because of this, the tax effects of items within AOCI do not reflect the appropriate tax rate. For additional information regarding the additional income tax expense recognized as a result of the remeasurement of the bank's net deferred tax asset, refer to Note 13.

On February 14, 2018, FASB finalized ASU 2018-02, "Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income" to allow reclassifying the effect of remeasuring deferred tax assets and liabilities related to items within accumulated other comprehensive income (AOCI) to retained earnings, effectively correcting the stranded tax effects created by the newly enacted tax rates. The Corporation elected to early adopt ASU 2018-02 in 2017 in order to properly reflect the effective tax rate within AOCI. This change in accounting principle caused the bank to reclassify $157,246 from AOCI to retained earnings during the year-ended December 31, 2017.

ASU 2014-09, Revenue from Contracts with Customers (Topic 606). ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. On January 1, 2018, the Company adopted ASU 2014-09 and all subsequent amendments (collectively "ASC 606"). The majority of the Company's revenue comes from interest income, including loans and securities that are outside the scope of ASC 606. The Company's services that fall within the scope of ASC 606 are presented within noninterest income on the statements of income and are recognized as revenue as the Company satisfies its obligation to the customer. Services within the scope of ASC 606 include service charges on deposit accounts, income from fiduciary investment management and brokerage activities and interchange fees from service charges on ATM and debit card transactions. ASC 606 was adopted using the retrospective method and did not result in a change to the accounting for any in-scope revenue streams; as such, no cumulative effect adjustment was recorded.

The Company adopted the provisions of the ASU 2017-07 on January 1, 2018 which deals with improving the presentation of the net periodic pension cost. This standard requires an employer to report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations. The amendments in this update also allow only the service cost component to be eligible for capitalization when applicable. The adoption of this standard had no material effect on the financial statements. The bank's pension plan is frozen so the service cost component of this standard does not apply to the bank.

The Company adopted the provisions of the ASU 2016-01 on January 1, 2018. This standard amends the guidance on the classification and measurement of financial instruments. Some of the amendments include the following: 1) requires equity investments to be measured at fair value with changes in fair value recognized in net income; 2) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; 3) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. The adoption of this standard had no material impact on the financial statements. The bank has no equity investments that need to be measured at fair value. Fair value of financial instruments are measured using the exit price notion.

1. Summary of Significant Accounting Policies (Continued)

Accumulated other Comprehensive Income (Loss)

The components of accumulated other comprehensive income (loss) and related tax effects are presented in the following table:

(Dollars in 000s)

	Unrealized Gains\(losses) on Securities	Defined Benefit Pension Plan	Total
Balance, December 31, 2016	$ (250)	$ (715)	$ (965)
Change in urealized losses on securities available for sale	301	-	301
Change in benefit obligation and plan assets	-	(47)	(47)
Tax effect of current period changes	(102)	16	(86)
Adjustment due to tax rate change	(10)	(147)	(157)
Balance, December 31, 2017	$ (61)	$ (893)	$ (954)
Change in urealized losses on securities available for sale	$ (240)	$ -	(240)
Change in benefit obligation and plan assets	-	95	95
Tax effect of current period changes	50	(20)	30
Balance, December 31, 2018	$ (251)	$ (818)	$ (1,069)

2. Restrictions on Cash and Due from Bank Balances

The Bank is required to maintain cash reserve balances with the Federal Reserve Bank. The required reserve balances were $ 627,000 at December 31, 2018 and $423,000 at December 31, 2017. The Bank maintains balances with its correspondent banks that may exceed federal insured limits, which management considers a normal business risk.

3. Securities

The amortized cost and fair value of securities are presented in the following tables:

December 31, 2018 *(Dollars in 000s)*	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
Certificates of deposit	$ 2,629	$ -	$ (26)	$ 2,603
Obligations of states and political subdivisions	11,148	48	(77)	11,119
Mortgage-backed securities in government-sponsored entities	27,105	119	(381)	26,843
Total	$ 40,882	$ 167	$ (484)	$ 40,565
Held-to-maturity securities:				
Mortgage-backed securities in government-sponsored entities	$ 43	$ 1	$ -	$ 44
Investment note receivable	800	-	-	800
Total	$ 843	$ 1	$ -	$ 844

3. Securities (Continued)

December 31, 2017 (Dollars in 000s)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
U.S. government agencies	$ 1,000	$ -	$ -	$ 1,000
Certificates of deposit	2,629	5	-	2,634
Obligations of states and political subdivisions	11,816	117	(35)	11,898
Mortgage-backed securities in government-sponsored entities	26,380	90	(255)	26,215
Total	$ 41,825	$ 212	$ (290)	$ 41,747
Held-to-maturity securities:				
Mortgage-backed securities in government-sponsored entities	$ 51	$ 2	$ -	$ 53
Investment note receivable	800	-	-	800
Total	$ 851	$ 2	$ -	$ 853

Securities with a fair value of $12,957,000 and $10,345,000 at December 31, 2018 and 2017, respectively, were pledged to secure public deposits and for other purposes as required or permitted by law. No securities were sold in 2018 or 2017.

The amortized cost and fair value of securities by contractual maturity are shown in the following table. Expected maturities may differ from contractual maturities because borrowers may have the right to prepay obligations with or without call or prepayment penalties.

December 31, 2018	Available for Sale		Held to Maturity	
(Dollars in 000s)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 2,218	$ 2,225	$ -	$ -
Due after one year through five years	2,824	2,814	400	400
Due after five years through ten years	3,254	3,241	400	400
Due after ten years	5,481	5,443	-	-
Mortgage-backed securities in government-sponsored entities	27,105	26,842	43	44
Total	$ 40,882	$ 40,565	$ 843	$ 844

3. Securities (Continued)

The following table shows the gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2018 and 2017:

December 31, 2018	Less Than Twelve Months		Twelve Months or Greater		Total	
(Dollars in 000s)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-sale securities:						
Certificates of deposit	$ 2,603	$ (26)	$ -	$ -	$ 2,603	$ (26)
Obligations of states and political subdivisions	2,899	(12)	3,872	(65)	6,771	(77)
Mortgage-backed securities in government-sponsored entites	2,986	(26)	17,101	(355)	20,087	(381)
Total	$ 8,488	$ (64)	$ 20,973	$ (420)	$ 29,461	$ (484)

December 31, 2017	Less Than Twelve Months		Twelve Months or Greater		Total	
(Dollars in 000s)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-sale securities:						
Obligations of states and political subdivisions	$ 2,342	$ (6)	$ 2,210	$ (29)	$ 4,552	$ (35)
Mortgage-backed securities in government-sponsored entites	12,919	(109)	5,562	(146)	18,481	(255)
Total	$ 15,261	$ (115)	$ 7,772	$ (175)	$ 23,033	$ (290)

In management's opinion, the unrealized losses reflect changes in interest rates subsequent to the acquisition of specific securities. At December 31, 2018, the Bank had 51 securities in a loss position and Management believes that the unrealized losses are temporary and the Bank: (a) does not have the intent to sell any of the debt securities prior to recovery; and (b) it is more likely than not that it will not have to sell any of the debt securities prior to recovery. In addition, management feels that these losses are the result of interest rate changes that are not expected to result in the non-collection of principal and interest during the period.

At December 31, 2017, the Bank had 31 securities in a loss position.

The Bank's investments are exposed to various risks, such as interest rate, market, currency and credit risks. Due to the level of risk associated with certain investments and the level of uncertainty related to the changes in the value of the investments, it is at least reasonably possible that charges in risks in the near term would materially affect investment assets reported in the financial statements.

4. Loans Receivable

Loans receivable consist of the following:

(Dollars in 000s)	December 31, 2018	2017
Commercial	$ 47,579	$ 57,542
Commercial real estate	119,943	96,644
Commercial real estate construction	6,226	10,145
Secured by residential real estate	142,490	143,079
Home equity lines of credit	57,942	63,507
Consumer - indirect automobile financing	121,803	106,882
Consumer - other	15,338	19,285
Gross loans	511,321	497,084
Less allowance for loan losses	(5,855)	(5,853)
Net loans	$ 505,466	$ 491,231

Net deferred costs included in the table above total $5,149,000 and $4,429,000 as of December 31, 2018 and 2017, respectively.

5. Allowance for Loan Losses

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 Bank has segmented certain loans in the portfolio by product type. Loans are segmented into the following pools: commercial loans, commercial real estate loans, residential real estate loans, home equity lines of credit, 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 three-year period for all loan segments. The following qualitative factors are analyzed for the loan portfolio:

- Trends in delinquency
- Underlying loan collateral value factors
- Trends in risk ratings
- Economic trends
- Concentrations of credit risk
- Lending policies and procedures
- Quality of loan review
- External factors (competition, legal, regulatory)
- Experience, depth and ability of lending management/staff
- Nature and volume of the portfolio and terms of loans
- Special mention and substandard trends
- Factors unique to home equity lines of credit, indirect loans, education loans

These qualitative factors are reviewed each quarter and adjusted based upon relevant changes within the portfolio. Historical loss percentages are calculated over a three-year period for all loan segments.

Two qualitative factors comprise 62% of the qualitative reserves for both 2017 and 2018, the economic risk based on unemployment statistics and trends in delinquencies in our loan portfolio. The loan growth qualitative factor resulted in a reduction in the reserve of $249,000 for 2018 because of the slow loan growth in 2018 compared to strong loan growth in 2017. Additional qualitative factors were added in 2018 related to indirect loans and educational loans. Because of the rapid growth of the indirect loans in 2016 and 2017 the historical charge-off numbers were skewed downward so this factor was added which increased the reserve by $73,000.

5. Allowance for Loan Losses (Continued)

The insurance company guaranteeing the educational loans became insolvent in 2018 so a qualitative factor was added for this resulting in an increase of $98,000 in the reserve.

Loans by Segment

The total allowance reflects management's estimate of loan losses inherent in the loan portfolio at the Balance Sheet date. The Bank considers the allowance for loan losses of $5,855,000 adequate to cover loan losses inherent in the loan portfolio at December 31, 2018. The following table presents, by portfolio segment, the allowance for loan losses for the years ended December 31:

As of December 31, 2018								
(Dollars in 000s)	Commercial	Commercial Real Estate	Secured by Residential Real Estate	Home Equity Lines of Credit	Consumer - Indirect Automobiles	Consumer Other	Not allocated	Total
Allowance for credit losses:								
Beginning Balance	$ 558	$ 1,109	$ 1,290	$ 768	$ 1,805	$ 292	$ 31	$ 5,853
Charge-offs	(7)	(2)	(161)	(23)	(804)	(208)	-	$ (1,205)
Recoveries	61	16	12	1	217	44	-	$ 351
Provision	(88)	13	134	(118)	599	347	(31)	$ 856
Ending Balance	$ 524	$ 1,136	$ 1,275	$ 628	$ 1,817	$ 475	$ -	$ 5,855
Ending balance: individually evaluated for impairment	$ 117	$ -	$ 38	$ 2	$ 34	$ 14	$ -	$ 205
Ending balance: collectively evaluated for impairment	$ 407	$ 1,136	$ 1,237	$ 626	$ 1,783	$ 461	$ -	$ 5,650
Financing receivables:								
Ending balance, net of fees	$ 47,579	$ 126,169	$ 142,490	$ 57,942	$ 121,803	$ 15,338		$ 511,321
Ending balance: individually evaluated for impairment	$ 884	$ 3,579	$ 3,724	$ 195	$ 99	$ 86		$ 8,567
Ending balance: collectively evaluated for impairment	$ 46,695	$ 122,590	$ 138,766	$ 57,747	$ 121,704	$ 15,252		$ 502,754

5. Allowance for Loan Losses (Continued)

Loans by Segment (Continued)

As of December 31, 2017								
(Dollars in 000s)	Commercial	Commercial Real Estate	Secured by Residential Real Estate	Home Equity Lines of Credit	Consumer - Indirect Automobiles	Consumer Other	Not allocated	Total
Allowance for credit losses:								
Beginning Balance	$ 571	$ 858	$ 1,460	$ 723	$ 1,123	$ 271	$ 32	$ 5,038
Charge-offs	(32)	(14)	(104)	(62)	(583)	(213)	-	$ (1,008)
Recoveries	2	10	97	1	211	52	-	$ 373
Provision	17	255	(163)	106	1,054	182	(1)	$ 1,450
Ending Balance	$ 558	$ 1,109	$ 1,290	$ 768	$ 1,805	$ 292	$ 31	$ 5,853
Ending balance: individually evaluated for impairment	$ 5	$ 6	$ 55	$ 24	$ 55	$ 4	$ -	$ 149
Ending balance: collectively evaluated for impairment	$ 553	$ 1,103	$ 1,235	$ 744	$ 1,750	$ 288	$ 31	$ 5,704
Financing receivables:								
Ending balance, net of fees	$ 57,542	$ 106,789	$ 143,079	$ 63,507	$ 106,882	$ 19,285		$ 497,084
Ending balance: individually evaluated for impairment	$ 159	$ 5,094	$ 2,664	$ 285	$ 164	$ 30		$ 8,396
Ending balance: collectively evaluated for impairment	$ 57,383	$ 101,695	$ 140,415	$ 63,222	$ 106,718	$ 19,255		$ 488,688

Credit Quality Information

The following tables represent credit exposures by internally assigned grades for the years ended December 31, 2018 and 2017. The grading analysis estimates the capability of the borrower to repay the contractual obligations of the loan agreements as scheduled or at all. The Bank's internal credit risk grading system is based on definitions determined by the Bank.

The Bank's internally assigned grades are as follows:

Pass – loans which 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 where a potential weakness or risk exists, which could cause a more serious problem if not corrected.

Substandard – loans that 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 classified as doubtful 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 classified as a loss are considered uncollectible, or of such value that continuance as an asset is not warranted.

5. Allowance for Loan Losses (Continued)

Credit Quality Information (Continued)

As of December 31, 2018

(Dollars in 000s)	Commercial	Commercial Real Estate	Commercial Real Estate Construction
Pass	$ 43,975	$ 116,444	$ 5,208
Special Mention	661	1,054	-
Substandard	2,943	2,445	1,018
Doubtful	-	-	-
Loss	-	-	-
Ending Balance	$ 47,579	$ 119,943	$ 6,226

As of December 31, 2017

(Dollars in 000s)	Commercial	Commercial Real Estate	Commercial Real Estate Construction
Pass	$ 53,746	$ 89,995	$ 7,519
Special Mention	979	2,615	-
Substandard	2,817	4,034	2,626
Doubtful	-	-	-
Loss	-	-	-
Ending Balance	$ 57,542	$ 96,644	$ 10,145

The following tables present performing and nonperforming residential real estate and consumer loans based on payment activity for the year ended December 31, 2018 and 2017. 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, but do not include non-accrual loans less than 90 days past due. For more information on non-accrual loans see the section on non-accrual loans later in this footnote.

As of December 31, 2018

(Dollars in 000s)	Secured by Residential Real Estate	Home Equity Lines of Credit	Indirect Automobile Financing	Other Consumer Loans
Performing	$ 141,523	$ 57,612	$ 121,754	$ 15,335
Nonperforming	967	330	49	3
Total	$ 142,490	$ 57,942	$ 121,803	$ 15,338

5. Allowance for Loan Losses (Continued)

Credit Quality Information (Continued)

As of December 31, 2017				
(Dollars in 000s)	Secured by Residential Real Estate	Home Equity Lines of Credit	Indirect Automobile Financing	Other Consumer Loans
Performing	$ 141,234	$ 62,979	$ 106,833	$ 19,282
Nonperforming	1,845	528	49	3
Total	$ 143,079	$ 63,507	$ 106,882	$ 19,285

Following is a table which includes an aging analysis of the recorded investment of past due financing receivables:

As of December 31, 2018							
(Dollars in 000s)	30-59 Days Past Due	60-89 Days Past Due	90 Days Or Greater	Total Past Due	Current	Total Financing Receivables	> 90 Days and Accruing
Commercial	$ 42	$ 78	$ 50	$ 170	$ 47,409	$ 47,579	$ -
Commercial real estate	418	116	668	1,202	118,741	119,943	-
Commercial real estate construction	-	-	-	-	6,226	6,226	-
Secured by residential real estate	1,915	234	967	3,116	139,374	142,490	
Home equity lines of credit	622	180	330	1,132	56,810	57,942	-
Consumer - indirect automobile financing	1,430	162	49	1,641	120,162	121,803	49
Consumer - other	164	22	3	189	15,149	15,338	3
Total	$ 4,591	$ 792	$ 2,067	$ 7,450	$ 503,871	$ 511,321	$ 52

As of December 31, 2017							
(Dollars in 000s)	30-59 Days Past Due	60-89 Days Past Due	90 Days Or Greater	Total Past Due	Current	Total Financing Receivables	> 90 Days and Accruing
Commercial	$ 39	$ 113	$ -	$ 152	$ 57,390	$ 57,542	$ -
Commercial real estate	450	-	597	1,047	95,597	96,644	-
Commercial real estate construction	-	-	-	-	10,145	10,145	-
Secured by residential real estate	2,754	55	1,845	4,654	138,425	143,079	
Home equity lines of credit	282	135	528	945	62,562	63,507	-
Consumer - indirect automobile financing	1,289	149	49	1,487	105,395	106,882	49
Consumer - other	134	35	3	172	19,113	19,285	3
Total	$ 4,948	$ 487	$ 3,022	$ 8,457	$ 488,627	$ 497,084	$ 52

5. Allowance for Loan Losses (Continued)

Impaired Loans

Management considers commercial loans and commercial real estate loans which are 90 days or more past due to be impaired along with loans that are not expected to be collected as per the original loan contract. Larger commercial loans and commercial real estate loans which are 90 days or more past due are selected for impairment testing in accordance with GAAP. All substandard and doubtful loans are reviewed to determine if the loan is impaired. These loans are analyzed to determine if 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 table includes the recorded investment and unpaid principal balances for impaired financing receivables with the associated allowance amount, if applicable

As of and for the year ended December 31, 2018					
(Dollars in 000s)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial	$ 707	$ 714	$ -	$ 717	$ 9
Commercial real estate	2,811	3,593	-	2,995	40
Commercial real estate construction	768	1,432	-	771	38
Secured by residential real estate	3,413	3,677	-	3,488	64
Home equity lines of credit	178	178	-	178	5
Consumer - indirect auto	5	5	-	8	1
Consumer - other	45	45	-	47	1
Subtotal	$ 7,927	$ 9,644	$ -	$ 8,204	$ 158
With an allowance recorded:					
Commercial	$ 177	$ 177	$ 117	$ 179	$ 1
Commercial real estate	-		-		-
Secured by residential real estate	311	311	38	318	13
Home equity lines of credit	17	28	2	26	-
Consumer - indirect auto	94	94	34	104	7
Consumer - other	41	41	14	44	2
Subtotal	$ 640	$ 651	$ 205	$ 671	$ 23
Total Impaired:					
Commercial	$ 884	$ 891	$ 117	$ 896	$ 10
Commercial real estate	2,811	3,593	-	2,995	40
Commercial real estate construction	768	1,432	-	771	38
Secured by residential real estate	3,724	3,988	38	3,806	77
Home equity lines of credit	195	206	2	204	5
Consumer - indirect auto	99	99	34	112	8
Consumer - other	86	86	14	91	3
Total	$ 8,567	$ 10,295	$ 205	$ 8,875	$ 181

5. Allowance for Loan Losses (Continued)

Impaired Loans (Continued)

As of and for the year ended December 31, 2017					
(Dollars in 000s)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial	$ 154	$ 158	$ -	$ 154	$ 5
Commercial real estate	3,867	4,773	-	4,012	38
Commercial real estate construction	1,106	1,106	-	1,645	64
Secured by residential real estate	2,255	2,395	-	2,338	37
Home equity lines of credit	256	256	-	259	11
Consumer - indirect auto	14	14	-	19	2
Consumer - other	17	17	-	18	1
Subtotal	$ 7,669	$ 8,719	$ -	$ 8,445	$ 158
With an allowance recorded:					
Commercial	$ 5	$ 5	$ 5	$ 5	$ -
Commercial real estate	121	121	6	133	8
Secured by residential real estate	409	417	55	421	15
	29	30	24	31	-
Consumer - indirect auto	150	150	55	168	11
Consumer - other	13	13	4	16	1
Subtotal	$ 727	$ 736	$ 149	$ 774	$ 35
Total Impaired:					
Commercial	$ 159	$ 163	$ 5	$ 159	$ 5
Commercial real estate	3,988	4,894	6	4,145	46
Commercial real estate construction	1,106	1,106	-	1,645	64
Secured by residential real estate	2,664	2,812	55	2,759	52
Home equity lines of credit	285	286	24	290	11
Consumer - indirect auto	164	164	55	187	13
Consumer - other	30	30	4	34	2
Total	$ 8,396	$ 9,455	$ 149	$ 9,219	$ 193

5. Allowance for Loan Losses (Continued)

Nonaccrual Loans

All loans except for consumer loans are place on non-accrual once the loan becomes 90 days past due. Consumer loans are generally charged-off on or before 90 days past due. A nonaccrual loan will generally only be placed back on accrual status after the borrower has become current and has demonstrated six consecutive months of non-delinquency. When a loan is placed in nonaccrual status, previously accrued but unpaid interest is deducted from interest income.

On the following table are the financing receivables on nonaccrual status as of December 31, 2018 and 2017. The balances are presented by class of financing receivable.

(Dollars in 000s)	As of December 31, 2018	As of December 31, 2017
Commercial	$ 242	$ 36
Commercial real estate	2,023	2,733
Secured by residential real estate	1,961	2,283
Home equity lines of credit	566	689
Consumer - other	-	-
Total	$ 4,792	$ 5,741

Troubled Debt Restructurings

In situations where, for economic or legal reasons related to a borrower's financial difficulties, management may grant a concession for other than an insignificant period of time to the borrower that would not otherwise be considered, the related loan is classified as a Troubled Debt Restructuring ("TDR"). Management strives to identify borrowers in financial difficulty early and work with them to modify more affordable terms before their loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. In cases where borrowers are granted new terms that provide for a reduction of either interest or principal, management measures any impairment on the restructuring by calculating the present value of the revised loan terms and comparing this balance to the Company's investment in the loan prior to the restructuring. As these loans are individually evaluated for impairment, they are excluded from pooled portfolios when calculating the allowance for loan and lease losses and a separate allocation within the allowance for loan and lease losses is provided. Management continually evaluates loans that are considered TDRs, including payment history under the modified loan terms, the borrower's ability to continue to repay the loan based on continued evaluation of their operating results, and cash flows from operations.

Loan modifications that are considered TDRs completed during the years ended December 31, 2018 and 2017, were as follows:

(Dollars in 000s)	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
2018			
Troubled debt restructurings:			
Secured by residential real estate	8	$ 1,477	$ 1,477
Consumer - indirect automobile financing	1	30	30
Consumer - other	2	67	67
Total	11	$ 1,574	$ 1,574

5. Allowance for Loan Losses (Continued)

Troubled Debt Restructurings (Continued)

(Dollars in 000s)	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
2017			
Troubled debt restructurings:			
Commercial real estate	1	$ 1,252	$ 1,252
Consumer - indirect automobile financing	1	26	26
Total	2	$ 1,278	$ 1,278

All of the TDRs are performing and are in compliance with their modified terms and there were no commitments to lend more funds to these borrowers. The restructuring of the majority of loans for both 2018 and 2017 was either an extension of the maturity date or temporary reduction or moratorium on the payment terms or amounts. No modifications involved any changes in principal balances for 2018 or 2017.

6. Mortgage Servicing

The Bank entered into agreements to sell residential mortgages to the FHLB of Pittsburgh. The agreements include a maximum credit enhancement of $515,000 which the Bank may be required to pay if realized losses on any of the sold mortgages exceed the amount held in the FHLB's Spread Account. The FHLB is funding the Spread Account at 0.04 percent of the outstanding balance of loans sold annually. The Bank's historical losses on residential mortgages have been lower than the amount that will be funded to the Spread Account. Therefore, the Bank does not anticipate paying a credit enhancement and has not recorded a liability for the credit enhancement. As compensation for the credit enhancement, the FHLB is paying the Bank 0.10 percent of the outstanding loan balance in the portfolio on a monthly basis.

Loans serviced for others are not included in the accompanying balance sheets. The unpaid principal balances of mortgage loans serviced for others were $77,461,000 and $78,501,000 at December 31, 2018 and 2017, respectively.

The Bank retains the servicing on certain loans sold to the FHLB and receives a fee based upon the principal balance outstanding. The balance of mortgage servicing rights included in other assets on the balance sheets was $215,000 and $234,000 at December 31, 2018 and 2017. Mortgage servicing fee income for the years ended December 31, 2018 and 2017 was $121,000 and $119,000, respectively, which is included in mortgage banking activities in the statements of income.

The following summarizes mortgage servicing rights capitalized and amortized:

(Dollars in 000s)	Years Ended December 31, 2018	2017
Beginning Balance	$ 234	$ 261
Mortgage servicing rights capitalized	71	72
Mortgage servicing rights amortized	(90)	(99)
Ending balance	$ 215	$ 234

7. Bank Premises and Equipment

Components of Bank premises and equipment are as follows:

(Dollars in 000s)	December 31, 2018	December 31, 2017
Land and improvements	$ 1,978	$ 1,978
Buildings	8,634	6,588
Furniture and equipment	3,560	2,775
Contruction in progress	-	1,141
Total premises and equipment	$ 14,172	$ 12,482
Less accumulated depreciation	(5,371)	(4,935)
Net premises and equipment	$ 8,801	$ 7,547

Depreciation expense for the years ended December 31, 2018 and 2017 was approximately $519,000 and $409,000, respectively.

The Bank leases land and office space under operating leases. Rental expense, including property fees, for these leases was $387000 and $325,000 for years ended December 31, 2018 and 2017 respectively. Future minimum rental commitments under these leases are as follows:

(Dollars in 000s)	Years Ending December 31,
2019	$ 351
2020	358
2021	363
2022	368
2023	372
Thereafter	2,098
Total	$ 3,910

8. Deposits

The composition of deposits is as follows:

(Dollars in 000s)	December 31, 2018	December 31, 2017
Demand, non-interest-bearing	$ 50,145	$ 48,267
Checking with interest and money market	236,247	208,461
Savings	46,834	47,130
Time deposits greater than $250,000	21,659	22,532
Other time deposits	147,567	137,776
Total	$ 502,452	$ 464,166

8. Deposits (Continued)

At December 31, 2018, the scheduled maturities of time deposits are as follows:

(Dollars in 000s)	Years Ended December 31,
2019	$ 85,286
2020	49,526
2021	15,586
2022	13,539
2023	5,289
Total	$ 169,226

9. Employee Benefits

The Bank has a defined contribution 401(k) plan for employees who meet the eligibility requirements set forth in the plan. All of the Bank's employees that are 21 years and older are eligible for the plan. The Bank increased its match in 2013 to 100% of elective contributions of employees not to exceed 4% of the employee's salary, plus 50% of the employees elective contribution that exceed 4% of their salary but not to exceed 6% of their salary. The Bank's contributions to this plan were $255,000 in 2018 and $223,000 in 2017.

The Bank has a noncontributory defined benefit pension plan (the "Plan") covering substantially all employees hired prior to February 1, 2006. The Plan's benefit formulas generally base payments to retired employees upon their length of service and the employees' average monthly compensation. This plan was frozen as of December 31, 2012 and no employees are accruing any more benefits.

The following table sets forth the Plan's funded status and the amounts recognized in the Bank's financial statements. The measurement date for purposes of these valuations was December 31, 2018 and 2017.

(Dollars in 000s)	December 31, 2018	December 31, 2017
Change in benefit obligation		
Benefit obligation at beginning of year	$ 4,200	$ 3,823
Interest cost	149	156
Actuarial (gain) loss	(388)	407
Benefits paid	(85)	(83)
Settlements	(359)	(103)
Benefit obligation at end of year	3,517	4,200
Change in plan assets		
Fair value of plan assets at beginning of year	4,000	3,635
Employer contribution	-	-
Actual return on plan assets	(204)	551
Benefits paid	(85)	(83)
Settlements	(359)	(103)
Fair value of plan assets at end of year	3,352	4,000
Funded status (Included in other liabilities)	$ (165)	$ (200)
Amounts recognized in accumulated other comprehensive income (loss) consist of:		
Net actuarial loss	$ (1,036)	$ (1,131)
Deferred tax benefit	218	238
Total	$ (818)	$ (893)

9. Employee Benefits (Continued)

Net periodic pension expense included the following components:

(Dollars in 000s)	Years Ended December 31, 2018	2017
Interest cost	$ 149	$ 156
Expected return on plan assets	(256)	(251)
Settlement Charge	105	-
Net amortization and deferral	62	60
Net periodic pension expense	$ 60	$ (35)

The components of net periodic benefit cost are included in salaries and employee benefits in the Statements of Income.

The accumulated benefit obligation was $3,517,000 and $4,200,000 at December 31, 2018 and 2017 respectively.

The following is a summary of actuarial assumptions used for the Bank's pension plan:

	December 31, 2018	2017
Discount rate	4.22%	3.60%
Expected long-term return on Plan assets	6.00%	6.50%
Rate of compensation increase	N/A	N/A

The estimated net actuarial loss that will be amortized into net periodic pension cost over the next year is $62,000.

The selected long-term rate of return on Plan assets (6.5 percent) was primarily based on the asset allocation of the Plan's assets. Analysis of the historic returns on these asset classes and projections of expected future returns were considered in setting the long-term rate of return.

The Bank's pension plan target asset allocations, by asset category, are as follows:

	December 31, 2018	2017
Equities	65%	65%
Fixed income	35%	35%
Other	0%	0%
Total	100%	100%

9. Employee Benefits (Continued)

The following table sets forth by level, within the fair value hierarchy, the Plan's assets at fair value:

	As of December 31, 2018			
(Dollars in 000s)	Level I	Level II	Level III	Total
Assets:				
Mutual funds:				
Equities				
Large-Cap Value	$ 198	$ -	$ -	$ 198
Large-Cap Core	269	-	-	269
Mid-Cap Core	221	-	-	221
Small-Cap Core	98	-	-	98
International Core	471	-	-	471
Large Cap Growth	411	-	-	411
Small/midcap Growth	120	-	-	120
Fixed income				
Fixed Income- US Core	972	-	-	972
Intermediate Duration	326	-	-	326
Other	-	209	-	209
Cash Equivalent	57	-	-	57
Total assets at fair value	$ 3,143	$ 209	$ -	$ 3,352

	As of December 31, 2017			
(Dollars in 000s)	Level I	Level II	Level III	Total
Assets:				
Mutual funds:				
Equities				
Large-Cap Value	$ 249	$ -	$ -	$ 249
Large-Cap Core	336	-	-	336
Mid-Cap Core	291	-	-	291
Small-Cap Core	138	-	-	138
International Core	658	-	-	658
Large Cap Growth	529	-	-	529
Small/midcap Growth	154	-	-	154
Fixed income				
Fixed Income- US Core	1,012	-	-	1,012
Intermediate Duration	342	-	-	342
Other	-	254	-	254
Cash Equivalent	37	-	-	37
Total assets at fair value	$ 3,746	$ 254	$ -	$ 4,000

9. Employee Benefits (Continued)

The Bank does not expect to contribute to its pension plan in 2019.

The following benefit payments are expected to be paid:

(Dollars in 000s)	Years Ended December 31,
2019	$ 110
2020	123
2021	141
2022	155
2023	166
2024 through 2028	978
	$ 1,673

10. Borrowed Funds

The Bank has available a $25 million line with the FHLB of Pittsburgh. This line expires in May 2019. The interest rate on this line was 2.62 percent at December 31, 2018, and 1.54 percent at December 31, 2017. The outstanding balance under this line as of December 31, 2018 and 2017 was $ 0 and $23,221,000 respectively. The Bank also has an unsecured $3 million line with the Atlantic Community Bankers Bank (ACBB), which was not used in 2018 or 2017. The Bank also entered into unsecured subordinated debt with ACBB in 2015, maturing in November 2025, at a fixed rate of 5.5% for five years and then a variable rate based on prime rate plus 0.50% for the last five years. The debt can be redeemed after November 2020.

Long-term debt is composed of the following FHLB fixed-rate advances and ACBB subordinated debt:

(Dollars in 000s)			December 31,	
Maturity Date		Rate	2018	2017
July 2018	(Non-amortizing)	1.81	$ -	$ 7,000
June 2019	(Non-amortizing)	1.68	2,000	2,000
Dec 2019	(Non-amortizing)	1.77	10,000	10,000
June 2020	(Non-amortizing)	1.84	10,000	10,000
June 2021	(Non-amortizing)	1.97	3,000	3,000
May 2023	(Amortizing)	4.57	920	1,105
May 2023	(Amortizing)	4.68	500	599
November 2025 subordinated debt		5.50	3,000	3,000
(requires $150,000 quarterly payments beginning in November 2020)				
			$ 29,420	$ 36,704

The following table represents maturities/repayments of the remaining FHLB advances and subordinated debt at December 31, 2018:

(Dollars in 000s)	Amount
2019	$ 12,297
2020	10,461
2021	3,926
2022	940
2023	746
Thereafter	1,050
Total	$ 29,420

10. Borrowed Funds (Continued)

Borrowings from the FHLB are collateralized by certain qualifying assets of the Bank with an approximate value of $219,000,000 at December 31, 2018. The Bank has a maximum borrowing capacity with the FHLB of approximately $149,467,000 of which $46,970,000 is outstanding and includes $20,550,000 in total letters of credits issued to municipalities to secure deposits.

The following table represents the activity related to the Bank's short-term borrowings under the $25 million line of credit with the FHLB of Pittsburgh:

(Dollars in 000s)	As of and for the Years Ended December 31, 2018	2017
Balance at year-end	$ -	$ 23,221
Average balance outstanding during the year	10,639	24,896
Maximum amount outstanding at any month-end	19,181	40,590
Weighted-average interest rate:		
As of year-end	2.62 %	1.54 %
Paid during the year	2.27 %	1.19 %

11. Related-Party Transactions

The Bank has had banking transactions in the ordinary course of business with its executive officers, directors, principal stockholders, and their affiliated companies (related parties) on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others. A summary of loan activity during the year ended December 31, 2018 is as follows:

Balance at December 31, 2017	Additions	Amount Collected	Balance at December 31, 2018
$2,102,000	$1,153,000	$616,000	$2,639,000

Deposits from related parties totaled $5,586,000 and $5,367,000 as of December 31, 2018 and 2017 respectively.

12. Off-Balance Sheet Commitments

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

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

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

12. Off-Balance Sheet Commitments (Continued)

necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include personal or commercial real estate, accounts receivable, inventory, and equipment.

Outstanding letters of credit written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The majority of these standby letters of credit expire within the next 12 months. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending other loan commitments. The Bank requires collateral supporting these letters of credit, as deemed necessary. Management believes that the proceeds obtained through a liquidation of such collateral would be sufficient to cover the maximum potential amount of future payments required under the corresponding guarantees.

A summary of the Bank's financial instrument commitments is as follows:

(Dollars in 000s)	December 31, 2018	December 31, 2017
Commitments to extend credit	$ 21,858	$ 6,803
Unfunded commitments	79,799	78,027
Standby letters of credit	9,205	7,669
Total	$ 110,862	$ 92,499

13. Income Taxes

The provision for federal income taxes consisted of the following:

(Dollars in 000s)	Years Ended December 31, 2018	Years Ended December 31, 2017
Current	$ 737	$ 962
Deferred	197	500
Total	$ 934	$ 1,462

Included within the applicable income tax for the year ended December 31, 2017 is $81,907 in reduction of income tax expense as a result of the remeasurement of the net deferred tax liability necessary because of the enacted corporate tax rates included in the "Tax Cuts and Jobs Act of 2017". The Act reduces the corporate tax rate from a graduated 34% tax rate to a flat 21% tax rate. As a result, in accordance with generally accepted accounting principles, the Bank was required to remeasure the net deferred tax asset as of December 22, 2017 to recognize future tax benefits and liabilities at the 21% tax rate.

Reconciliation of the statutory income tax expense computed at 21% to the income tax expense included in the statements of income is as follows:

(Dollars in 000s)	Years Ended December 31, 2018		Years Ended December 31, 2017	
	Amount	% of Pretax Income	Amount	% of Pretax Income
Provision at statutory rate	$ 1,214	21.0 %	$ 2,023	34.0 %
Tax exempt interest, net	(217)	(3.8)	(387)	(6.5)
Life insurance	(45)	(0.8)	(75)	(1.3)
Effect of tax rate change	-	(0.3)	(82)	(1.4)
Other, net	(18)	(0.0)	(17)	(0.3)
Actual tax expense and effective rate	$ 934	16.2 %	$ 1,462	24.5 %

13. Income Taxes (continued)

Net deferred tax assets (liabilities) consisted of the following components:

(Dollars in 000s)	As of December 31, 2018	2017
Deferred tax assets:		
Allowance for loan losses	$ 1,090	$ 1,049
Other pension adjustments	218	238
Nonaccrual loan interest	75	97
Net unrealized loss on securities	67	16
Deferred loan fees	189	110
Deferred gains from sale of assets	54	72
Other	63	42
Total deferred tax assets	1,756	1,624
Deferred tax liabilities:		
Accrued pension	(183)	(195)
Premises and equipment	(464)	(360)
Deferred loan fees costs	(1,277)	(1,079)
Mortgage servicing rights	(45)	(49)
Prepaid expenses	(85)	(73)
Total deferred tax liabilities	(2,054)	(1,756)
Net deferred tax assets (liability)	$ (298)	$ (132)

14. Concentration of Credit Risk

The Bank grants commercial, residential, and consumer loans to customers primarily located in Lebanon County, Pennsylvania. The concentrations of credit by type of loan are set forth in Note 4. Although the Bank has a diversified loan portfolio, its debtors' ability to honor their contracts is influenced by the region's economy.

15. Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet 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 and 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.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of Total, Tier I capital and Common Equity Tier I capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2018, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2018, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the Bank's category.

15. Regulatory Matters (Continued)

The Bank's actual capital amounts and ratios as of December 31 are also presented below:

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
(Dollars in 000s)	Amount	Ratio	≥ Amount	≥ Ratio	≥ Amount	≥ Ratio
Total capital (to risk-weighted assets)						
2018	$ 63,909	12.50 %	$ 40,915	8.00 %	$ 51,144	10.00 %
2017	$ 58,690	11.88 %	$ 39,518	8.00 %	$ 49,398	10.00 %
Tier I capital (to risk-weighted assets)						
2018	$ 54,971	10.75 %	$ 30,686	6.00 %	$ 40,915	8.00 %
2017	$ 49,785	10.08 %	$ 29,639	6.00 %	$ 39,518	8.00 %
Tier I capital (to average assets)						
2018	$ 54,971	9.41 %	$ 23,366	4.00 %	$ 29,208	5.00 %
2017	$ 49,785	8.74 %	$ 22,841	4.00 %	$ 28,552	5.00 %
Common equity tier one capital (to risk-weighted assets)						
2018	$ 54,971	10.75 %	$ 23,015	4.50 %	$ 32,244	6.50 %
2017	$ 49,785	10.08 %	$ 22,229	4.50 %	$ 32,109	6.50 %

The Bank is subject to certain restrictions on the amount of dividends that it may declare without prior regulatory approval. At December 31, 2018, $43,206,000 of retained earnings was available for dividend declaration without prior regulatory approval, subject to the above regulatory capital requirements.

16. Fair Value

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1) and the lowest priority to unobservable inputs (level 3). Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The three levels of the fair value hierarchy under Table 820 are described as follows:

Level I: Inputs to the valuation methodology are quoted prices (unadjusted) in active markets for identical assets or liabilities that the organization can access at the measurement date.

Level II: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, such as:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level III: Inputs that are unobservable inputs for the asset or liability.

16. Fair Value (Continued)

An asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

All securities available for sale are priced using pricing models, quoted prices of securities with similar characteristics or using discounted cash flows and therefore are classified in the level 2 hierarchy.

For financial assets measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2018 and 2017 are as follows:

	As of December 31, 2018			
(Dollars in 000s)	Level I	Level II	Level III	Total
Assets measured on a recurring basis:				
Available-for-sale securities:				
U.S. government agencies	$ -	$ -	$ -	$ -
Certificates of deposit	-	2,603	-	2,603
Obligations of states and political subdivisions	-	11,119	-	11,119
Mortgage-backed securities in government-sponsored entities	-	26,843	-	26,843
Total	$ -	$ 40,565	$ -	$ 40,565

	As of December 31, 2017			
(Dollars in 000s)	Level I	Level II	Level III	Total
Assets measured on a recurring basis:				
Available-for-sale securities:				
U.S. government agencies	$ -	$ 1,000	$ -	$ 1,000
Certificates of deposit	-	2,634	-	2,634
Obligations of states and political subdivisions	-	11,898	-	11,898
Mortgage-backed securities in government-sponsored entities	-	26,215	-	26,215
Total	$ -	$ 41,747	$ -	$ 41,747

Certain financial assets are measured at fair value on a nonrecurring basis in accordance with accounting principles generally accepted in the United States of America. Adjustments to the fair value of these assets usually result from the application of lower-of-cost-or-market accounting or write-downs of individual assets.

The following describes the valuation techniques used by the Bank to measure certain financial assets recorded at fair value on a nonrecurring basis in the financial statements.

Other Real Estate Owned

Certain assets such as other real estate owned (OREO) acquired through foreclosure are initially recorded at fair value of the property at the transfer date less estimated selling costs. At or near the time of foreclosure, real estate appraisals are obtained on the properties acquired through foreclosure in order to establish fair value. Appraised values are typically determined utilizing an income or market valuation approach based on an appraisal conducted by an independent, licensed appraiser outside of the Bank using observable market data or on a recent sale offer (Level 2).

16. Fair Value (Continued)

Other Real Estate Owned (Continued)

However, if the appraisal for the acquired property is over two years old, then the fair value is considered Level 3. The estimate of costs to sell the property is based on historical transactions of similar holdings. There were no OREO properties with write-downs during the year ended December 31, 2018 and two with write-downs during the year ended December 31, 2017.

Impaired Loans

Loans of a commercial nature are designated as impaired when, in the judgment of management based on current information and events, it is probable that all amounts due will not be collected according to the contractual terms of the loan agreement. The measurement of loss associated with impaired loans can be based on either the observable market price of the loan, the fair value of the collateral (if collateral dependent), or the present value of expected future cash flows. Fair value is measured based on the value of the collateral securing the loan less estimated costs to sell or the expected present value of future cash flows. Collateral may be in the form of real estate or business assets including equipment, inventory, and accounts receivable. The value of the collateral is typically determined utilizing an income or market valuation approach based on an appraisal conducted by an independent, licensed appraiser outside of the Bank using observable market data (Level 2). However, if the collateral is a house or building in the process of construction or if an appraisal of the real estate property is stale, then the fair value is considered Level 3. The value of business equipment is based upon an outside appraisal if deemed significant, or the net book value on the applicable business' financial statements if not considered significant. Likewise, values for inventory and accounts receivable collateral are based on financial statement balances or aging reports (Level 3). Impaired loans with an allocation to the allowance for loan losses are measured at fair value on a nonrecurring basis. Any fair value adjustments are recorded in the period incurred as provision for loan losses on the Statements of Income.

The fair value of impaired loans reported below is based on the total impaired loans with a specific allowance for loan loss allocation less the total allocations for such loans, while the fair value measurement level is based on the age of the underlying appraisal of the collateral securing the loans. Specific allocations to the allowance for loan losses for impaired loans were $205,000 and $149,000 at December 31, 2018 and 2017, respectively.

There were no loans held for sale as of December 31, 2018 or December 31, 2017.

For financial assets measured at fair value on a nonrecurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2018 and 2017 are as follows:

	As of December 31, 2018				
(Dollars in 000s)	Level I	Level II	Level III	Total	Gain\(Losses)
Impaired loans	$ -	$ -	$ 435	$ 435	$ -
Other real estate owned	-	-	433	433	-
Total	$ -	$ -	$ 868	$ 868	$ -

	As of December 31, 2017				
(Dollars in 000s)	Level I	Level II	Level III	Total	Gain\(Losses)
Impaired loans	$ -	$ -	$ 578	$ 578	$ -
Other real estate owned	-	-	554	554	
Total	$ -	$ -	$ 1,132	$ 1,132	$ -

16. Fair Value (Continued)

Impaired Loans (Continued)

The following table provides a listing of the significant unobservable inputs used in the fair value measurement process for items valued utilizing Level III techniques:

As of December 31, 2018				
(Dollars in 000s)	Fair Value	Valuation Techniques	Unobservable Input	Range
Impaired Loans	$ 435	Appraised collateral values and discounted cash flows	Discount for time since appraisal	0-30%
			Selling costs	0-8%
Other real estate owned	$ 433	Appraised collateral values	Selling costs	0-8%

As of December 31, 2017				
(Dollars in 000s)	Fair Value	Valuation Techniques	Unobservable Input	Range
Impaired Loans	$ 578	Appraised collateral values and discounted cash flows	Discount for time since appraisal	0-30%
			Selling costs	0-6%
Other real estate owned	$ 554	Appraised collateral values	Selling costs	0-6%

17. Fair Values of Financial Instruments

On January 1, 2018 the company adopted ASU 2016-01, which requires the use of the exit price notion to measure the fair value of financial instruments. The following information should not be interpreted as an estimate of the fair value of the entire Bank, since a fair value calculation is only provided for a limited portion of the Bank's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Bank's disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Bank's financial instruments at December 31, 2018 and 2017.

Cash and due from banks and interest bearing balances with other banks
The carrying amounts reported in the balance sheet for cash and short-term instruments approximate those assets' fair values.

Securities available for sale and held to maturity
The Bank utilizes a third-party source to determine the fair value of its securities available for sale (carried at fair value) and held to maturity (carried at amortized cost). The methodology consists of pricing models based on asset class and includes available trade, bid, other market information, broker quotes, proprietary models, various databases and trading desk quotes, some of which are heavily influenced by unobservable inputs. The carrying amount of time certificates of deposit approximates its fair value.

17. Fair Values of Financial Instruments (Continued)

Loans receivable
For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. The fair values for other loans (e.g., residential real estate and consumer loans) are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality.

Restricted investment in Bank stock
The carrying amount of restricted investment in Bank stock approximates fair value.

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

Mortgage servicing rights
The fair value of mortgage servicing rights is based on observable market prices, when available, or the present value of expected future cash flows.

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

Short-term debt
The amounts of short-term debt approximate their fair value.

Long-term debt
Fair values of long-term debt are estimated using discounted cash flow analysis, based on rates currently available to the Bank for advances from the FHLB with similar terms and remaining maturities.

Off-balance sheet financial instruments
Fair values for the Bank's off-balance sheet financial instruments (lending commitments and letters of credit) are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing.

17. Fair Values of Financial Instruments (Continued)

The estimated fair values of the Bank's financial instruments were as follows at December 31, 2018 and 2017:

			As of December 31, 2018		
(Dollars in 000s)	Carrying Amount	Fair Value	Level I	Level II	Level III
Financial assets:					
Cash and due from banks	$ 3,355	$ 3,355	$ 3,355		
Interest Bearing Balances with other Banks	10,519	10,519	10,519		
Available-for-sale securities	40,565	40,565		40,565	
Held-to-maturity securities	843	844		844	
Net loans	505,466	501,234		500,799	435
Accrued interest receivable and dealer reserve	1,999	1,999	1,999		
Restricted investment in Bank stock	1,734	1,734		1,734	
Mortgage servicing rights	215	581		581	
Financial liabilities:					
Deposits	$ 502,452	$ 500,779		$ 500,779	
Long-term debt	29,420	29,411		29,411	
Accrued interest payable	217	217	217		

			As of December 31, 2017		
(Dollars in 000s)	Carrying Amount	Fair Value	Level I	Level II	Level III
Financial assets:					
Cash and due from banks	$ 2,769	$ 2,769	$ 2,769		
Interest Bearing Balances with other Banks	10,528	10,528	10,528		
Available-for-sale securities	41,747	41,747		41,747	
Held-to-maturity securities	851	853		853	
Net loans	491,231	491,824		491,246	578
Accrued interest receivable and dealer reserve	2,131	2,131	2,131		
Restricted investment in Bank stock	2,965	2,965		2,965	
Mortgage servicing rights	234	604		604	
Financial liabilities:					
Deposits	$ 464,166	$ 463,273		$ 463,273	
Short-term debt	23,221	23,221		23,221	
Long-term debt	36,704	36,637		36,637	
Accrued interest payable	184	184	184		

18. Contingencies

The Bank is subject to claims and lawsuits which arise primarily in the ordinary course of business. Based on information presently available and advice received from legal counsel representing the Bank in connection with any such claims and lawsuits, it is the opinion of management that the disposition or ultimate determination of any such claims and lawsuits will not have a material adverse effect on the financial position, results of operations or liquidity of the Bank.

19. Subsequent Events

Management has reviewed events occurring through February 26, 2019, the date the financial statements were available to be issued and no subsequent events occurred requiring disclosure.

ROLLING FOR REPEAL

Images provided by Eric Kovac, Communications Director, PACB.

During 2018, Troy Peters served as Chairman of Pennsylvania Association of Community Bankers. One of the priorities during his PACB term was to advocate for government regulatory relief.

Together with Nick DiFrancesco, PACB President & CEO, the duo toured on their motorcycles across Pennsylvania several times during the year. Troy and Nick donned branded leather vests with safety gear, and enjoyed good seasonal biking weather with only a few adverse weather challenges.

They were well received in each community, speaking with news media, government officials, and community banking executives about why the Economic Growth, Regulatory Relief and Consumer Protection Act (S.2155) was critically important. Ultimately, the president signed this Act into law, giving regulatory relief to community banks.

For online details about the *Rolling For Repeal* initiative, please visit: **www.pacb.org/advocacy/rolling-for-repeal**

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This statement has not been reviewed, or confirmed for accuracy or relevance, by the Federal Deposit Insurance Corporation.

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