Consolidated Financial Statements
Years Ended December 31, 2017 and 2016

Fentura Financial, Inc.

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INDEPENDENT AUDITORS' REPORT

March 21, 2018

Shareholders and Board of Directors Fentura Financial, Inc.
Fenton, Michigan

We have audited the accompanying consolidated financial statements of ***Fentura Financial, Inc.*** (the "Corporation"), which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of income, comprehensive income, shareholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Independent Auditors' Responsibility

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

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

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

Opinion

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

Consolidated Balance Sheets

(Dollars in thousands except per share amounts)

	December 31	
	2017	**2016**
ASSETS		
Cash and due from banks	$ 15,928	$ 59,713
Federal funds sold	-	18,600
Cash and cash equivalents	**15,928**	**78,313**
Securities, available-for-sale (AFS)	51,720	68,572
Securities, held-to-maturity (HTM)	3,603	3,886
Total securities	**55,323**	**72,458**
Loans held for sale	**2,067**	**3,869**
Loans	672,530	515,775
Less allowance for loan losses	3,603	2,851
Net loans	**668,927**	**512,924**
Premises and equipment, net	14,448	12,113
Bank owned life insurance	9,763	9,649
Federal Home Loan Bank (FHLB) stock	2,925	1,774
Accrued interest receivable	2,393	1,896
Other real estate owned	92	250
Goodwill	3,219	3,219
Core deposit intangibles	1,895	2,526
Other assets	4,463	4,359
Total assets	**$ 781,443**	**$ 703,350**
LIABILITIES AND SHAREHOLDERS' EQUITY		
Noninterest-bearing deposits	$ 216,607	$ 160,903
Interest-bearing deposits	456,898	442,464
Total deposits	**673,505**	**603,367**
FHLB advances	30,000	30,000
Subordinated debentures	14,000	14,000
Federal funds purchased	2,000	-
Senior debt	-	1,000
Accrued interest and other liabilities	2,491	4,323
Total liabilities	**721,996**	**652,690**
Shareholders' equity		
Common stock, no par value; 5,000,000 shares authorized, 3,631,933 in 2017 (3,619,282 in 2016) shares issued and outstanding	58,961	58,734
Retained earnings (accumulated deficit)	156	(7,847)
Accumulated other comprehensive income (loss)	330	(227)
Total shareholders' equity	**59,447**	**50,660**
Total liabilities and shareholders' equity	**$ 781,443**	**$ 703,350**

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

Consolidated Statements of Income
(Dollars in thousands except per share amounts)

	Year Ended December 31	
	2017	2016
Interest and dividend income		
Loans, including fees	$ 28,765	$ 18,119
Investments		
Taxable	939	355
Tax-exempt	238	99
Cash and cash equivalents	88	13
Federal Home Loan Bank Stock	81	59
Total interest and dividend income	**30,111**	**18,645**
Interest expense		
Deposits	1,890	1,394
Borrowings	1,230	978
Total interest expense	**3,120**	**2,372**
Net interest income	**26,991**	**16,273**
Provision for loan losses	609	(900)
Net interest income, after provision for loan losses	**26,382**	**17,173**
Noninterest income		
Service charges on deposit accounts	1,217	779
ATM and debit card income	1,474	1,150
Net gain on sales of mortgage loans	1,231	1,886
Trust and investment services	1,424	1,367
Other income and fees	3,642	1,476
Total noninterest income	**8,988**	**6,658**
Noninterest expenses		
Compensation	12,437	9,544
Occupancy	1,569	1,142
Furniture and equipment	1,706	1,192
Loan and collection	548	561
Advertising and promotional	598	524
Telephone and communication	433	267
Acquisition related	646	728
Professional services	2,533	1,469
Other general and administrative	3,348	1,670
Total noninterest expenses	**23,818**	**17,097**
Income before federal income taxes	11,552	6,734
Federal income taxes	2,876	2,293
Net income	**$ 8,676**	**$ 4,441**
Earnings per share	**$ 2.39**	**$ 1.70**

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

Consolidated Statements of Comprehensive Income
(Dollars in thousands)

	Year Ended December 31	
	2017	**2016**
Net Income	**$ 8,676**	**$ 4,441**
Other comprehensive income (loss)		
Unrealized gains (losses) on investment securities available for sale	527	(110)
Net unrealized cash flow hedge gains (losses) arising during the year	98	(49)
Reclassification from AOCI resulting from the enactment of the Tax Act. [(1)]	(52)	-
Other comprehensive income (loss) before income taxes	**573**	**(159)**
Income tax (provision) benefit related to other comprehensive income (loss)	(16)	54
Other comprehensive income (loss)	**557**	**(105)**
Comprehensive income	**$ 9,233**	**$ 4,336**

[(1)] The reclassification from accumulated comprehensive income (loss) to retained earnings (accumulated deficit) is due to the early adoption of ASU 2018-02; refer to Notes 1 and 14 for futher details on the adoption.

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

Consoldiated Statements of Shareholders' Equity
(Dollars in thousands except per share amounts)

	Common Stock				
	Common Shares Outstanding	Amount	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Income (Loss)	Total
Balances, January 1, 2016	**2,517,748**	**$ 43,873**	**$ (11,277)**	**$ (122)**	**$ 32,474**
Issuance of common shares under stock purchase and dividend reinvestment plans	30,106	422	-	-	422
Issuance of common shares in private placements, net of issuance costs	1,071,428	14,439	-	-	14,439
Cash dividends paid	-	-	(1,011)	-	(1,011)
Comprehensive income	-	-	4,441	(105)	4,336
Balances, December 31, 2016	**3,619,282**	**58,734**	**(7,847)**	**(227)**	**50,660**
Issuance of common shares under stock purchase and dividend reinvestment plans	12,651	227	-	-	227
Reclassification from AOCI resulting from the enactment of the Tax Act. [1]			52	(52)	-
Cash dividends paid	-	-	(725)	-	(725)
Comprehensive income	-	-	8,676	609	9,285
Balances, December 31, 2017	**3,631,933**	**$ 58,961**	**$ 156**	**$ 330**	**$ 59,447**

[1] The reclassification from accumulated comprehensive income (loss) to retained earnings (accumulated deficit) is due to the early adoption of ASU 2018-02; refer to Notes 1 and 14 for futher details on the adoption.

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

Consoldated Statements of Cash Flows

(Dollars in thousands)

	Year Ended December 31	
	2017	2016
Cash flows from operating activities		
Net income	$ 8,676	$ 4,441
Adjustments to reconcile net income to net cash provided by operating activities, net in 2016 of business combination		
Depreciation	910	750
Net amortization (accretion) on securities	417	(169)
Amortization of mortgage servicing rights	538	477
Amortization of core deposit intangibles	631	-
Provision for loan losses	609	(900)
Mortgage loans originated for sale	(77,540)	(101,628)
Proceeds from sale of mortgage loans	80,573	102,550
Net (gains) losses on sales of mortgage loans	(1,231)	(1,886)
Net (gains) losses on sales of foreclosed assets	(11)	(11)
Write-down of foreclosed assets	46	-
Net (gains) losses on sales of premises and equipment	150	-
Net (gains) losses on redemptions of bank owned life insurance	(1,155)	-
Deferred income tax (benefit) expense	2,468	1,296
Increase in cash surrender value of bank owned life insurance	(217)	(217)
Net (increase) decrease in interest receivable and other assets	(3,525)	(76)
Net increase (decrease) in accrued interest payable and other liabilities	(1,832)	999
Net cash provided by (used in) operating activities	**9,507**	**5,626**
Cash flows from investing activities		
Activity in AFS securities		
Sales, calls, maturities, and principal paydowns	22,291	7,259
Purchases	(5,293)	-
Activity in HTM securities		
Sales, calls, maturities, and principal paydowns	247	414
Purchases	-	(2,124)
Net loan principal (originations) collections	(156,681)	(52,792)
Proceeds from sales of foreclosed assets	192	206
Purchases of FHLB stock	(1,151)	(464)
Net purchases of premises and equipment	(3,395)	(498)
Proceeds from redemption of bank owned life insurance	1,258	-
Acquisition, net of cash acquired	-	21,170
Net cash provided by (used in) investing activities	**(142,532)**	**(26,829)**
Cash flows from financing activities		
Net increase (decrease) in deposits	70,138	56,016
Cash dividends paid	(725)	(1,011)
Net advances (repayments) on line of credit	(1,000)	1,000
Net advances (repayments) from FHLB	2,000	9,225
Net proceeds from common stock issuance	227	14,861
Net cash provided by (used in) financing activities	**70,640**	**80,091**
Net change in cash and cash equivalents	**(62,385)**	**58,888**
Cash and cash equivalents, beginning of year	78,313	19,425
Cash and cash equivalents, end of year	**$ 15,928**	**$ 78,313**
Supplemental cash flows information:		
Interest paid	$ 3,014	$ 2,331
Income taxes paid	$ 2,275	$ 169
Transfers of loans to other real estate	$ 69	$ 98
Loans provided for sales of other real estate owned	**$** -	$ 162
Business Combinations		
Fair value of tangible assets acquired	**$** -	$ 144,481
Goodwill, mortgage servicing rights, and core deposit intangible asset acquired	**$** -	$ 5,925
Liabilities assumed	**$** -	$ 171,576

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands except per share amounts)

Note 1 – Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations and Principles of Consolidation

The consolidated financial statements include Fentura Financial, Inc. (the "Parent") and its wholly owned subsidiaries Fentura Holdings LLC ("FHLLC") and The State Bank ("the Bank"), (collectively the "Corporation"). Intercompany transactions and balances are eliminated in consolidation.

The Corporation provides banking and trust services principally to individuals, small businesses and governmental entities through its fifteen community banking offices in Genesee, Livingston, Oakland, Saginaw and Shiawassee Counties in central and southeastern Michigan. Its primary deposit products are checking, savings, and term certificate accounts, and its primary lending products are residential mortgage, commercial, and installment loans. Substantially all loans are secured by specific items of collateral including business assets, consumer assets and real estate. Commercial loans are expected to be repaid from cash flow from operations of businesses. Real estate loans are secured by both residential and commercial real estate. The Corporation's exposure to credit risk is substantially affected by the economy in the Corporation's market area and by changes in commercial real estate values. While the loan portfolio is substantially commercial based, the Corporation is not dependent on any single borrower. Refer to Note 6 for further disclosures related to the composition of the loan portfolio.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the consolidated financial statements and the disclosures provided, and future results could differ. The allowance for loan losses, the fair value amounts related to business combinations, the fair values of securities and derivatives, and other financial instruments, other-than-temporary impairment of securities, goodwill and other intangible asset impairment and the carrying value of deferred income taxes are particularly subject to change.

Business Combinations

Pursuant to the guidance of Accounting Standards Codification ("ASC") Topic 805, Business Combinations ("ASC 805"), the Corporation recognizes assets acquired, including identified intangible assets, and the liabilities assumed in acquisitions at their fair values as of the acquisition date, with the acquisition-related transaction costs expensed in the period incurred.

On December 31, 2016, the Corporation acquired all of the outstanding common stock of Community Bancorp, Inc. in St. Charles, Michigan ("Community") for total cash consideration of approximately $21.6 million. The Corporation recorded approximately $3.2 million of goodwill in conjunction with the acquisition, which represented the purchase price over the fair value of identifiable net assets acquired. Additionally, the Corporation recorded approximately $2.5 million of identifiable core deposit intangible assets in conjunction with the acquisition related to total deposits acquired of approximately $171.4 million.

See Note 2 for further information regarding the Corporation's acquisition activity.

Basis of Presentation

The cash consideration of $21.6 million paid to acquire Community was not actually disbursed to the transfer agent until January 4, 2017, though the transaction legally closed effective December 31, 2016. The 2016 consolidated financial statements presented herein reflect the effect of this cash transfer as if it had occurred on December 31, 2016.

Cash and Cash Equivalents

Cash and cash equivalents (see preceding paragraph), includes cash, deposits with other financial institutions under 90 days, and federal funds sold. Net cash flows are reported for customer loan and deposit transactions and short-term borrowings.

Restrictions on Cash

Cash on hand or on deposit with the Federal Reserve Bank of $0 and $223 was required to meet regulatory reserve and clearing requirements at December 31, 2017 and 2016, respectively. Such amounts are included in cash and due from banks in the consolidated balance sheets.

Investment Securities

Securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Securities are classified as available for sale when they might be sold before maturity. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income.

Interest income includes amortization or accretion of purchase premiums or discounts. Premiums and discounts on securities are amortized or accreted on the level-yield method without anticipating prepayments, except for mortgage-backed securities, where prepayments are anticipated. Premiums are amortized to call date whereby discounts are accreted to maturity. Gains and losses on sales are based on the amortized cost of the security sold.

Management evaluates securities for other-than-temporary impairment ("OTTI") at least on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation.

In determining OTTI, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether the Corporation has the intent to sell the debt security or it is more likely than not it will be required to sell the debt security before its anticipated recovery. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

When OTTI occurs, the amount of the OTTI recognized in earnings depends on whether the Corporation intends to sell the security or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss. If the Corporation intends to sell or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss, the OTTI shall be recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. If the Corporation does not intend to sell the security and it is not more likely than not that, the Corporation will not be required to sell the security before recovery of its amortized cost basis less any current-period loss, the OTTI shall be separated into the amount representing the credit loss and the amount related to all other factors. The amount of the total OTTI related to the credit loss is determined based on the present value of cash flows expected to be collected and is recognized in earnings. The amount of the total OTTI related to other factors is recognized in other comprehensive income, net of applicable taxes. The previous amortized cost basis less the OTTI recognized in earnings becomes the new amortized cost basis of the investment.

Loans Held for Sale

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of aggregate cost or fair value, as determined by outstanding commitments from investors. Net unrealized losses, if any, are recorded as a valuation allowance and charged to earnings.

Mortgage loans held for sale are generally sold with servicing rights retained. The carrying value of mortgage loans sold is reduced by the amount allocated to the servicing right. Gains and losses on sales of mortgage loans are based on the difference between the selling price and the carrying value of the related loan sold.

Originated Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, unearned interest, deferred loan fees and costs, and an allowance for loan losses. Loan origination fees, net of are deferred and recognized in interest income using the level-yield method without anticipating prepayments.

Interest income on mortgage and commercial loans is discontinued and placed on non-accrual status at the time the loan is 90 days delinquent unless the loan is well-secured and in the process of collection. Mortgage loans are charged off at 180 days past due and commercial loans are charged off to the extent principal or interest is deemed uncollectible. Consumer and credit card loans continue to accrue interest until they are charged-off (no later than 120 days past due unless the loan is in the process of collection). Past-due

status is based on the contractual terms of the loan. In all cases, loans are placed on non-accrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. Non-accrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

All interest accrued but not received for loans placed on nonaccrual is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Under the cost-recovery method, interest income is not recognized until the loan balance is reduced to zero. Under the cash-basis method, interest income is recorded when the payment is received in cash. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Acquired Loans

Purchased loans are recorded at fair value at the date of acquisition based on a discounted cash flow methodology that considered various factors including the type of loan and related collateral, classification status, fixed or variable interest rate, term of loan and whether or not the loan was amortizing, and a discount rate reflecting the Corporation's assessment of risk inherent in the cash flow estimates. These cash flow evaluations are inherently subjective as they require material estimates, all of which may be susceptible to significant change.

Purchased credit impaired loans are accounted for in accordance with the provisions of Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Subtopic 310-30, "Receivables—Loans and Debt Securities Acquired with Deteriorated Credit Quality" ("ASC 310-30"). The cash flows expected to be collected on purchased loans are estimated based upon the expected remaining life of the underlying loans, which includes the effects of estimated prepayments. Purchased loans are considered credit impaired if there is evidence of credit deterioration at the date of purchase and if it is probable that not all contractually required payments will be collected. Purchased credit impaired loans are not classified as nonperforming assets as the loans are considered performing under ASC 310-30. Interest income, through accretion of the difference between the carrying value of the loans and the expected cash flows is recognized on all purchased loans accounted for under ASC 310-30. Expected cash flows are re-estimated at least annually for all loans accounted for under ASC 310-30. A decline in the present value of current expected cash flows compared to the previously estimated expected cash flows, due in any part to change in credit, is referred to as credit impairment and recorded as provision for loan losses during the period. Declines in the present value of expected cash flows only from the expected timing of such cash flows is referred to as timing impairment and recognized prospectively as a decrease in yield on the loan. Improvement in expected cash flows is recognized prospectively as an adjustment to the yield on the loan once any previously recorded impairment is recaptured. Accelerated discounts on acquired loans result from the accelerated recognition of a portion of the loan discount that would have been recognized over the expected life of the loan and occur when a loan is paid in full or otherwise settled.

Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable incurred credit losses, increased by the provision for loan losses and decreased by charge-offs less recoveries. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management’s judgment, should be charged-off. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Consumer loans are typically charged off no later than 120 days past due.

The allowance consists of specific, general, and unallocated components. The specific component relates to loans that are individually classified as impaired or loans otherwise classified as substandard or doubtful. The general component covers non-classified loans and is based on historical loss experience adjusted for current factors. The historical loss experience is determined by portfolio segments and is based on the actual weighted average loss history experienced by the Corporation over a range of the most recent 4 quarters to the most recent 20 quarters. This actual loss experience is supplemented with other economic factors based on the risks present for each portfolio segment. These economic factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; and effects of changes in credit concentrations. The following portfolio segments have been identified: commercial, commercial real estate, residential real estate, installment loans and home equity loans.

A loan is impaired when full payment under the loan terms is not expected. Commercial and commercial real estate loans are

individually evaluated for impairment. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Large groups of smaller balance homogeneous loans, such as consumer and residential real estate loans, are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosures.

Troubled Debt Restructurings

Under certain circumstances, the Bank will provide borrowers relief through loan restructurings and modifications. A loan restructuring constitutes a troubled debt restructuring ("TDR") if for economic or legal reasons related to the borrower's financial difficulties the Bank grants a concession to the borrower that it would not otherwise consider. Restructured loans typically present an elevated level of credit risk, as the borrowers are not able to perform according to the original contractual terms. Loans that are reported as TDRs are considered impaired and are measured for impairment.

Transfers of Financial Assets

Transfers of financial assets, including mortgage loans held-for-sale, as described above, 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 legally 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. Other than servicing, the Bank has no substantive continuing involvement related to these loans.

Derivative Instruments and Hedging Activities

Derivative instruments are carried at fair value on the consolidated balance sheets and are recorded in either other assets or accrued interest payable and other liabilities. The accounting for changes in the fair value (i.e., gains or losses) of a derivative instrument is determined by whether it has been designated and qualifies as part of a hedging relationship, and, further, by the type of hedging relationship. For derivative instruments that are designated and qualify as cash flow hedges (i.e., hedging the exposure to variability in expected future cash flows that are attributable to a particular risk), the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The remaining gain or loss on the derivative instrument in excess of the cumulative change in the present value of future cash flows of the hedged item (i.e. the ineffective portion), if any, is recognized in earnings during the period of change.

For cash flow hedging relationships, the Corporation assesses prospective and retrospective effectiveness as well as measurement based upon the cumulative hypothetical derivative method. Under the hypothetical derivative method, the cumulative change in the fair value of the derivative instrument is compared to the cumulative change in the fair value of a hypothetical derivative. The Corporation uses the cumulative dollar-offset ratio resulting from the application of the hypothetical derivative method to assess effectiveness. In addition, the Corporation assesses whether the hedged forecasted transactions are still probable of occurring, and monitors the creditworthiness of the Counterparty to determine whether the risk of default continues to be remote.

Further information on the Corporation's derivative instrument and hedging activities is included in Note 9.

Servicing

Servicing assets are recognized as separate assets when rights are acquired through the purchase or sale of financial assets. For sales of mortgage loans, a portion of the cost of originating the loan is allocated to the servicing right based on relative fair value. Fair value is based on market prices for comparable mortgage servicing contracts when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses.

Servicing assets or liabilities are amortized in proportion to and over the period of net servicing income or net servicing loss and are assessed for impairment or increased obligation based on fair value of rights compared to amortized cost at each reporting date. Impairment is determined by reviewing the vintage of the loans and comparing the prospective interest rate market to the rate on the current portfolio. Given the recent vintage of the portfolio and the stable to rising rate environment, no impairment has been recorded. Should this situation change, impairment may be evaluated by stratifying rights into tranches based on predominant risk

characteristics, such as interest rate, loan category, and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the capitalized amount for the tranche. If the Bank later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income. The portfolio was reviewed qualitatively at December 31, 2017 and deemed to have no impairment.

The following table outlines the key economic assumptions and the resulting estimated fair value of mortgage servicing rights as of:

	December 31	
	2017	2016
Annual constant prepayment speed (CPR)	9.48%	9.76%
Weighted average life (in months)	281	288
Discount rate	9.21%	9.15%
Estimated fair value	$ 3,120	$ 2,499

The following table outlines activity recorded within and year end balances for mortgage servicing rights and the year end balances of mortgage loans serviced for others as of and for the years ended:

	December 31	
	2017	2016
Beginning of year	$ 2,390	$ 1,465
Additions	1,191	1,402
Amortized to expense	(538)	(477)
End of year	**$ 3,043**	**$ 2,390**
Gross mortgage servicing rights	$ 3,849	$ 3,028
Accumulated amortization	(806)	(638)
End of year	**$ 3,043**	**$ 2,390**
Mortgage loans serviced for others	**$ 288,357**	**$ 212,126**

Servicing fee income is recorded for fees earned for servicing loans for others. The fees are based on a contractual percentage of the outstanding principal, or a fixed amount per loan and are recognized as income when earned. These fees were $614 and $420 in 2017 and 2016, respectively and were included in noninterest income. The amortization of mortgage servicing rights is netted against loan servicing fee income, a component of other income and fees.

Other Real Estate Owned and Foreclosed Assets

Assets acquired through or instead of loan foreclosure are initially recorded at fair value less estimated selling costs when acquired, establishing a new cost basis. Physical possession of residential real estate property collateralizing a consumer mortgage loan occurs when legal title is obtained upon completion of foreclosure or when the borrower conveys all interest in the property to satisfy the loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. If fair value declines, a valuation allowance is recorded through expense. Costs after acquisition are expensed, as incurred.

Bank Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Buildings and related components are depreciated using the straight-line method with useful lives ranging from 15 to 40 years. Furniture, fixtures and equipment are depreciated using the straight-line method with useful lives ranging from 3 to 7 years. Premises and equipment and other assets are reviewed for impairment when events indicate their carrying amount may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value, if lower than the carrying amount.

Federal Home Loan Bank (FHLB) Stock

The Bank is a member of the FHLB system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest additional amounts. FHLB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

Bank Owned Life Insurance

The Corporation holds life insurance policies purchased on the lives of key members of management. In the event of death of one of these individuals, the Corporation, as beneficiary of the policies, would receive a specified cash payment equal to the face value of the policy. Such policies are recorded at their cash surrender value, or the amount that can be currently realized as of the balance sheet date. The change in cash surrender value is an adjustment of premiums paid in determining the net expense or income recognized under the contracts for the year and is included in noninterest income.

Stock Based Compensation

Compensation cost is recognized for stock options, restricted stock awards issued to employees, and stock appreciation rights based on the fair value of these awards at the date of grant. A valuation model is utilized to estimate the fair value of stock options and stock appreciation rights. Compensation cost is recognized over the required service period, generally defined as the vesting period. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award.

Income Taxes

Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. If determined necessary, a valuation allowance reduces deferred tax assets to the amount expected to be realized.

A tax position is recognized as a benefit only if it is “more likely than not” that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that has a greater than 50% likelihood of being realized on examination including the appeals process. For tax positions not meeting the “more likely than not” test, no tax benefit is recorded.

The Corporation recognizes interest and/or penalties related to income tax matters in income tax expense. Such interest or penalties recorded in 2017 and 2016 were not significant.

See Note 10 for a discussion of the impact of federal tax legislation (Tax Cuts and Jobs Act), which was enacted on December 22, 2017.

Goodwill and Other Intangible Assets

Goodwill resulting from business combinations is generally determined as the excess of the fair value of the consideration transferred over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized but tested for impairment at least annually or more frequently if events and circumstances exist that indicate that a goodwill impairment test should be performed. Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill is the only intangible asset with an indefinite life on the consolidated balance sheet. Core deposit intangible assets arising from whole bank and branch acquisitions are amortized using an accelerated method over their estimated useful lives of 7 years.

Loan Commitments and Financial Instruments

Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and standby letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Earnings Per Common Share

Basic earnings per common share is calculated as net income divided by the weighted average number of common shares outstanding during the year. Employee Stock Ownership Plan (ESOP) shares are considered outstanding for this calculation unless unearned.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains and losses on securities available for sale and cash flow hedges, which are also recognized as separate components of equity.

Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated.

Fair Value of Financial Instruments

Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in Note 13. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Reclassifications

Certain items in the prior year consolidated financial statements were reclassified to conform to the current year presentation.

Subsequent Events

In preparing these consolidated financial statements, the Corporation has evaluated, for potential recognition or disclosure, significant events or transactions that occurred during the period subsequent to December 31, 2017, the most recent balance sheet presented herein, through March 21, 2018, the date these consolidated financial statements were available to be issued. No significant such events or transactions were identified other than as disclosed in the basis of presentation section of this footnote.

Recent Accounting Pronouncements

Accounting Standards Update (ASU) No. 2014-09, "Revenue from Contracts with Customers (Topic 606)", supersedes the current revenue recognition requirements in Topic 605, "Revenue Recognition". The ASU is based on the principle that revenue is recognized to depict the transfer of 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. The ASU also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including specific judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. The new guidance will be effective for the Corporation's year ending December 31, 2018. The ASU permits application of the new revenue guidance to be applied using one of two retrospective application methods, although the Corporation has not yet determined which application method it will use, the new standard is not expected to have a significant impact on the Corporation's consolidated financial statements.

ASU No. 2016-02, "Leases (Topic 842)", requires lessees to recognized a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The reporting of lease-related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for the Corporation's year ending December 31, 2019 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The new lease standard is not expected to have a significant effect on the Corporation's consolidated financial statements.

ASU 2016-13, “Financial Instruments - Credit Losses (Topic 326)”, requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts and requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization’s portfolio. In addition, ASU 2016-13 amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. We are currently developing an implementation plan to include an assessment of processes, portfolio segmentation, model development, system requirements and the identification of data and resource needs, among other things. The adoption of ASU 2016-13 is likely to result in an increase in the allowance for loan losses as a result of changing from an “incurred loss” model, which encompasses allowances for current known and inherent losses within the portfolio, to an “expected loss” model, which encompasses allowances for losses expected to be incurred over the life of the portfolio. ASU 2016-13 will be effective on January 1, 2020. We are currently evaluating the potential impact of ASU 2016-13 on our consolidated financial statements.

ASU 2017-01, “Business Combinations (Topic 805) - Clarifying the Definition of a Business.” clarifies the definition and provides a more robust framework to use in determining when a set of assets and activities constitutes a business. ASU 2017-01 is intended to provide guidance when evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. ASU 2017-01 will be effective on January 1, 2018 and is not expected to have a significant impact on the consolidated financial statements.

ASU 2017-04, “Intangibles - Goodwill and Other (Topic 350) - Simplifying the Test for Goodwill Impairment.” eliminates Step 2 from the goodwill impairment test which required entities to compute the implied fair value of goodwill. Under ASU 2017-04, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit’s fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. ASU 2017-04 will be effective for us on January 1, 2020, with earlier adoption permitted and is not expected to have a significant impact on the consolidated financial statements.

ASU 2017-08,“Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20) - Premium Amortization on Purchased Callable Debt Securities.” shortens the amortization period for certain callable debt securities held at a premium to require such premiums to be amortized to the earliest call date unless applicable guidance related to certain pools of securities is applied to consider estimated prepayments. Under prior guidance, entities were generally required to amortize premiums on individual, non-pooled callable debt securities as a yield adjustment over the contractual life of the security. ASU 2017-08 does not change the accounting for callable debt securities held at a discount. ASU 2017-08 will be effective for us on January 1, 2019, and is not expected to have a significant impact on the consolidated financial statements.

ASU 2017-09, “Compensation - Stock Compensation (Topic 718) - Scope of Modification Accounting.” clarifies when changes to the terms or conditions of a share-based payment award must be accounted for as modifications. Under ASU 2017-09, an entity will not apply modification accounting to a share-based payment award if all of the following are the same immediately before and after the change: (i) the award's fair value, (ii) the award's vesting conditions and (iii) the award's classification as an equity or liability instrument. ASU 2017-09 will be effective on January 1, 2018 and is not expected to have a significant impact on the consolidated financial statements.

ASU 2017-12, “Derivatives and Hedging (Topic 815) - Targeted Improvements to Accounting for Hedging Activities.” amends the hedge accounting recognition and presentation requirements in ASC 815 to improve the transparency and understandability of information conveyed to financial statement users about an entity’s risk management activities to better align the entity’s financial reporting for hedging relationships with those risk management activities and to reduce the complexity of and simplify the application of hedge accounting. ASU 2017-12 will be effective on January 1, 2019 and is not expected to have a significant impact on the consolidated financial statements.

ASU 2018-02, ″Income Statement - Reporting Comprehensive Income (Topic 220)″ requires deferred tax liabilities and assets to be adjusted for the effect of a change in tax laws or rates with the effect included in income from continuing operations in the reporting period that includes the enactment date and permitted early adoption. The Corporation elected to early adopt ASU 2018-02 during the fourth quarter of 2017 and an election was made to reclassify the income tax effects of the Tax Cuts and Jobs Act from accumulated other comprehensive income (loss) to retained earnings. The early adoption of ASU 2018-02, resulted in a $52 reclassification from accumulated other comprehensive income to retained earnings (accumulated deficit) related to the income tax effects of the Tax Cuts and Jobs Act.

Note 2 – Acquisition

Acquisition of Community

On March 23, 2016, the Corporation entered into an Agreement and Plan of Merger with Community and its wholly owned subsidiary Community State Bank, to acquire 100% of the seller's outstanding common stock in a cash transaction. The effective closing date was December 31, 2016. Total cash consideration paid for the purchase of Community was $21,630. In addition, the Corporation incurred $728 of acquisition-related transaction expenses for the year ended December 31, 2016 related to the purchase of Community. As a result of the acquisition, Community State Bank was merged into The State Bank, a wholly owned subsidiary of the Corporation.

The Corporation determined that the purchase of Community constitutes a business combination as defined by ASC 805. Accordingly, the assets acquired and liabilities assumed were recorded at their fair values on the date of acquisition. Fair values were determined in accordance with the guidance provided in ASC Topic 820, "Fair Value Measurements."

The following table summarizes the consideration paid for Community and the amounts of the assets acquired and liabilities assumed recognized at the acquisition date, as well as the fair value at the acquisition date:

Cash consideration paid	**$ 21,630**
Fair value of identifiable assets acquired:	
Cash and cash equivalents	24,200
Federal funds sold	18,600
Investments - available for sale	52,662
Loans, net	84,071
Premises and equipment, net	2,645
Bank owned life insurance	2,864
Accrued interest receivable	544
Other real estate owned	112
Core deposit intangible	2,526
Other assets	1,763
Total identifiable assets acquired	**$ 189,987**
Fair value of liabilities assumed	
Deposits	$ 171,380
Accrued interest payable and other liabilities	196
Total liabilities assumed	**$ 171,576**
Fair value of net identifiable assets acquired	**$ 18,411**
Goodwill resulting from acquisition	**$ 3,219**

Unaudited Pro Forma Combined Results of Operations

The following table presents pro forma 2016 financial information as if the acquisition of Community had occurred at the beginning of 2016. The pro forma information includes adjustments for certain purchase accounting fair value adjustments, amortization of intangibles arising from the transaction, depreciation expense on property acquired and the related income tax effects. The pro forma financial information is not necessarily indicative of the results of operations that would have occurred had the transaction been effected on the assumed date of January 1, 2016. In particular, no adjustments have been made to eliminate the amount of Community's provision for loan losses incurred prior to the acquisition date that would not have been necessary had the acquired loans been recorded at their fair value as of the beginning of 2016.

	Pro Forma 2016
Net interest income	$ 22,622
Net income	$ 5,363
Basic earnings per share	$ 2.06

Note 3 – Goodwill and Intangible Assets

The Corporation has goodwill and core deposit intangible assets which arose from the acquisition of Community effective on December 31, 2016. The carrying value of goodwill was $3,219 as of December 31, 2017 and 2016.

	2017		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Core deposit premium resulting from acquisitions	$ 2,526	$ 631	$ 1,895

	2016		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Core deposit premium resulting from acquisitions	$ 2,526	$ -	$ 2,526

The estimated future amortization expense on the core deposit intangible asset for years ending December 31 are as follows:

2018	$ 541
2019	451
2020	361
2021	271
2022	180
Thereafter	91
Total	**$ 1,895**

Note 4 – Earnings Per Share

The components in the earnings per share computation follow:

	December 31	
	2017	2016
Net Income	$ 8,676	$ 4,441
Weighted average common shares outstanding	3,625,568	2,608,903
Basic earnings per common share	**$ 2.39**	**$ 1.70**

There were no common stock options or other common stock equivalents outstanding at December 31, 2017 or 2016.

Note 5 – Investment Securities

The following is a summary of the amortized cost and fair value of investment securities available-for-sale and held-to-maturity as of:

	December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
U.S. Government and federal agency	$ 23,146	$ 3	$ (83)	$ 23,066
State and municipal	14,972	121	(25)	15,068
Mortgage backed residential	5,193	59	(47)	5,205
Certificates of deposit	4,449	2	(11)	4,440
Collateralized mortgage obligations - agencies	2,019	1	(8)	2,012
Equity	1,288	646	(5)	1,929
Total available for sale	**$ 51,067**	**$ 832**	**$ (179)**	**$ 51,720**
Held to maturity				
State and municipal	**$ 3,603**	**$ -**	**$ (36)**	**$ 3,567**

	December 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
U.S. Government and federal agency	$ 37,414	$ -	$ -	$ 37,414
State and municipal	15,945	10	(32)	15,923
Mortgage backed residential	6,194	92	(16)	6,270
Certificates of deposit	4,460	-	-	4,460
Collateralized mortgage obligations - agencies	3,177	19	(2)	3,194
Equity	1,256	72	(17)	1,311
Total available for sale	**$ 68,446**	**$ 193**	**$ (67)**	**$ 68,572**
Held to maturity				
State and municipal	**$ 3,886**	**$ 1**	**$ (85)**	**$ 3,802**

Contractual maturities of securities at December 31, 2017, were as follows. Securities not due at a single maturity date, such as mortgage backed residential, collateralized mortgage obligations, and equity securities are shown separately.

	December 31, 2017			
	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
U.S. Government and federal agency				
Due from one year or less	$ 6,206	$ 6,200	$ -	$ -
Due from one to five years	16,940	16,866	-	-
Due from five to ten years	-	-	-	-
Due after ten years	-	-	-	-
State and Municipal				
Due from one year or less	6,020	6,017	569	569
Due from one to five years	6,802	6,833	1,823	1,808
Due from five to ten years	2,150	2,218	906	893
Due after ten years	-	-	305	297
Certificates of Deposit				
Due from one year or less	1,240	1,240	-	-
Due from one to five years	3,209	3,200	-	-
Due from five to ten years	-	-	-	-
Due after ten years	-	-	-	-
Mortgage backed residential	5,193	5,205	-	-
Collateralized mortgage obligations - agencies	2,019	2,012	-	-
Equity	1,288	1,929	-	-
Total	**$ 51,067**	**$ 51,720**	**$ 3,603**	**$ 3,567**

Securities pledged at December 31, 2017 and 2016 had a carrying amount of $13,403 and $6,839, respectively, and were pledged to secure public deposits and borrowings.

Securities with unrealized losses at December 31, 2017 and 2016, including both available for sale and held to maturity securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position are as follows:

	December 31, 2017					
	Less Than 12 Months		Over 12 Months			
	Amortized Cost	Gross Unrealized Losses	Amortized Cost	Gross Unrealized Losses	Fair Value	Total Gross Unrealized Losses
U.S. Government and federal agency	$ 1,039	$ (7)	$ 19,898	$ (76)	$ 20,854	$ (83)
State and municipal	5,780	(26)	5,083	(35)	10,802	(61)
Mortgage backed residential	2,016	(47)	-	-	1,969	(47)
Certificates of deposit	-	-	3,954	(11)	3,943	(11)
Collateralized mortgage obligations - agencies	1,737	(8)	-	-	1,729	(8)
Equity	1,000	(5)	-	-	995	(5)
Total	**$ 11,572**	**$ (93)**	**$ 28,935**	**$ (122)**	**$ 40,292**	**$ (215)**

	December 31, 2016					
	Less Than 12 Months		Over 12 Months			
	Amortized Cost	Gross Unrealized Losses	Amortized Cost	Gross Unrealized Losses	Fair Value	Total Gross Unrealized Losses
U.S. Government and federal agency	$ -	$ -	$ -	$ -	$ -	$ -
State and municipal	5,800	(96)	479	(21)	6,279	(117)
Mortgage backed residential	2,146	(16)	-	-	2,146	(16)
Certificates of deposit	-	-	-	-	-	-
Collateralized mortgage obligations - agencies	490	(2)	-	-	490	(2)
Equity	986	(14)	3	(3)	989	(17)
Total	**$ 9,422**	**$ (128)**	**$ 482**	**$ (24)**	**$ 9,904**	**$ (152)**

As of December 31, 2017 , the Corporation's security portfolio consisted of 170 securities, 95 of which were in an unrealized loss position.

Management evaluates securities for other-than-temporary impairment ("OTTI") at least on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. In evaluating OTTI, management additionally considers the factors presented in Note 1. No OTTI was indicated following analysis in 2017 and 2016.

Note 6 – Loans and Allowance for Loan Losses

The Bank originates primarily residential and commercial real estate loans, commercial, and installment loans. The Corporation estimates that the majority of the Bank's loan portfolio is based in Genesee, Oakland, Saginaw, Shiawassee and Livingston counties within central and southeast Michigan. The ability of the Corporation's debtors to honor their contracts is dependent upon the real estate and general economic conditions in these areas.

Loans are summarized as follows at December 31:

	2017	2016
Commercial	$ 82,667	$ 66,912
Commercial real estate	298,920	232,543
Residential real estate	234,032	178,706
Home equity	44,602	30,629
Installment	12,309	6,985
Total loans	672,530	515,775
Allowance for loan losses	(3,603)	(2,851)
Loans, net	**$ 668,927**	**$ 512,924**

Included in total loans above were unamortized premiums (discounts) on purchased loans and net deferred loan fees as of December 31:

	2017	2016
Unamortized premium (discount) on purchased loans	**$ (3,318)**	**$ (5,234)**
Net deferred loan fees	**$ 1,254**	**$ 962**

Activity in the allowance for loan losses, by loan portfolio segment, for the years ended December 31, 2017 and 2016, is as follows:

	Commercial	Commercial Real Estate	Residential Real Estate	Installment	Home Equity	Unallocated	Total
January 1, 2017	$ 236	$ 1,504	$ 922	$ 28	$ 174	$ (13)	$ 2,851
Provision for loan losses	103	(76)	454	79	33	16	609
Loans charged-off	-	-	(23)	(46)	(8)	-	(77)
Loan recoveries	5	209	-	3	3	-	220
December 31, 2017	**$ 344**	**$ 1,637**	**$ 1,353**	**$ 64**	**$ 202**	**$ 3**	**$ 3,603**

	Commercial	Commercial Real Estate	Residential Real Estate	Installment	Home Equity	Unallocated	Total
January 1, 2016	$ 229	$ 1,843	$ 590	$ 41	$ 110	$ 692	$ 3,505
Provision for loan losses	7	(469)	230	(19)	56	(705)	(900)
Loans charged-off	-	(8)	-	(3)	-	-	(11)
Loan recoveries	-	138	102	9	8	-	257
December 31, 2016	**$ 236**	**$ 1,504**	**$ 922**	**$ 28**	**$ 174**	**$ (13)**	**$ 2,851**

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by loan portfolio segment, and impairment evaluation method at December 31, 2017:

	Commercial	Commercial Real Estate	Residential Real Estate	Installment	Home Equity	Unallocated	Total
Individually evaluated for impairment	$ -	$ -	$ 43	$ -	$ -	$ -	$ 43
Collectively evaluated for impairment	319	1,637	1,310	64	202	3	3,535
Acquired with deteriorated credit quality	25	-	-	-	-	-	25
Total ALLL	**$ 344**	**$ 1,637**	**$ 1,353**	**$ 64**	**$ 202**	**$ 3**	**$ 3,603**

	Commercial	Commercial Real Estate	Residential Real Estate	Installment	Home Equity	Unallocated	Total
Individually evaluated for impairment	$ -	$ 1,736	$ 241	$ -	$ -		$ 1,977
Collectively evaluated for impairment	82,508	295,682	232,143	12,287	44,562		667,182
Acquired with deteriorated credit quality	159	1,502	1,648	22	40		3,371
Total loans	**82,667**	**298,920**	**234,032**	**12,309**	**44,602**		**672,530**
Accrued interest receivable	252	830	582	18	223		1,905
Total recorded investment in loans	**$ 82,919**	**$ 299,750**	**$ 234,614**	**$ 12,327**	**$ 44,825**		**$ 674,435**

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by loan portfolio segment, and impairment evaluation method at December 31, 2016:

	Commercial	Commercial Real Estate	Residential Real Estate	Installment	Home Equity	Unallocated	Total
Individually evaluated for impairment	$ 4	$ 234	$ 59	$ -	$ -	$ -	$ 297
Collectively evaluated for impairment	232	1,270	863	28	174	(13)	2,554
Acquired with deteriorated credit quality	-	-	-	-	-	-	-
Total ALLL	**$ 236**	**$ 1,504**	**$ 922**	**$ 28**	**$ 174**	**$ (13)**	**$ 2,851**

	Commercial	Commercial Real Estate	Residential Real Estate	Installment	Home Equity	Unallocated	Total
Individually evaluated for impairment	$ 28	$ 3,134	$ 253	$ -	$ 32		$ 3,447
Collectively evaluated for impairment	65,734	226,908	176,212	6,963	30,492		506,309
Acquired with deteriorated credit quality	1,150	2,501	2,241	22	105		6,019
Total loans	**66,912**	**232,543**	**178,706**	**6,985**	**30,629**		**515,775**
Accrued interest receivable	197	627	348	32	127		1,331
Total recorded investment in loans	**$ 67,109**	**$ 233,170**	**$ 179,054**	**$ 7,017**	**$ 30,756**		**$ 517,106**

Acquired loans were recorded at fair value as of the acquisition date. At the acquisition date, where a loan exhibited evidence of credit deterioration since origination and it was probable at the date of acquisition that the Corporation would not collect all principal and interest payments in accordance with the terms of the loan agreement, the Corporation accounted for the loan under ASC 310-30 and recognized the expected shortfall of expected future cash flows, as compared to the contractual amount due, as a nonaccretable discount. Any excess of the net present value of expected future cash flows over the acquisition date fair value was recognized as the accretable discount, or accretable yield. We recognize accretion of the accretable discount as interest income over the expected remaining life of the purchased loan. Fair value discounts/premiums created on acquired loans accounted for outside the scope of ASC 310-30 are accounted for under ASC 310-20 and are accreted/amortized into interest income over the remaining term of the loan as an adjustment to the related loan's yield.

Changes in the carrying amount of accretable discount for purchased loans accounted for under ASC 310-30 were as follows for the years ended December 31:

	2017	**2016**
Balance at January 1,	$ 1,441	$ -
Additions due to acquisitions	-	1,441
Discount accretion recognized in interest income	(1,108)	-
Net reclassifications (to) from nonaccretable difference [(1)]	1,535	-
Balance at December 31,	**$ 1,868**	**$ 1,441**

(1) The reclassification from nonaccretable discount and other additions to accretable discount may include increases in the amount of contractual principal and interest expected to be collected due to improvement in credit quality, increases in balances outstanding from advances, renewals, extensions and interest rates; as well as reductions in contractual principal and interest expected to be collected due to credit deterioration, payoffs, and decreases in interest rates.

For loans accounted for under ASC 310-30, the Corporation remeasures expected cash flows on at least an annual basis. For loans where the remeasurement process results in a decline in expected cash flows, impairment is recorded. Alternatively, when a loan's remeasurement results in an increase in expected cash flows, the effective yield of the related loan is increased through an addition to the accretable discount.

The total identified improvement in the cash flow expectations resulting in yield adjustments on a prospective basis during the year ended December 31, 2017 for purchased credit impaired loans was $1,535. The Corporation also identified declines in the cash flow expectations of certain loans. A decline in the present value of current expected cash flows compared to the previously estimated expected cash flows, due in any part to change in credit, is referred to as credit impairment and recorded as provision for loan losses

during the year. Declines in the present value of expected cash flows only from the expected timing of such cash flows is referred to as timing impairment and recognized prospectively as a decrease in yield on the loan. Prepayment assumptions are based on one or more of the following estimates or observations: historical observed prepayments, industry trends, or anticipated fluctuations in interest rates. The Corporation recorded a provision for loan losses on purchase credit impaired loans of $25 for the year ended December 31, 2017. As purchase credit impaired loans were acquired on December 31, 2016 there was no associated allowance as of year-end or accretion recorded in the 2016 consolidated statement of income.

Below is the composition of the recorded investment for purchased credit impaired loans accounted for under ASC 310-30 at December 31:

	2017	2016
Contractual cash flows	$ 7,880	$ 11,551
Contractual cash flows not expected to be collected (nonaccretable difference)	2,641	4,091
Expected cash flows	5,239	7,460
Interest component of expected cash flows (accretable yield)	1,868	1,441
Recorded investment	**$ 3,371**	**$ 6,019**

Below is the composition of the outstanding contractual principal balance and carrying amount of acquired loans as of December 31:

	2017	2016
Contractual principal balance	$ 59,663	$ 89,303
Carrying amount	$ 56,345	$ 84,071

For loans not accounted for under ASC 310-30, the Corporation individually assesses for impairment all nonaccrual loans and TDRs.

The following table presents originated loans individually evaluated for impairment by portfolio class of loans as of December 31, 2017:

	Conctractual Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded					
Commercial	$ -	$ -	$ -	$ -	$ -
Commercial real estate	1,736	1,741	-	2,998	146
Residential real estate	-	-	-	-	-
Consumer					
Installment loans	-	-	-	-	-
Home equity	-	-	-	3	-
With an allowance recorded					
Commercial	-	-	-	22	4
Commercial real estate	-	-	-	-	-
Residential real estate	241	242	43	247	11
Consumer					
Installment loans	-	-	-	-	-
Home equity	-	-	-	-	-
Total	**$ 1,977**	**$ 1,983**	**$ 43**	**$ 3,270**	**$ 161**

The following table presents originated loans individually evaluated for impairment by portfolio class of loans as of December 31, 2016:

	Conctractual Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded					
Commercial	$ -	$ -	$ -	$ 9	$ -
Commercial real estate	1,766	1,353	-	1,003	75
Residential real estate	-	-	-	28	4
Consumer					
Installment loans	-	-	-	-	-
Home equity	32	32	-	7	1
With an allowance recorded					
Commercial	41	26	4	88	5
Commercial real estate	1,786	1,790	234	3,508	84
Residential real estate	253	254	59	384	11
Consumer					
Installment loans	-	-	-	-	-
Home equity	-	-	-	23	-
Total	**$ 3,878**	**$ 3,455**	**$ 297**	**$ 5,050**	**$ 180**

Non-accrual loans and loans past due 90 days still accruing include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

Modifications

A modification of a loan constitutes a troubled debt restructuring ("TDR") when a borrower is experiencing financial difficulty and the modification constitutes a concession. The Corporation offers various types of concessions when modifying a loan or lease, however, forgiveness of principal is rarely granted. Commercial loans modified in a TDR often involve temporary interest-only payments, term extensions, and converting revolving credit lines to term loans. Additional collateral, a co-borrower, or a guarantor is often requested. Commercial real estate loans modified in a TDR often involve reducing the interest rate for the remaining term of the loan, extending the maturity date at an interest rate lower than the current market rate for new debt with similar risk, or substituting or adding a new borrower or guarantor. Residential real estate loans modified in a TDR are primarily comprised of loans where monthly payments are lowered to accommodate the borrowers' financial needs through a reduction of interest rate and/or extension of the maturity date. Installment loans modified in a TDR are primarily comprised of loans where the Corporation has lowered monthly payments by extending the term.

Loans modified in a TDR are typically already on nonaccrual status and partial charge-offs have in some cases been taken against the outstanding loan balance. As a result, loans modified in a TDR for the Corporation may have the financial effect of increasing the specific allowance associated with the loan.

The following schedule presents the Corporation's TDRs as of:

	Accruing TDRs	Nonaccrual TDRs	Total
Commercial real estate	$ 1,736	$ -	$ 1,736
Residential real estate	241	-	241
December 31, 2017	$ 1,977	$ -	$ 1,977

	Accruing TDRs	Nonaccrual TDRs	Total
Commercial	$ 20	$ -	$ 20
Commercial real estate	3,134	$ -	3,134
Residential real estate	253	-	253
December 31, 2016	$ 3,407	$ -	$ 3,407

The Corporation allocated $43 and $283 of specific reserves to customers whose loan terms have been modified in TDRs as of December 31, 2017 and 2016, respectively. The Corporation does not have material commitments to lend additional funds to borrowers with loans whose terms have been modified in troubled debt restructurings or whose loans are on nonaccrual as of December 31, 2017.

There were no loans modified in a TDR during 2017 or 2016. There were no TDRs that defaulted in 2017 or 2016.

Based on the Corporation's historical loss experience, losses associated with TDRs are not significantly different than other impaired loans within the same loan segment. As such, TDRs are analyzed in the same manner as other impaired loans within their respective loan segment.

Credit Quality Indicators

Loan delinquency, excluding acquired loans accounted for under ASC 310-30, was as follows as of:

	December 31, 2017					
	Accruing					
	Curent	30-89 Days Past Due	90+ Days Past Due	Nonaccrual	Total Loans	Total Past Due and Nonaccrual
Commercial	$ 82,508	$ -	$ -	$ -	$ 82,508	$ -
Commercial real estate	297,418	-	-	-	297,418	-
Residential real estate	231,261	1,097	-	26	232,384	1,123
Home equity	44,562	-	-	-	44,562	-
Installment	12,282	5	-	-	12,287	5
Total	**$ 668,031**	**$ 1,102**	**$ -**	**$ 26**	**$ 669,159**	**$ 1,128**

	December 31, 2016					
	Accruing					
	Curent	30-89 Days Past Due	90+ Days Past Due	Nonaccrual	Total Loans	Total Past Due and Nonaccrual
Commercial	$ 65,762	$ -	$ -	$ -	$ 65,762	$ -
Commercial real estate	230,042	-	-	-	230,042	-
Residential real estate	176,465	-	-	-	176,465	-
Home equity	30,524	-	-	-	30,524	-
Installment	6,963	-	-	-	6,963	-
Total	**$ 509,756**	**$ -**	**$ -**	**$ -**	**$ 509,756**	**$ -**

The Corporation categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debts such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Corporation analyzes loans individually by classifying the loans as to credit risk. This analysis includes non-homogeneous loans, such as commercial and commercial real estate loans. This analysis is performed on a quarterly basis. The Corporation uses the following definitions for classified risk ratings:

Pass - Loans have a moderate to average risk to established borrowers that display sound financial condition and operating results. The capacity to service debt is stable and demonstrated at a level consistent with or above the industry norms. Borrower and industry trends and outlook are considered good.

Special Mention **-** Loans have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the Corporation's credit position at some future date.

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

Doubtful - Loans have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The Corporation does not typically classify loans as doubtful. Loans that approach this status are charged-off.

Based on the most recent analysis performed, the ending loan balance by risk category of loans by portfolio class is as follows at December 31:

	2017			
	Pass	Special Mention	Substandard	Total
Originated Loans				
Commercial	$ 75,416	$ -	$ -	$ 75,416
Commercial Real Estate	268,793	357	-	269,150
Total	$ 344,209	$ 357	$ -	$ 344,566
Acquired Loans				
Commercial	$ 6,956	$ 135	$ 160	$ 7,251
Commercial Real Estate	28,255	462	1,053	29,770
Total	$ 35,211	$ 597	$ 1,213	$ 37,021

	2016			
	Pass	Special Mention	Substandard	Total
Originated Loans				
Commercial	$ 50,855	$ 38	$ 144	$ 51,037
Commercial Real Estate	204,089	498	129	204,716
Total	$ 254,944	$ 536	$ 273	$ 255,753
Acquired Loans				
Commercial	$ 14,306	$ 1,111	$ 458	$ 15,875
Commercial Real Estate	25,179	1,613	1,035	27,827
Total	$ 39,485	$ 2,724	$ 1,493	$ 43,702

The Corporation considers the performance of the loan portfolio and its impact on the allowance for loan losses. For residential and consumer loan classes, the Corporation also evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. The following table presents the ending loan balance in residential and consumer loans based on payment activity as of December 31:

	2017			
	Home Equity	Installment	Residential Real Estate	Total
Originated loans				
Performing	$ 39,487	$ 10,867	$ 221,265	$ 271,619
Nonperforming	-	-	-	-
Total	$ 39,487	$ 10,867	$ 221,265	$ 271,619
Acquired loans				
Performing	$ 5,115	$ 1,442	$ 12,539	$ 19,096
Nonperforming	-	-	228	228
Total	$ 5,115	$ 1,442	$ 12,767	$ 19,324

	2016			
	Home Equity	Installment	Residential Real Estate	Total
Originated loans				
Performing	$ 26,220	$ 6,440	$ 143,291	$ 175,951
Nonperforming	-	-	-	-
Total	$ 26,220	$ 6,440	$ 143,291	$ 175,951
Acquired loans				
Performing	$ 4,409	$ 545	$ 35,415	$ 40,369
Nonperforming	-	-	-	-
Total	$ 4,409	$ 545	$ 35,415	$ 40,369

Loans to principal officers, directors, and affiliates at December 31, 2017 and 2016 were $5,415 and $5,372, respectively.

Note 7 – Premises and Equipment, Net

Bank premises and equipment, net, is comprised of the following at:

	December 31	
	2017	2016
Land and land improvements	$ 2,951	$ 2,956
Building and building improvements	14,155	13,717
Furniture and equipment	8,251	5,488
Construction in progress	43	-
	25,400	22,161
Less accumulated depreciation	10,952	10,048
Total	$ 14,448	$ 12,113
Depreciation expense for the year	$ 910	$ 750

The Corporation leases property for certain branches and ATM locations. Rent expense was $85 and $76 for 2017 and 2016, respectively. Rent commitments under non-cancelable operating leases were as follows, before considering renewal options that generally are present, at December 31, 2017:

2018	$ 65
2019	58
2020	58
2021	32
2022	4
	$ 217

Note 8 – Deposits

The following is a summary of deposits at:

	December 31	
	2017	2016
Non-interest bearing		
Demand	$ 216,607	$ 160,903
Interest bearing		
Savings	224,558	213,499
Money market demand	67,387	105,007
NOW	2,253	2,153
Time, $100,000 and over	89,397	46,252
Time, $100,000 and under	73,303	75,553
Total interest bearing	456,898	442,464
Total deposits	**$ 673,505**	**$ 603,367**

Scheduled maturities of time deposits for years succeeding December 31, 2017, were as follows:

2018	$ 76,222
2019	39,127
2020	34,488
2021	6,289
2022	6,545
Thereafter	29
Total	$ 162,700

The Corporation held $21,845 and $10,109 in brokered deposits at December 31, 2017 and 2016, respectively.

Deposits from principal officers, directors, and affiliates at December 31, 2017 and 2016 were $5,746 and $5,671, respectively.

Note 9 – Borrowings

Federal Home Loan Bank Advances

Advances from the FHLB were as follows as of December 31,

	2017		2016	
	Rate	Amount	Rate	Amount
Fixed rate due 2017	-	$ -	1.19%	$ 5,000
Fixed rate due 2018	1.66%	10,000	1.66%	10,000
Fixed rate due 2019	1.82%	7,500	1.84%	5,000
Fixed rate due 2020	1.93%	2,500	-	-
One-time putable due 2026, putable in 2021	1.06%	10,000	1.06%	10,000
	1.52%	$ 30,000	1.41%	$ 30,000

The advances are payable at their maturity date; a prepayment penalty is assessed with early payoffs of advances. The advances are collateralized by securities totaling $4,928 and loans totaling $165,940 at December 31, 2017 and securities totaling $6,320 and loans totaling $117,386 at December 31, 2016.

Subordinated Debentures and Trust Preferred Securities

A trust formed by the Corporation issued $12,000 of trust preferred securities in 2003 as part of a pooled offering of such securities. The interest rate is a floating rate (3 month LIBOR plus 3.00%), and the current rate at December 31, 2017 is 4.59%. The Corporation issued subordinated debentures at the same terms as the trust preferred securities to the trust in exchange for the proceeds of the offering; the debentures and related debt issuance costs represent the sole assets of the trust. The Corporation may redeem the subordinated debentures, in whole but not in part, any time after 2008 at a price of 100% of face value. The subordinated debentures must be redeemed no later than 2033.

A trust formed by the Corporation issued $2,000 of trust preferred securities in 2005 as part of a pooled offering of such securities. The interest rate is a floating rate (3 month LIBOR plus 1.60%), and the current rate at December 31, 2017 is 3.05%. The Corporation issued subordinated debentures at the same terms as the trust preferred securities to the trust in exchange for the proceeds of the offering; the debentures and related debt issuance costs represent the sole assets of the trust. The Corporation may redeem the subordinated debentures, in whole but not in part, any time after 2010 at a price of 100% of face value. The subordinated debentures must be redeemed no later than 2035.

The Corporation is not considered the primary beneficiary of these trusts, therefore the trusts are not consolidated in the Corporation's financial statements, rather, the subordinated debentures are presented as a liability.

In the normal course of the interest rate risk management processes, management identified a possible risk to its interest rate risk profile that exposed the Corporation to a possible rise in funding costs. Specifically, during management's review of its Trust Preferred ("Trups") facilities referred to above, it noted that the interest rate currently is a floating rate based upon LIBOR. Management determined that the continuation of the Trups facilities at a floating rate may adversely affect the Corporation's net interest margin in a possible rising rate environment, exposing the Corporation to increased interest rate costs.

In the second quarter of 2013, the Corporation entered into an interest rate cap with Wells Fargo. An interest-rate cap is an over-the-counter derivative that protects the holder from rises in interest rates by making a payment to the holder when an underlying interest rate (the "index" interest rate) exceeds a specified strike rate (the "cap rate"). The interest rate cap is intended to effectively fix the maximum interest rate paid on the Corporation's trust preferred securities.

The interest rate cap has a notional amount of $12,000 and expires on June 15, 2020. During the term of the interest rate cap the Corporation will receive quarterly payments from Wells Fargo, calculated as the excess (if any) of LIBOR over the strike rate (2.00%). As of December 31, 2017 and 2016, respectively, the fair value of the interest rate cap was $69 and $142 which is included in other assets on the consolidated balance sheets.

In the third quarter of 2017, the Corporation entered into an $8,000 line of credit secured by the Corporation's investment in the Bank. This instrument has the option to be at a fixed or variable rate at the time of each draw and matures annually with any individual draw having a maturity of no more than 3 years. The fixed rate option would be priced at the time of draw and the variable rate spreads are 2.75% over 1, 2, or 3 month LIBOR or 0.50% below National Prime if the respective LIBOR rate cannot be determined or offered. There were no outstanding advances against this line as of December 31, 2017. There was $1,000 outstanding on the line at December 31, 2016 at a prime based variable rate of 3.00%.

Note 10 – Income Taxes

The provision for income taxes reflected in the consolidated statements of income for the years ended December 31 consists of the following:

	2017	2016
Current expense	$ 423	$ 997
Deferred expense	2,453	1,296
Income tax expense	**$ 2,876**	**$ 2,293**

The Tax Cuts and Jobs Act (The "Act") was enacted on December 22, 2017. The Act reduced the U.S. federal corporate tax rate from 35% to 21%, among other provisions. The Corporation remeasured certain deferred tax assets and liabilities as of December 31, 2017 based on the rates at which they are expected to reverse in the future, which is generally 21%, resulting in an immediate tax reduction of $489 in 2017.

Income tax expense for continuing operations was less than the amount computed by applying the statutory federal income tax rate to income before income taxes. The reasons for the difference are as follows for the years ended December 31:

	2017	2016
Income tax at statutory rate	$ 3,928	$ 2,290
Tax-exempt interest income	(160)	(68)
Net indemnity proceeds on bank owned life insurance	(393)	-
Bank owned life insurance	(29)	(17)
Remeasurment of deferred taxes due to changes in federal tax law	(489)	-
Other, net	19	88
Income tax expense	**$ 2,876**	**$ 2,293**

The net deferred tax asset (liability) recorded includes the following amounts of deferred tax assets and liabilities as of December 31:

	2017 (Remeasured at 21%)	2016
Deferred tax assets		
Allowance for loan losses	674	$ 796
Acquired loans	697	1,797
Compensation	156	330
Alternative minimum tax credit	-	751
Non-accrual interest	-	37
Other comprehensive income tax adjustments	84	78
Other	91	700
Total deferred tax assets	1,702	4,489
Deferred tax liabilities		
Fixed assets	$ 1,106	$ 977
Mortgage servicing rights	649	818
Core deposit intangible	398	741
Prepaid expenses	96	-
Deferred loan fees (costs)	185	171
Other	53	171
Total deferred tax liabilities	2,487	2,878
Net deferred tax asset (liability)	**$ (785)**	**$ 1,611**

The deferred tax assets will continue to be analyzed at each reporting period for changes affecting realizability and a valuation allowance may be recorded in future periods accordingly. The ultimate realization of these deferred tax assets is primarily dependent on the generation of future taxable income during the periods in which those temporary differences become deductible. Changes in existing tax laws could also affect actual tax results and the valuation of deferred tax assets over time. The accounting for deferred taxes is based on an estimate of future results. Differences between anticipated and actual outcomes of these future tax consequences could have an impact on the Corporation's consolidated statement of income and balance sheet.

The Corporation concluded that there are no significant uncertain tax positions requiring recognition in the Corporation's consolidated financial statements based on the evaluation performed for 2014 through 2017, the years which remain subject to examination by major tax jurisdictions as of December 31, 2017. The Corporation does not expect the total amount of unrecognized tax benefits to significantly change in the next 12 months.

Note 11 – Benefit Plans

The Corporation has a noncontributory discretionary ESOP covering substantially all of its employees. It is a requirement of the plan to invest principally in the Corporation's common stock. The Corporation contributed $25 and $0 to the Plan in 2017 and 2016, respectively. Contributions are allocated to participants based on relative compensation. Total allocated shares outstanding related to the employee stock ownership plan at December 31, 2017 and 2016 were 28,777 and 30,477, respectively. Such shares are included in the computation of dividends and earnings per share in each of the respective years. Expenses related to the ESOP were $9 for both of the years ended December 31, 2017 and 2016.

The Corporation has also established a 401(k) Plan in which 100% of the employees' contribution can be matched up to 3% of their gross pay and 50% can be matched on the next 2% of their gross pay with a discretionary contribution by the Corporation. Contributions to the plan were $294 and $215 in 2017 and 2016, respectively.

The Corporation entered into Supplemental Executive Retirement Agreements (“SERP Agreements”) with certain executives. The SERP Agreements are designed to encourage executives to remain long term employees of the Corporation, and to provide specified benefits to certain key executives who contribute materially to the continued growth, development and future business success of the Corporation. The retirement benefits are an unsecured obligation of the Corporation. At year end 2017 and 2016, the accumulated liability for these plans totaled $628 and $746, respectively, and are included in accrued interest and other liabilities on the accompanying consolidated balance sheets. Expenses related to the SERP agreements were $107 and $68 for the years ended December 31, 2017 and 2016, respectively.

Note 12 - Common Stock Purchase and Option Plans

Director and Employee Plans

The Stock Purchase Plan permits directors and employees of the Corporation to purchase shares of common stock made available for purchase under the plan at the average fair value of the shares over the most recent five days prior to the issuance date. The total number of shares issuable under this plan is limited to 330,000 shares.

The Retainer Stock Plan allows directors to elect to receive shares of common stock in full or partial payment of the director's retainer fees and fees for attending meetings. The number of shares is determined by dividing the dollar amount of fees to be paid in shares by the fair value of the stock on the first business day prior to the payment date.

The Executive Stock Bonus Plan permits the administrator of the plan to grant shares of the Corporation's common stock to eligible employees. Any executive or managerial level employee is eligible to receive grants under the plan. The Board of Directors administers the plan and the numbers of shares issued are at the sole discretion of the Board of Directors. No shares were granted under the Executive Stock Bonus Plan during 2017 and 2016.

Dividend Investment Plan

The Automatic Dividend Reinvestment Plan ("DRIP") permits enrolled shareholders to automatically use dividends paid on common stock to purchase additional shares of the Corporation's common stock at its fair value on the investment date. Any shareholder who is the beneficial or record owner of not more than 9.9% of the issued and outstanding shares of the Corporation's common stock is eligible to participate in the plan.

Pursuant to a separate agreement with a family who collectively holds more than 9.9% of the Corporation's stock on or prior to January 31 of each year beginning January 31, 1997, the Corporation is to advise the family, in a written notice, of the number of shares sold under the DRIP. Each family member will have the option, until February 28 of the same year, to purchase from the Corporation one-third of the total number of shares that would be sufficient to prevent the dilution to all family members as a group that result from the DRIP shares. The purchase price under this agreement is the fair value on December 31 of the year immediately preceding the year in which the written notice is given. Similarly, a reverse agreement exists which allows the Corporation to redeem family shares to maintain the family ownership percentage in the event that stock repurchase activity more than offsets the shares available because of the DRIP.

The following summarizes shares issued under the various plans for the years ended December 31:

	2017	2016
Dividend reinvestment plan	5,751	22,263
Director and employee stock purchase and retainer stock plan	6,900	7,843
	12,651	**30,106**

Stock Option Plans

The Nonemployee Director Stock Option Plan provides for granting options to nonemployee directors to purchase the Corporation's common stock. The purchase price of the shares is the estimated fair value at the date of the grant, and there is a three-year vesting period before options may be exercised. Options to acquire no more than 8,131 shares of stock may be granted under the plan in any calendar year and options to acquire not more than 73,967 shares in the aggregate may be outstanding at any one time. No such options were granted in 2017 and 2016.

The Employee Stock Option Plan grants options to eligible employees to purchase the Corporation's common stock at or above the fair market value of the stock at the date of the grant. Awards granted under this plan are limited to an aggregate of 86,936 shares. The administrator of the plan is a committee of directors. The administrator has the power to determine the number of options to be granted, the exercise price of the options and other terms of the options, subject to consistency with the terms of the plan. No options were granted in 2017 and 2016.

The fair value of each option award is estimated on the date of grant using a closed form option valuation (Black-Scholes) model. Expected volatilities are based on historical volatilities of the Corporation’s common stock. The Corporation uses historical data to estimate option exercise and post-vesting termination behavior. The expected term of options granted is based on historical data and represents the period of time that options granted are expected to be outstanding, which takes into account that the options are not transferable. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of the grant. Shares that are issued upon option exercise come from authorized but unissued shares.

There was no stock option activity in 2017 or 2016. No options were outstanding at December 31, 2017 or 2016. As of December 31, 2017 and 2016, there was no unrecognized compensation cost related to non-vested stock options granted under the Plan.

The Corporation issued a total of 35,000 stock appreciation rights (“SARs”) to the executive management team, using a price of $2.00 per share. The terms of the SARs provided that any appreciation in stock price be paid in cash on two fixed dates which were subject to certain performance conditions, which management determined were met during 2013. SAR payment dates varied by individual agreement and ranged from February 2014 through May 2017. Expense of $0 and $17 was recorded in 2017 and 2016, respectively, resulting in a total liability of $0 and $167 at December 31, 2017 and 2016, respectively. No SARs were outstanding at December 31, 2017.

The Corporation adopted a Stock Compensation Plan in 2017 to provide for discretionary grants of restricted stock, stock options, or stock appreciation rights to certain executives. The plan’s purpose is to advance the interests of the Corporation and its stockholders by helping the Corporation and its Subsidiaries attract and retain the services of executives, upon whose judgment, initiative and efforts the Corporation is substantially dependent, and to provide those persons with further incentives to advance the interests of the Corporation. The plan is also established with the objective of encouraging stock ownership by such executives and aligning their interests with those of stockholders. There were no grants during 2017.

Note 13 – Fair Value Measurements

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values.

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity’s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Following is a description of the valuation methodologies and key inputs used to measure financial assets and liabilities recorded at fair value, as well as a description of the of the methods and significant assumptions used to estimate fair value disclosures for financial instruments not recorded at fair value in their entirety on a recurring basis. The description includes an indication of the level of the fair value hierarchy in which the assets or liabilities are classified.

Securities Available for Sale

The fair values of securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs). The remaining fair values of securities (Level 3 inputs) are based on the reporting entity's own assumptions and basic knowledge of market conditions and individual investment performance. The Corporation reviews the performance of the securities that comprise level 3 on a quarterly basis.

Interest Rate Cap

Substantially all of the derivative instruments held by the Corporation for risk management purposes are traded in over-the-counter markets where quoted market prices are not readily available. For those derivatives, the Corporation measures fair value using models that use primarily market observable inputs, such as yield curves and option volatilities, and include the value associated with counterparty credit risk. As such, the Corporation classifies those derivative instruments as Level 2.

Impaired Loans

The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

Other Real Estate Owned

Nonrecurring adjustments to certain commercial and residential real estate properties classified as other real estate owned are measured at the lower of carrying amount or fair value, less costs to sell. Fair values are generally based on third party appraisals of the property. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available, which results in a Level 3 classification. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized.

Goodwill

Goodwill is subject to impairment testing on an annual basis. The assessment of goodwill for impairment requires a significant degree of judgment. In the event the assessment indicates that it is more-likely-than-not that the fair value is less than the carrying value, the asset is considered impaired and recorded at fair value. Goodwill that is impaired and subject to nonrecurring fair value measurements is a Level 3 valuation. At December 31, 2017 and 2016, no goodwill was impaired.

Core Deposit Intangible

The core deposit intangible is recorded at fair value when initially recorded. Subsequently, core deposit intangible assets are amortized primarily on an accelerated basis over a 7 year period and are subject to impairment testing whenever events or changes in circumstances indicate that the carrying amount exceeds the fair value of the asset. If core deposit intangible asset impairment is identified, the Corporation classifies impaired core deposit intangible assets subject to nonrecurring fair value measurements as Level 3 valuations. At December 31, 2017 and 2016, there was no impairment identified for core deposit intangible assets.

Mortgage Servicing Rights ("MSRs")

MSRs originated by the Corporation and those acquired in acquisitions are accounted for under the amortization method. The fair value of these MSRs is initially estimated using a model that calculates the net present value of estimated future cash flows using various assumptions, including prepayment speeds, the discount rate and servicing costs. If the valuation model reflects a value less than the carrying value, MSRs are adjusted to fair value, as determined by the model, through a valuation allowance. The Corporation classifies the MSRs subject to nonrecurring fair value measurements as Level 3 valuations. At December 31, 2017 and 2016, there was no impairment identified for MSRs.

Assets Measured at Fair Value on a Recurring Basis

Assets measured at fair value on a recurring basis are summarized below:

	December 31, 2017			
	Total	Level 1	Level 2	Level 3
Available for sale				
U.S. Government and federal agency	$ 23,066	$ 3,981	$ 19,085	$ -
State and municipal	15,068	-	15,068	-
Mortgage backed residential	5,205	-	5,205	-
Certificates of deposit	4,440	-	4,440	-
Collateralized mortgage obligations - agencies	2,012	-	2,012	-
Equity	1,929	-	1,081	848
Total available for sale	**$ 51,720**	**$ 3,981**	**$ 46,891**	**$ 848**
Interest rate cap	**$ 69**	**$ -**	**$ 69**	**$ -**

	December 31, 2016			
	Total	Level 1	Level 2	Level 3
Available for sale				
U.S. Government and federal agency	$ 37,414	$ 13,531	$ 23,883	$ -
State and municipal	15,923	-	15,923	-
Mortgage backed residential	6,270	-	6,270	-
Certificates of deposit	4,460	-	4,460	-
Collateralized mortgage obligations - agencies	3,194	-	3,194	-
Equity	1,311	-	988	323
Total available for sale	**$ 68,572**	**$ 13,531**	**$ 54,718**	**$ 323**
Interest rate cap	**$ 142**	**$ -**	**$ 142**	**$ -**

The table below presents a reconciliation and income statement classification of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended December 31:

	2017	2016
Balance, January 1	$ 323	$ 391
Included in net income	-	-
Included in other comprehensive income	525	(68)
Balance, December 31	**$ 848**	**$ 323**

Assets Measured at Fair Value on a Non-Recurring Basis

Assets measured at fair value on a non-recurring basis are summarized below:

	December 31, 2017			
	Total	Level 1	Level 2	Level 3
Impaired loans				
Commercial	$ -	$ -	$ -	$ -
Commercial real estate	-	-	-	-
Residential real estate	198	-	-	198
Home equity	-	-	-	-
Installment	-	-	-	-
Total impaired loans	$ 198	$ -	$ -	$ 198

	December 31, 2016			
	Total	Level 1	Level 2	Level 3
Impaired loans				
Commercial	$ 12	$ -	$ -	$ 12
Commercial real estate	1,551	-	-	1,551
Residential real estate	208	-	-	208
Home equity	-	-	-	-
Installment	-	-	-	-
Total impaired loans	$ 1,771	$ -	$ -	$ 1,771

The following represent impairment charges recognized during the years ended December 31, 2017 and 2016:

Impaired loans that are measured for impairment using the fair value of discounted cash flows had a carrying amount of $241, with a valuation allowance of $43 at December 31, 2017. Impaired loans that are measured for impairment using the fair value of the collateral had a carrying amount of $2,055, with a valuation allowance of $284 at December 31, 2016.

Other real estate owned (a Level 3 fair value instrument) which is measured at the lower of carrying value or fair value less costs to sell, had a net carrying amount of $92, which was carried at fair value at December 31, 2017, as a write-down of $46 was taken during 2017. Other real estate owned which is measured at the lower of carrying value or fair value less costs to sell, had a net carrying amount of $250, none of which was at fair value at December 31, 2016, as no write-downs were taken during 2016.

Qualitative information about level 3 fair value instruments is as follows as of:

	December 31, 2017				
	Fair Value		Valuation Technique	Unobservable Input	Weighted Average
Equity securities	$	848	Market Comparable	Price to Book Ratio	70.00%
Impaired loans	$	198	Discounted Cash Flows	Discount Rate	7.10%
Other real estate owned	$	92	Appraisal Value - Real Estate	Discount Applied to Appraisal	20.00%

	December 31, 2016				
	Fair Value		Valuation Technique	Unobservable Input	Weighted Average
Equity securities	$	323	Market Comparable	Price to Book Ratio	77.40%
Impaired loans	$	1,771	Appraisal Value - Real Estate	Discount Applied to Appraisal	7.60%

Carrying amount and estimated fair value of financial instruments, not previously presented, at year end were as follows:

	2017		2016	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets				
Cash and cash equivalents	$ 15,928	$ 15,928	$ 78,313	$ 78,313
Securities held to maturity	$ 3,603	$ 3,567	$ 3,886	$ 3,802
Loans held for sale	$ 2,067	$ 2,067	$ 3,869	$ 3,869
Net loans (including impaired loans)	$ 668,927	$ 670,450	$ 512,924	$ 507,616
FHLB stock	$ 2,925	$ 2,925	$ 1,774	$ 1,774
Accrued interest receivable	$ 2,393	$ 2,393	$ 1,896	$ 1,896
MSRs	$ 3,043	$ 3,120	$ 2,390	$ 2,499
Liabilities				
Deposits	$ 673,505	$ 672,899	$ 603,367	$ 603,088
FHLB advances	$ 30,000	$ 29,039	$ 30,000	$ 29,649
Subordinated debentures	$ 14,000	$ 14,000	$ 14,000	$ 14,000
Federal funds purchased	$ 2,000	$ 2,000	$ -	$ -
Senior debt	$ -	$ -	$ 1,000	$ 1,000
Accrued interest payable	$ 249	$ 249	$ 180	$ 180

The following methods and assumptions were used by the Corporation in estimating its fair value disclosures for financial instruments:

Cash and Cash Equivalents

The carrying amounts reported in the consolidated balance sheets for cash and short-term instruments approximate their fair values.

Securities Held to Maturity

Fair values for securities held to maturity are based on similar information previously presented for securities available for sale.

Loans Held for Sale

The fair values of these loans are determined in the aggregate on the basis of existing forward commitments or fair values attributable to similar loans.

FHLB Stock

It was not practical to determine the fair value of FHLB stock due to restrictions placed on its transferability.

Loans

For variable rate loans that re-price frequently and with no significant change in credit risk, fair values are based on carrying values. The fair value of other loans is estimated using discounted cash flow analysis.

Accrued Interest

The carrying amount of accrued interest approximates its fair value.

Off-Balance-Sheet Instruments

The fair value of off-balance sheet items is not considered material.

Deposits

The fair values disclosed for demand deposits are, by definition, equal to the amount payable on demand at the reporting date. The carrying amounts for variable rate, fixed term money market accounts and certificates of deposit approximate their fair values at the reporting date. Fair values for fixed certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on similar certificates.

FHLB Advances

Rates currently available for FHLB advances with similar terms and remaining maturities are used to estimate the fair value of the existing obligations.

Subordinated Debentures

The estimated fair value of the existing subordinated debentures is calculated by comparing a current market rate for the instrument compared to the book rate. The difference between these rates computes the fair value.

Senior Debt

The estimated fair value of the existing senior debt is calculated by comparing a current market rate for the instrument compared to the book rate. The difference between these rates computes the fair value.

Limitations

Fair value estimates are made at a specific point in time, based on relevant market data and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Corporation's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Corporation's financial instruments, fair value estimates are based on management's judgments regarding future expected loss experience, current economic conditions, risk characteristics and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Note 14 – Accumulated Other Comprehensive Income (Loss)

The following table presents a reconciliation of the changes in the components of accumulated other comprehensive income and details the components of other comprehensive income for the years ended December 31, 2017 and 2016, including the amount of income tax (benefit) expense allocated to each component of other comprehensive income:

	2017	2016
Accumulated net unrealized gains on investment securities available-for-sale		
Balance at beginning of year, net of tax	$ 106	$ 179
Net unrealized holding gains (losses) arising during the year	527	(110)
Income taxes	16	37
Reclassification resulting from enactment of the Tax Act	1	-
Net unrealized holding gains (losses) arising during the year, net of tax	**544**	**(73)**
Balance at end of year, net of tax	**650**	**106**
Accumulated net losses on cash flow hedge		
Balance at beginning of year, net of tax	(333)	(301)
Net cash flow hedge gains (losses) arising during the year	98	(49)
Income taxes	(32)	17
Reclassification resulting from enactment of the Tax Act	(53)	-
Net cash flow hedge gains (losses) arising during the year, net of tax	**13**	**(32)**
Balance at end of year, net of tax	**(320)**	**(333)**
Accumulated other comprehensive income (loss) at end of year, net of tax	**$ 330**	**$ (227)**

In accordance with the Tax Act, the effect of income tax law changes on deferred taxes also applies to items recognized in other comprehensive income. In February 2018, the FASB issued ASU 2018-02 which allowed for the “stranded” tax effects in AOCI to be reclassified to retained earnings rather than charged to income tax expense. The Corporation early adopted this guidance and applied this accounting alternative in the consolidated statements of shareholders’ equity as of December 31, 2017.

Note 15 – Regulatory Matters

The Corporation and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory - and possibly discretionary - actions by regulators that, if undertaken, could have a direct material effect on the Corporation and the Bank. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Corporation and the Bank must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance-sheet items that are calculated under regulatory accounting practices. The capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Failure to meet capital requirements can initiate regulatory action. The final rules related to the implementation of the Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Corporation and the Bank on January 1, 2015, with full compliance of all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. The capital conservation buffer was 1.250% and 0.625% as of December 31, 2017 and 2016, respectively. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital.

Quantitative measures established by regulation to ensure capital adequacy require the Corporation and the Bank to maintain minimum amounts and ratios (set forth in the table below). As of December 31, 2017 and 2016, the most recent notifications from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. Management believes, as of December 31, 2017 and 2016, that the Corporation and the Bank met all capital adequacy requirements to which they are subject. There are no conditions or events since the notifications that management believes have changed the Corporation and the Bank's category.

The Corporation's principal source of funds for dividend payments is dividends received from the Bank. Banking regulations limit the amount of dividends that may be paid without prior approval of regulatory agencies.

The tables below illustrate the regulatory capital amounts and ratios for the Corporation and The State Bank as of:

	December 31, 2017					
	Actual		Minimum Capital Requirement		Minimum to be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital to risk weighted assets						
The Corporation	$ 72,303	10.932%	$ 61,176	9.250%	N/A	N/A
The State Bank	69,124	10.460%	61,130	9.250%	66,086	10.00%
Tier 1 capital to risk weighted assets						
The Corporation	68,700	10.388%	47,949	7.250%	N/A	N/A
The State Bank	65,521	9.914%	47,913	7.250%	52,869	8.00%
Common Tier 1 capital to risk weighted assets						
The Corporation	54,700	8.271%	38,028	5.750%	N/A	N/A
The State Bank	65,521	9.914%	38,000	5.750%	42,956	6.50%
Tier 1 capital to average assets[1]						
The Corporation	68,700	8.981%	61,197	8.000%	N/A	N/A
The State Bank	65,521	8.571%	61,157	8.000%	61,157	8.00%

	December 31, 2016					
	Actual		Minimum Capital Requirement		Minimum to be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital to risk weighted assets						
The Corporation	$ 63,004	11.483%	$ 47,323	8.625%	N/A	N/A
The State Bank	61,610	11.239%	47,280	8.625%	54,817	10.00%
Tier 1 capital to risk weighted assets						
The Corporation	60,153	10.963%	36,350	6.625%	N/A	N/A
The State Bank	58,759	10.719%	36,316	6.625%	43,854	8.00%
Common Tier 1 capital to risk weighted assets						
The Corporation	46,153	8.412%	28,119	5.125%	N/A	N/A
The State Bank	58,759	10.719%	28,094	5.125%	35,631	6.50%
Tier 1 capital to average assets(1)						
The Corporation	60,153	11.951%	40,268	8.000%	N/A	N/A
The State Bank	58,759	11.685%	40,228	8.000%	40,228	8.00%

(1) The minimum capital requirements and minimum to be well capitalized under prompt corrective action represent the minimum capital requirements set forth in the regulatory approval for the acquisition of the Community in 2016.

Note 16 – Loan Commitments and Other Related Activities

Off-Balance-Sheet Risk

Some financial instruments, such as loan commitments, credit lines, letters of credit, and overdraft protection, are issued to meet customer financing needs. These are agreements to provide credit or to support the credit of others, as long as conditions established in the contract are met, and usually have expiration dates. Commitments may expire without being used. Off-balance-sheet risk to credit loss exists up to the face amount of these instruments, although material losses are not anticipated. The same credit policies are used to make such commitments as are used for loans, including obtaining collateral at exercise of the commitment.

The contractual amount of financial instruments with off-balance-sheet risk was as follows at:

	December 31	
	2017	2016
Commitments to make loans (at market rate)	$ 39,693	$ 43,430
Unused lines of credit and letters of credit	147,746	69,283

Commitments to make loans are generally made for periods of 90 days or less.

Note 17 – Contingencies

Litigation

The Corporation is party to litigation arising during the normal course of business. In the opinion of management, based on consultation with legal counsel, the resolution of such litigation is not expected to have a material effect on the consolidated financial statements.

Environmental Issues

As a result of acquiring real estate from foreclosure proceedings, the Corporation is subject to potential claims and possible legal proceedings involving environmental matters. No such claims have been asserted as of December 31, 2017.