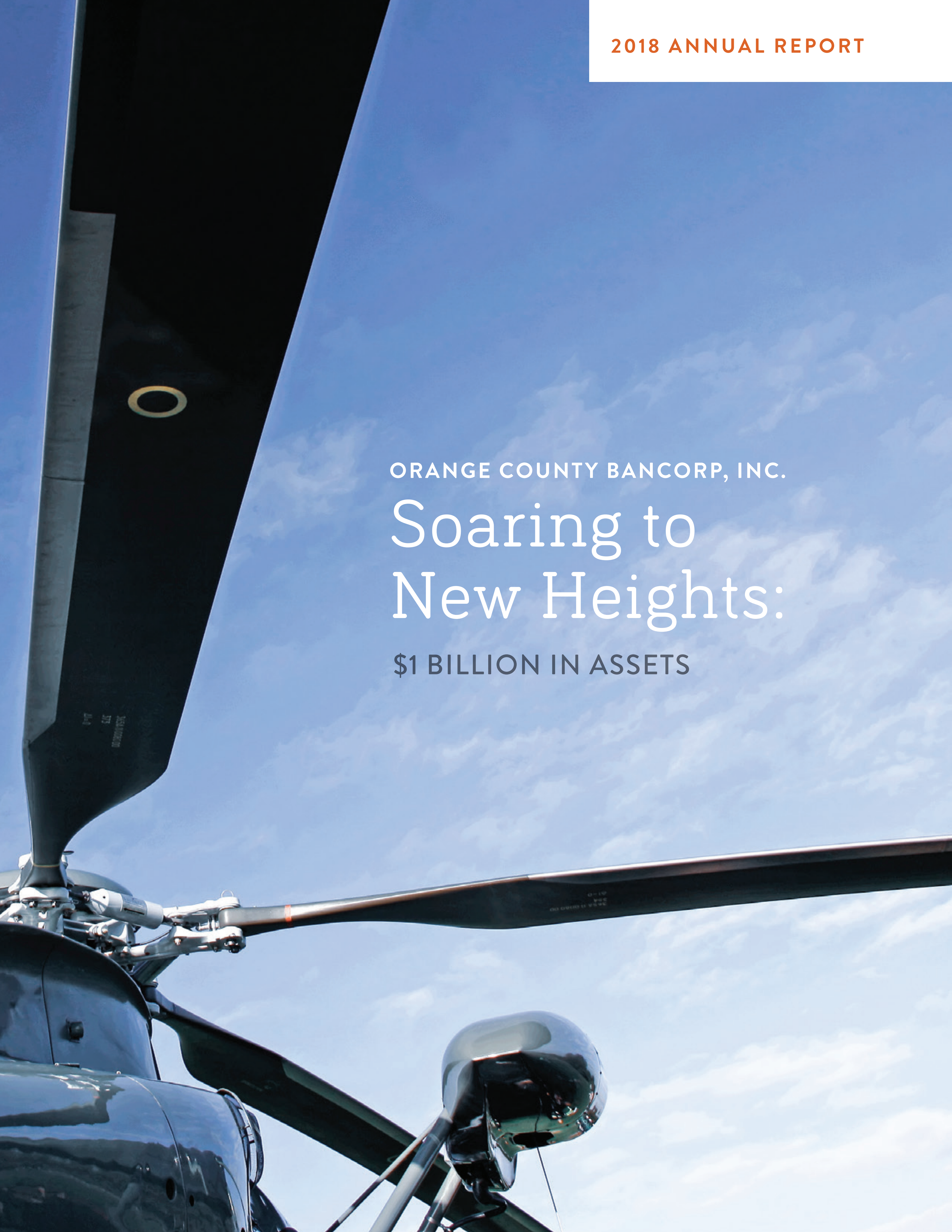
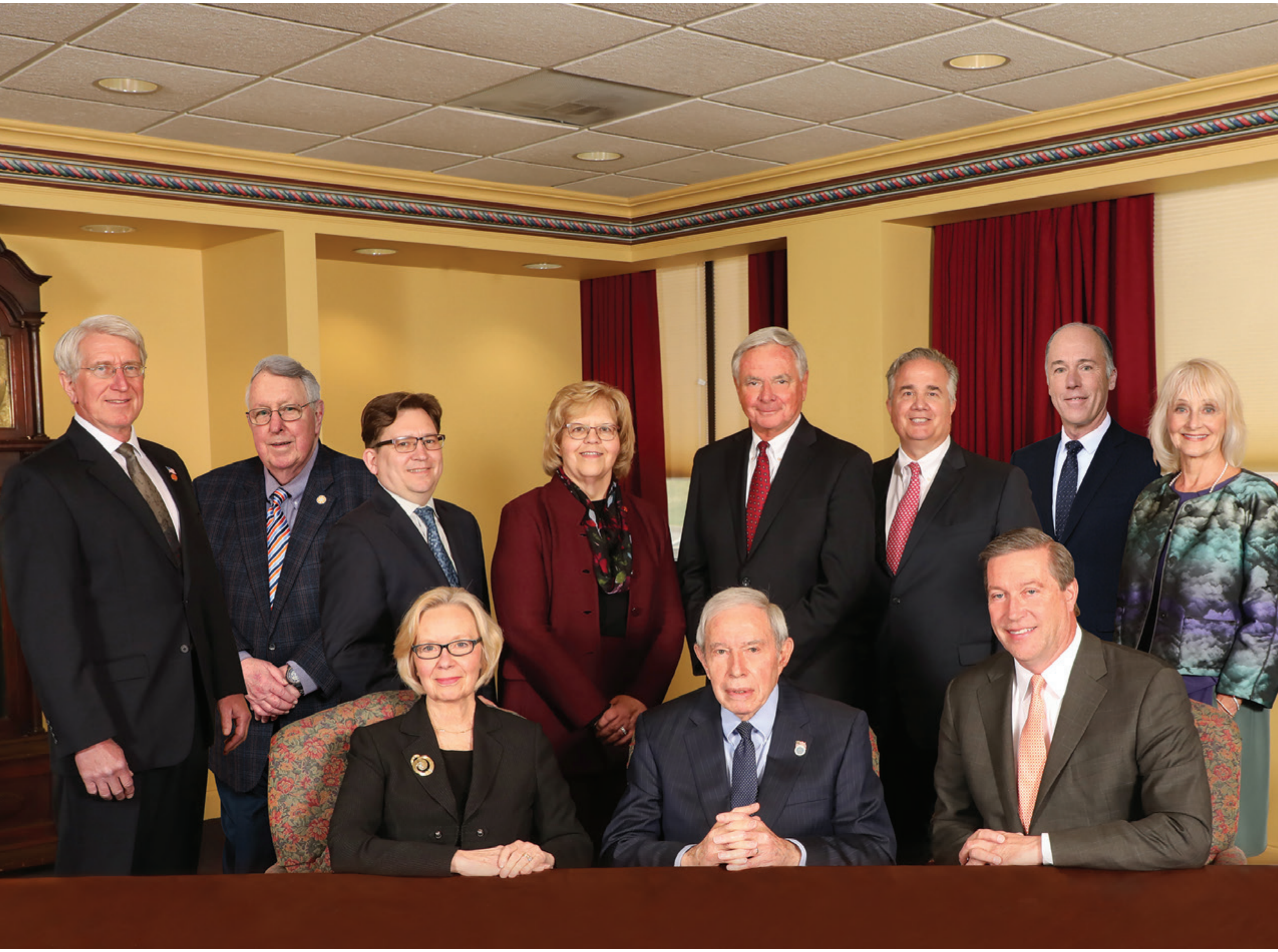
2018 ANNUAL REPORT

ORANGE COUNTY BANCORP, INC.

Soaring to New Heights:

$1 BILLION IN ASSETS



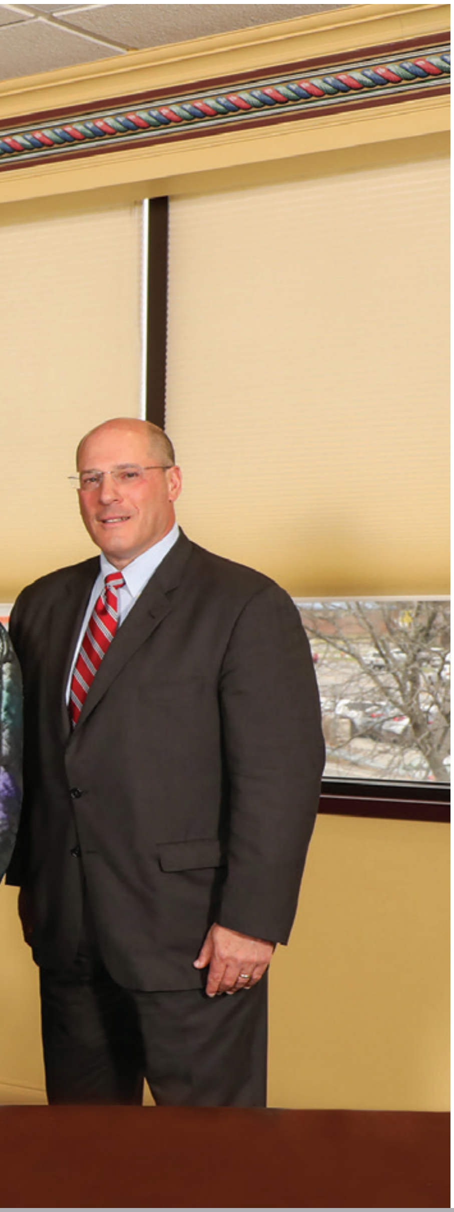


Board of Directors

PICTURED FROM LEFT TO RIGHT.

FRONT ROW: Susan Metzger, Louis Heimbach, Chairman, Michael Gilfeather

BACK ROW: William D. Morrison, David A. DeWilde, Jonathan Rouis, Terry R. Saturno, Paul T. McDermott, Greg Holcombe, Richard Rowley, Virginia Rizzo, Gus Scacco



Member

Federal Reserve System
Federal Home Loan Bank
Federal Deposit Insurance Corporation
Financial Industry Regulatory Authority

Subsidiaries

Orange Bank & Trust Company ("Bank")
Hudson Valley Investment Advisors, Inc. ("HVIA")

Shares of Orange County Bancorp, Inc. stock are available under stock

SYMBOL OCBI

For information regarding stock transfers and other transactions, contact our Transfer Agent:

Computershare, Inc.
250 Royall Street, Canton, MA 02021
1.800.368.5948
web.queries@computershare.com

For more information about purchasing stock,
contact either:

STIFEL NICOLAUS & CO. INC.
Andrew Lieb: 800.342.2325 Ext. 4128

FIG PARTNERS, LLC
Dan Flaherty: 404.601.7200

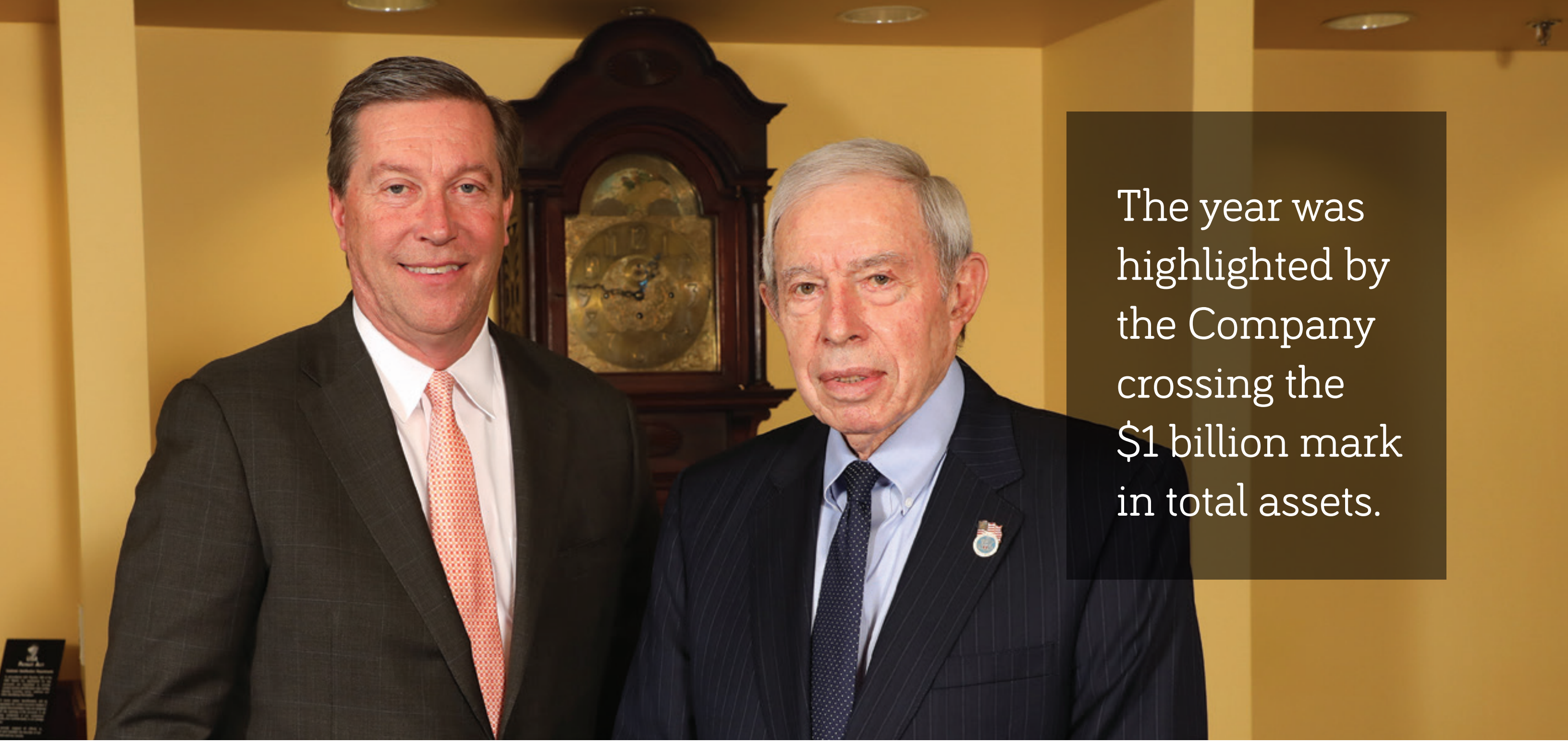
SANDLER O'NEILL + PARTNERS
Jerome (Jace) Day, Jr: 212.466.7831

Notice to Shareholders

ANNUAL DISCLOSURE STATEMENT

Financial information about the Bank is available to our customers and the general public upon request. In accordance with the federal regulation to facilitate more informed decision-making by depositors, investors, and the general public, we will provide an ANNUAL DISCLOSURE STATEMENT containing financial information for the Bank for the previous two years. This information will be updated annually and available as of June 1, each year.

To obtain a copy of the ANNUAL DISCLOSURE STATEMENT, please contact:
Robert Peacock, EVP Chief Financial Officer
Orange Bank & Trust Company • 212 Dolson Avenue • Middletown, New York 10940



The year was highlighted by the Company crossing the $1 billion mark in total assets.

Letter from the President & Chairman

To Our Shareholders, Clients and Friends:

We are delighted to share our 2018 results, which reflect our banking leadership in the markets we serve. Our commitment to reinvest customer deposits into the local economy, in the form of loans, is a matter we take great pride in. It also results in the Bank playing an important role in the success of our customers and the communities they and we call home.

As with 2017, the past year was a busy and highly productive one, with growth initiatives we have been engaged in continuing to gain traction with customers across the counties we serve; Orange, Rockland and Westchester. During the year we opened two new branches in Westchester County, one in Cortlandt Manor, and another in Thornwood. In addition to these and the hiring of related personnel, our concierge level Private Banking initiative, introduced in Orange County in late 2017, continued to resonate with customers. We have secured over 200 clients and $57 million in net new money via the program since its introduction.

In 2018, loans to our business clients grew $153 million or 29%. Business lending was identified as a key growth driver for the Bank during strategic planning several years ago as we determined our 125+ years of experience could best be leveraged through robust support of the businesses in our communities. We are happy to report that not only did business loan volume increase in 2018 as a result of initiatives stemming from this effort, but we also crossed the $1 billion mark in total assets. This was an aggressive benchmark we set for the bank several years ago, and represents a nearly $300 million (76%) increase in assets since 2015. We did this while maintaining the same conservative underwriting standards that have served the Bank well over time. (If 125 years has taught us anything, it's that loans are easy to make, but good loans require rigorous lending standards, knowledge of your customer, and diligent monitoring).

The extension of credit requires capital, with deposits serving as the primary source of financing for bank lending. Business checking and escrow accounts are the key drivers of core deposits, without which growth in our loan portfolio would not be possible. To support the significant loan growth the Bank experienced in 2018, deposits grew an equally impressive $72 million, or approximately 9%. These deposits were acquired organically, and are a highly cost effective source of funds.

In addition to deposit growth, we also secured external financing in 2018 to support the investment opportunities we've identified. In October, we announced the close of a private placement of $16.4 million of the Company's common stock through the sale of 566,783 shares to accredited investors at an offering price of $29.00 per share. True to our community bank roots, support for the transaction came primarily from Company "friends and family" – our clients and colleagues.

The offering followed a 2-for-1 stock split approved by the Board earlier in the year. This corporate action stemmed from ongoing efforts to improve the liquidity and valuation of our stock, as well as fund the Bank's growth. We believe the combination of this stock split, which served to double our total shares outstanding, the addition of new shares via the aforementioned sale and recent announcement of our move to the OTCQX Best Market, should improve the trading liquidity of our stock and potentially lead to higher assessed value in the market. These are, of course, only measured steps in our strategic efforts, but we view them as among various initiatives reflecting our appreciation of and commitment to improving shareholder value.

Although the extension of credit and provision of a safe place for deposits – the services we know as "banking" today – have always been central to our business, the word "bank" was not initially in our name. Founded as the Orange County Trust and Safe Deposit Company in 1892, trust services held a prominent role among our lines of business. This has evolved through intervening years, most explicitly in a name change to Orange County Trust Company in 1905, and it remains a vital and vibrant part of our business to this day. As a measure of our ongoing commitment to trust services, we hired dedicated personnel with expertise in the unique requirements of the Special Needs Trust sub-sector for oversight of the division several years ago. The investment has served us well, with net fee income more than doubling since 2015 to $2.3 million and the division adding $61 million in client relationships, primarily in Special Needs Trust Services, in 2018. We expect the group to remain a foundational pillar of our business going forward.

The last of our core businesses, critical to both our Private Bank initiative and commitment to client service and product diversification, is our investment management platform, Hudson Valley Investment Advisors, Inc. (HVIA). The group showed strong operating performance in 2018, with an ROE of 15.64% and a record year of new investment flows of over $37MM.

Thanks to positive contributions from each of our principal business groups, we are pleased to report the bank earned $7.55 million in 2018, up $5.2 million, or 212%, over the prior year's earnings of $2.35 million.

Our reported results would not have been possible or sustainable without the significant investment we have made in people. Most notably, Robert Peacock joined the Bank in 2018 as Executive Vice President and Chief Financial Officer. Robert brings extensive experience and expertise in financial management and strategic planning, which he has already put to use in thoughtful analysis and support of our efforts.

We want to thank our clients, shareholders, directors, and employees for their patience and support as we have invested in and executed our growth strategy over the past several years. Our 2018 results reflect the benefits of these plans taking hold. On behalf of all our employees and Board members, we appreciate your confidence and commit ourselves to continuing to build and strengthen the Company in the year ahead. From our perspective, we are just getting started!

Sincerely,

Michael Gilfeather	Lou Heimbach
President & CEO	Chairman

The Company is the parent organization for Orange Bank & Trust Company (the "Bank") and Hudson Valley Investment Advisors, Inc. ("HVIA"). Together, the Bank and HVIA are the principal drivers of revenue for the Company and their results are fully consolidated into the Company's financials as reflected in the accompanying statements.

Orange County Bancorp, Inc.
Performance Highlights

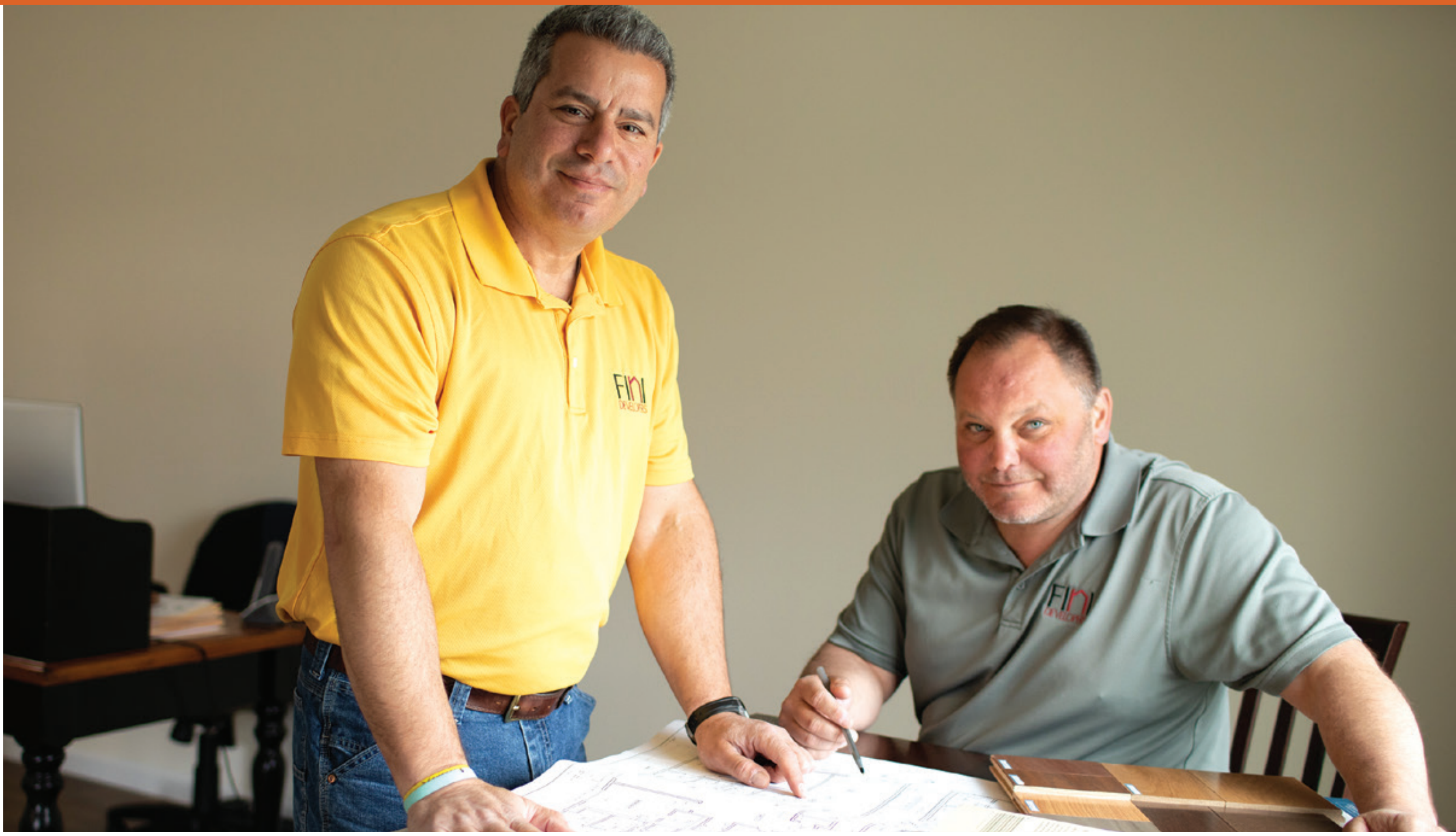
PRE-TAX INCOME:
IMPROVED 41%
TO $9.2 MILLION
Core Activity in all areas improved

TOTAL ASSETS:
INCREASED
$104 MILLION
TO $1.06 BILLION

TOTAL PORTFOLIO LOANS:
GREW $160 MILLION
TO $737 MILLION
The Percentage of non-accruing loans in portfolio improved from 0.4% in 2017 to 0.37% in 2018

DEPOSIT GROWTH*:
GREW $72 MILLION
TO $905 MILLION
Non-interest bearing deposits up by $39 million

Orange Bank & Trust Supports Local Business, Building a Strong Marketplace



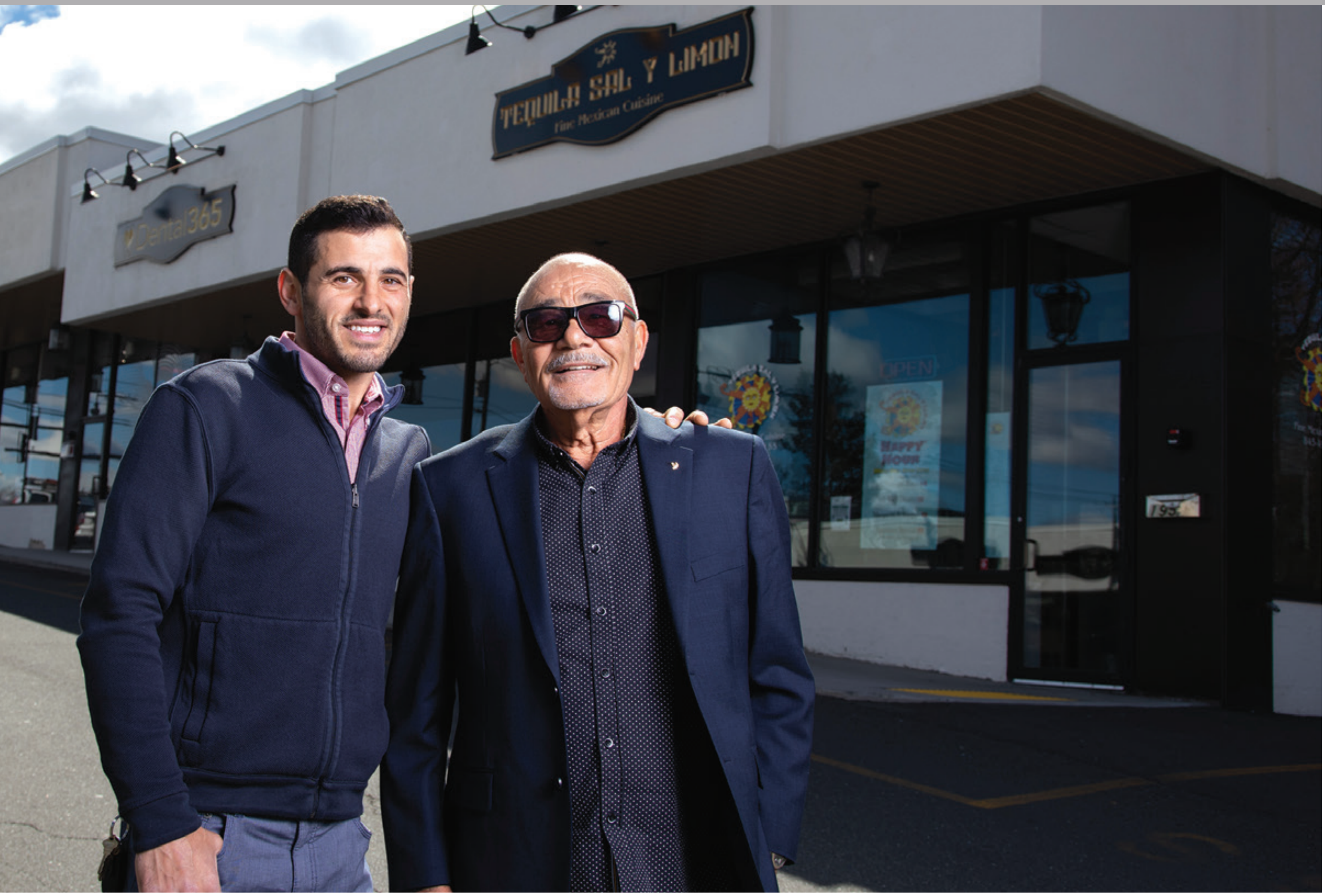
Fini Developers—A Passion for Construction and the Community

Al and Tom Fini had a construction destiny. They grew up in the family construction business with their fathers and uncles. With a Bachelors degree in Construction Management and 10 years experience already behind them, Al and Tom went off on their own and formed Fini Developers Inc.

They specialized in single and multi-family homes and excavating. In 2006 "the worst housing economy, ever," caused their bank to stop funding construction. Al tried Orange Bank & Trust Company. He says, "They believed in me, gave us a lifeline, and allowed me to thrive. They really became my partner and I'll never forget that."

Like Orange Bank & Trust Company, he believes in community service, and in the last seven years he has helped raise over $1,250,000 to combat Rett Syndrome. Al and Tom look forward to remaining a building leader in the region and continuing the Fini tradition of quality, well built homes and developments. They also look forward to passing on the traditions and work ethic they learned to their own kids who may someday become part of the Fini Developers team.

"...They really became my partner and I'll never forget that."



FTG Realty–An Entrepreneurial Spirit from One Generation to the Next

Frank Battaglia's father arrived from Italy in the 1970s with $200, his wife and a dream. He opened a butcher shop, which morphed into six apartment units and by the 1990s he had 60 units. Frank was born into the business and raised to be an entrepreneur—going to work with his father every Saturday.

In 2007, Frank took the opportunity to prove himself in the business when more apartments, a barber shop, and a gourmet mini-market joined the portfolio. Frank says the mini-market was his college education, a blessing and the hardest thing he's ever done. Realizing that real estate is "where it is at," Frank sought a banking partner to fund expansion and found Orange Bank & Trust to be the best fit—an "unbelievable" relationship. Frank praises Orange Bank & Trust as being, "Nothing but kind and more friends than bankers." He adds that he is learning the banking business from Orange Bank & Trust and that he knows the relationship is for the long term. What would he tell a businessperson looking for a bank? "I have a wonderful bank for you!"

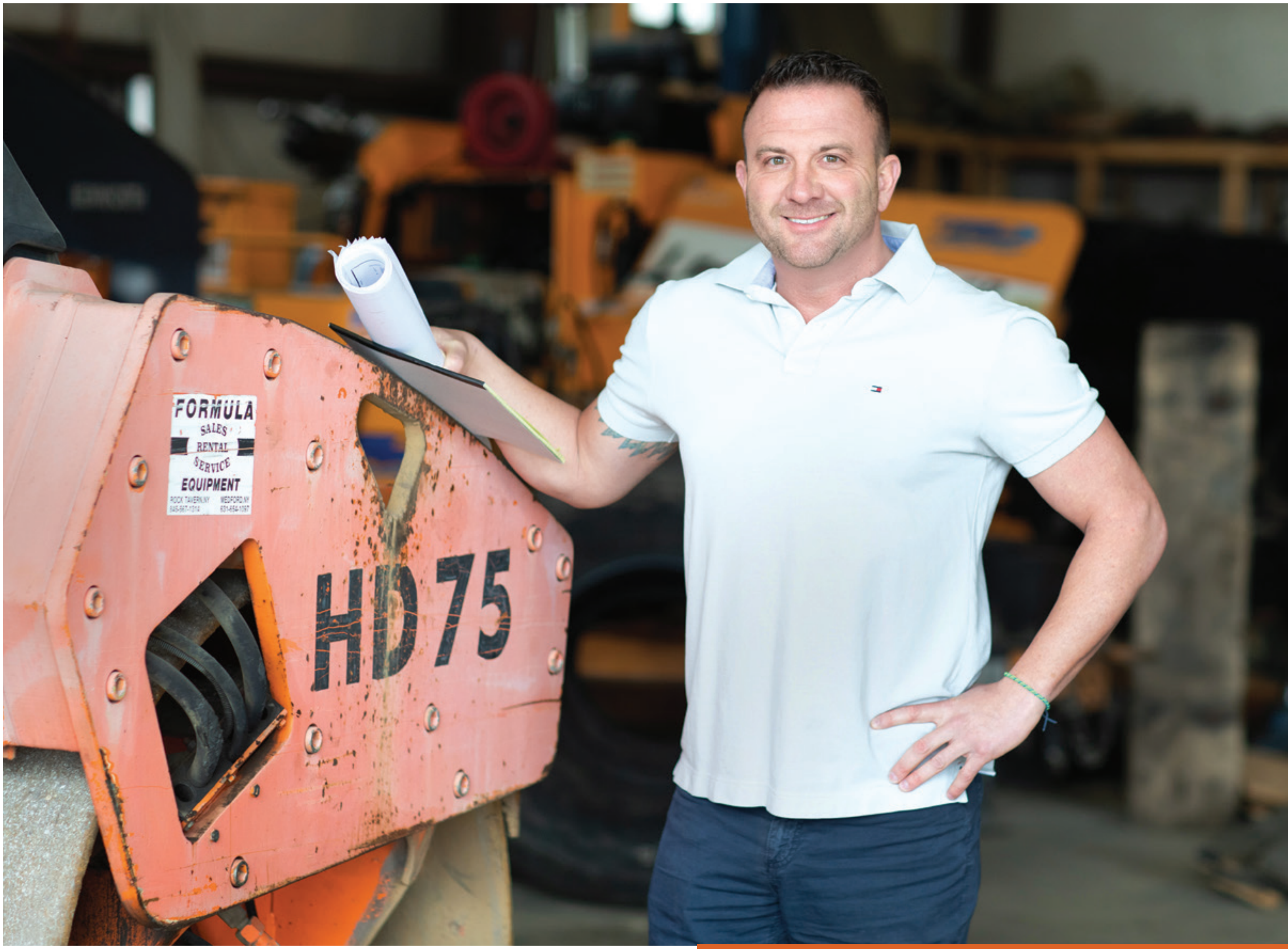
> "...Orange Bank & Trust is nothing but kind and more friends than bankers."

Todd Lyons Paving–A Love of the Outdoors and Construction Paves the Road to Success

Todd Lyons studied Criminal Justice in college, but he liked working outside and seeing things happen. In 2004, at the age of 23, he started his paving firm and began to grow. In 2007, when his current bank wasn't cooperative, he moved to Orange Bank & Trust and began to really expand his business. Todd says Orange Bank & Trust was there for him from the beginning of the relationship and remains a valued partner because we know what his needs are, stay on top of things, and understand what it takes to be successful.

What it takes to be successful, Todd adds, is that partnership—always being there when needed. Todd makes good use of Orange Bank & Trust Business Banking and is a big fan of Orange Bank & Trust Private Banking. "Orange Bank & Trust got me to where I am now," he says, "and are instrumental to my continued success."

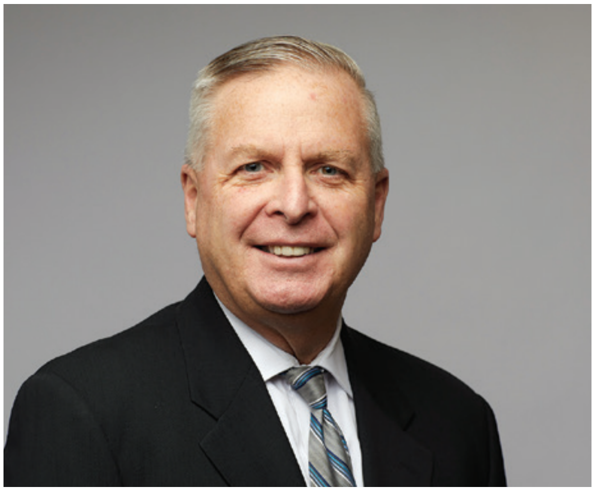
> "...Orange Bank & Trust is instrumental to my continued success."



Value-Added Financial Services Grow the Bank's Bottom Line

To increase shareholder value we need to earn our customers' trust. We do that by tailoring financial services that help meet their business and personal financial goals. Three of our divisions—**Private Banking**, **Trust Services** and **Hudson Valley Investment Advisors** do just that.

Private Banking Sees Positive Growth in First Full Year.



Managing Director Tim McCausland led The Private Banking team to significant growth and positive financial results in 2018 after launching the service in the second half of 2017. It is poised to contribute significantly to the bottom line of the Company and now serves over 200 clients. Operated as a division of the Bank, Orange Private Banking is a client-driven service model that offers the Bank's clients a high-touch level of attention across four business lines including:

- Cash Management/Treasury (Deposit Products)
- Loans (both Commercial and Residential)
- Trust, Estate and Custody Services
- Investment Advisory (through HVIA)

The primary goal of Private Banking is to deliver a level of service to our clients that is both valuable and memorable. In doing so, we anticipate that our clients will remain loyal and expand their relationship with the organization. By focusing on service and "quarterbacking" all the Bank's capabilities, Private Banking differentiates itself from the competition with resources and a level of service that cannot be surpassed.

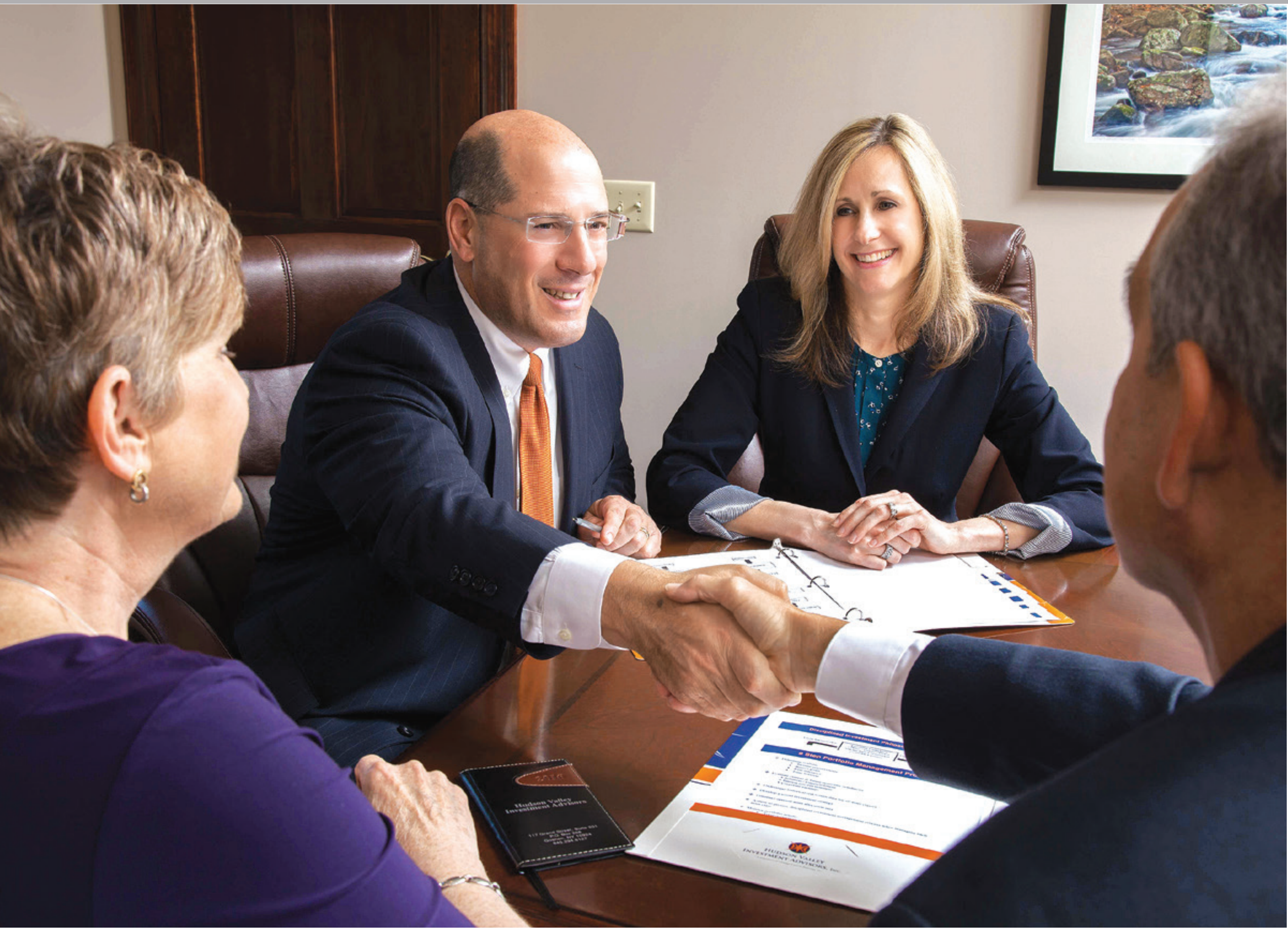
Private Banking was created with the idea that our clients deserve a higher level of service. This is not a new or novel concept. But, only through execution, client engagement, and a continuing dedication to the standards we set for ourselves will our clients experience the benefits of their Private Banking relationship.

> Orange Private Banking now serves over 200 clients.

Trust Services Grows 7% in 2018

The Trust Services Division continued its trend of strong growth in 2018, ending the year at $421 million, representing a 7% increase over year end 2017. Under the watchful eye of SVP and Trust Services Director, Kathryn Maloney, the Division added $61 million in new client relationships, with a high concentration in the areas of Special Needs Trusts, Court Appointed Trusts and Guardianships. The Westchester Division, opened in 2016, expanded to $104 million in client assets and contributed 28% of the Division's gross income in 2018. Gross and net revenue for the Division, exceeded budgeted goals and made a significant contribution to the non-interest income of the Bank.

The Trust Division added $61 million in new client relationships.



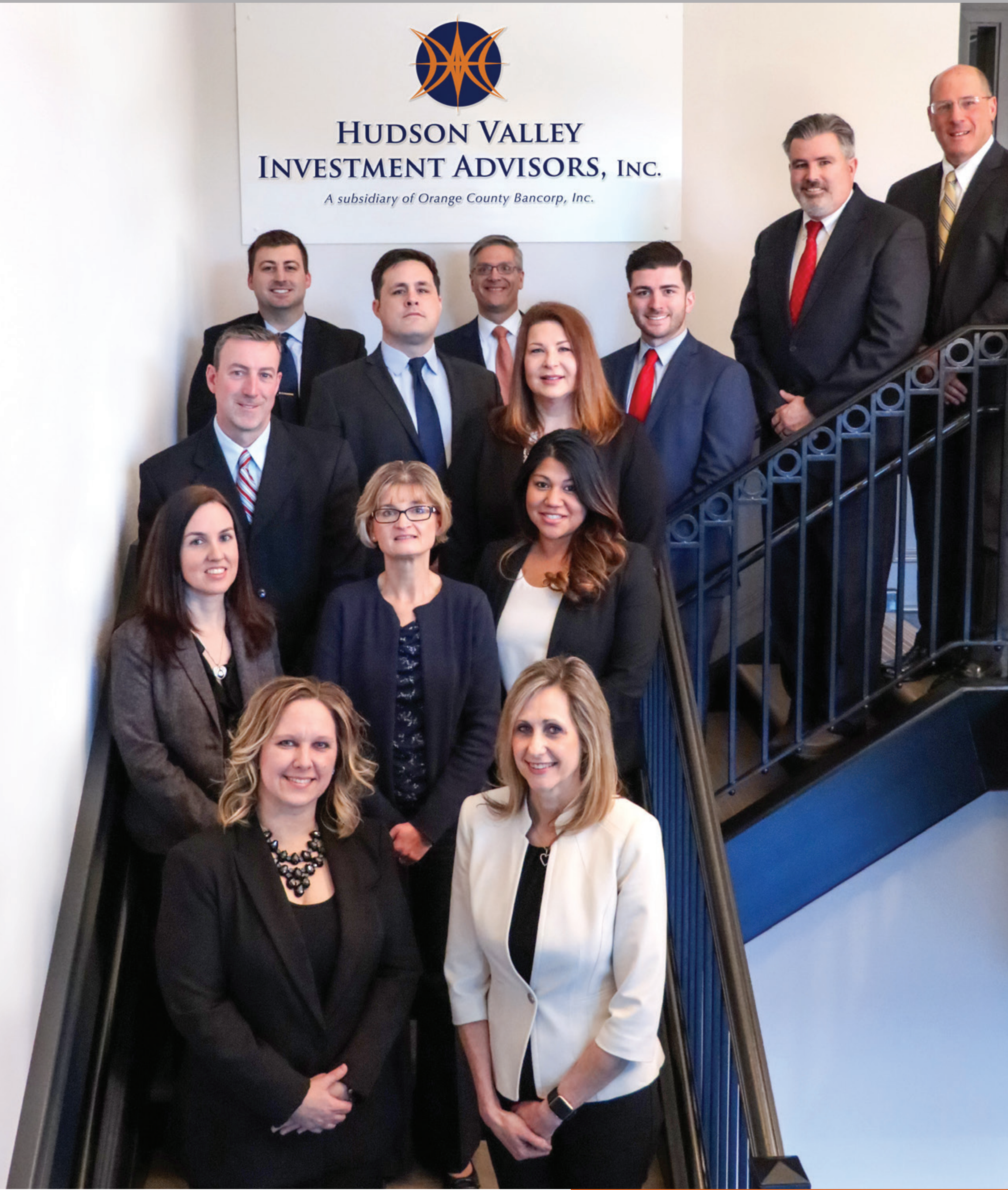
Record New Asset Growth for Hudson Valley Investment Advisors

Working closely with the Bank's Trust Services Division and Orange Private Banking, our subsidiary Hudson Valley Investment Advisors (HVIA), saw solid operating performance in 2018 with assets under management over $750 million and a record year of investment inflows. As the Bank continues its growth trajectory by expanding its footprint into new markets, HVIA expanded too, opening a new office in Westchester's White Plains.

Marketing outreach continued as well in 2018 as **CEO Gus Scacco** was a frequent guest of Fox Business News' *National Business News* program. The division also continued to expand its website to include educational videos on investing, and other topical economic and financial information.

In 2019 HVIA is poised for more growth through a combination of strategic marketing moves and partnerships including television advertising to its marketing channels, a focus on attracting more institutional investors, and providing monthly economic updates to Orange County and surrounding areas.

HVIA is expanding its footprint into new markets.


HUDSON VALLEY
INVESTMENT ADVISORS, INC.
A subsidiary of Orange County Bancorp, Inc.

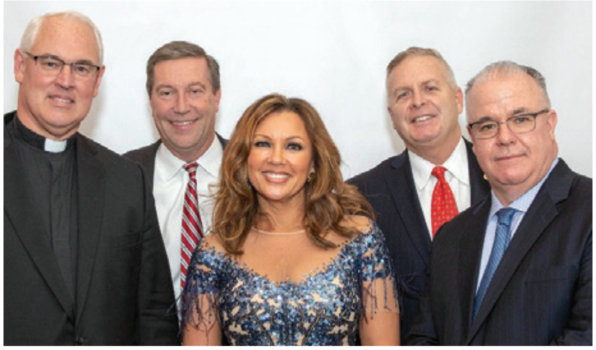
Investing in Our Community

Since our early beginnings 126 years ago, the Bank has been actively engaged in strengthening and supporting the people and organizations that bring out the best in us all. In 2018, whether financially, or through the time and talent our employees lend, Orange Bank & Trust joined in the efforts of these community service organizations:

Feeding Westchester

Feeding Westchester hosted its first-ever Holiday Hop Pack-A-Thon and Orange Bank & Trust took part in the friendly food packing competition. Our employees helped package nearly 24,000 pounds of sweet potatoes in time for Thanksgiving. We proudly stand shoulder to shoulder with Feeding Westchester in the fight against hunger to help feed their 200,000 neighbors including 60,000 children struggling with hunger in Westchester County.

> Our employees helped package nearly 24,000 sweet potatoes in time for Thanksgiving.



San Miguel Academy of Newburgh

We partnered with San Miguel Academy of Newburgh to host a Holiday Benefit Concert by Vanessa Williams at the Chappaqua Performing Arts Center. The proceeds of the event support at-risk boys from the city of Newburgh and puts them on a 12-year education path to success. Additionally, we supported San Miguel's 2018 Annual Scholarship Dinner.

United Way of Dutchess-Orange

In 2018, the Bank had a record amount of employee pledges to the United Way of Dutchess-Orange Campaign. We achieved our goal, raising $25,922. In addition, the Bank committed a Corporate Gift of $3,818 and $500 in "In-Kind" food drive, which brought our total contribution to $30,240. United Way fights for the health, education, and financial stability of every person in our community. They serve as a catalyst to increase the community's capacity to improve the lives of its citizens. United Way helps more than 101,000 individuals each year.

> We had a record amount of employee pledges to the United Way...

Junior Achievement

Junior Achievement is the world's largest organization dedicated to giving young people the knowledge and skills they need to own their economic success, plan for their future and make smart academic and economic choices. The Junior Achievement program partners with businesses, educators, and volunteers to directly reach the students in an environment conducive to education and learning. In 2018 Orange Bank & Trust employees took part in "JA in a day," and worked with over 225 students at Goshen Intermediate School.

> Our employees worked with over 225 students at Goshen Intermediate School

The Center for Safety & Change

The Center for Safety & Change endeavors to end gender-based violence and provide shelter and supportive services to empower survivors of domestic violence, sexual abuse and other crimes. Their vision is to help create a society in which all individuals can live with dignity and equality, free from fear, violence and oppression. Center for Safety & Change provides services to domestic violence victims and their families both in person at one of their six office locations and by telephone. Domestic violence victims with special circumstances may receive services at other safe locations of their choice. In 2018 the bank supported their annual 'A Night for Change' event along with other fundraisers held throughout the year keeping Center for Safety and Change a leader in educating the community and ending domestic violence and sexual assault.

Crowe LLP
Independent Member Crowe Global

INDEPENDENT AUDITOR'S REPORT

Board of Directors and Shareholders
Orange County Bancorp, Inc.
Middletown, New York

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Orange County Bancorp, Inc., which comprise the consolidated statement of condition as of December 31, 2018, and the related consolidated statement of income, comprehensive income, changes in stockholders' equity, and cash flows for the year then ended, and the related notes to consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit 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 from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Orange County Bancorp, Inc. as of December 31, 2018, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

The consolidated financial statements of Orange County Bancorp, Inc. as of December 31, 2017, were audited by other auditors whose report dated July 19, 2018, expressed an unmodified opinion on those statements.

Crowe LLP

Crowe LLP

Livingston, New Jersey
April 30, 2019

CONSOLIDATED STATEMENTS OF CONDITION

December 31, 2018 and 2017

(Dollar Amounts in thousands except per share data)

	2018	2017
ASSETS		
Cash and due from banks	$ 18,374	$ 30,220
Investment securities - available-for-sale	255,536	297,698
Restricted investment in bank stocks	2,522	1,817
Loans held for sale	-	11,614
Loans	737,076	565,549
Allowance for loan losses	(10,663)	(8,526)
Loans, net	726,413	557,023
Premises and equipment	13,934	13,686
Premises and equipment held for sale, net	-	783
Accrued interest receivable	3,008	2,793
Cash surrender value of bank-owned life insurance	27,128	26,438
Goodwill	5,359	5,359
Intangible assets	2,535	2,820
Other assets	10,064	10,492
TOTAL ASSETS	$ 1,064,873	$ 960,743
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Noninterest bearing	$ 240,432	$ 201,936
Interest bearing	664,576	606,854
Total deposits	905,008	808,790
Deposits held for sale		
Noninterest bearing	-	1,584
Interest bearing	-	22,171
Total deposits held for sale	-	23,755
FHLB advances	35,500	20,000
Note payable	3,057	3,113
Accrued expenses and other liabilities	12,768	13,777
TOTAL LIABILITIES	956,333	869,435
STOCKHOLDERS' EQUITY		
Common stock, $0.50 par value; 15,000,000 shares authorized; 4,533,304 and 3,966,521 issued; 4,501,125 and 3,933,042 outstanding at December 31, 2018 and 2017, respectively	2,266	1,983
Surplus	85,496	69,476
Undivided profits	30,956	26,668
Accumulated other comprehensive loss, net of taxes	(8,986)	(5,463)
Treasury stock, at cost; 32,179 and 33,479 shares at December 31, 2018 and 2017, respectively	(1,192)	(1,356)
TOTAL STOCKHOLDERS' EQUITY	108,540	91,308
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 1,064,873	$ 960,743

See accompanying notes

CONSOLIDATED STATEMENTS OF INCOME

Years Ended December 31, 2018 and 2017

(Dollar Amounts in thousands except per share data)

	2018	2017
INTEREST INCOME		
Interest and fees on loans	$ 31,608	$ 25,440
Interest on investment securities:		
Taxable	4,944	5,347
Tax exempt	1,416	1,946
Interest on Federal funds sold and other	731	396
TOTAL INTEREST INCOME	38,699	33,129
INTEREST EXPENSE		
Interest on savings and NOW accounts	1,488	811
Interest on time deposits	873	679
Interest on FHLB advances	241	1,187
Interest on note payable	185	188
TOTAL INTEREST EXPENSE	2,787	2,865
NET INTEREST INCOME	35,912	30,264
Provision for loan losses	2,465	1,780
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	33,447	28,484
OTHER OPERATING INCOME		
Service charges on deposit accounts	932	966
Trust income	3,165	2,987
Investment advisory income	4,332	4,158
Investment securities gains	-	302
Earnings on bank-owned life insurance	691	706
Gain on the sale of other real estate owned	-	28
Other	899	772
TOTAL OTHER OPERATING INCOME	10,019	9,919
OTHER OPERATING EXPENSES		
Salaries	15,058	13,734
Employee benefits	3,534	3,784
Occupancy expense	2,724	2,893
Furniture and equipment expense	615	572
Professional fees	2,658	2,030
Directors' fees and expenses	984	808
Computer software expense	2,777	1,944
FDIC assessment	521	346
Advertising expenses	990	890
Advisor expenses related to trust income	842	684
Telephone expenses	410	635
Intangible amortization	286	286
Other	2,887	3,294
TOTAL OTHER OPERATING EXPENSES	34,286	31,900
Income before income taxes	9,180	6,503
Provision for income taxes	1,628	4,152
NET INCOME	$ 7,552	$ 2,351
Earnings per share	$ 1.87	$ 0.60
Cash dividends declared per share	$ 0.806	$ 0.824
Weighted average shares outstanding	4,034,633	3,914,197

See accompanying notes

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Years Ended December 31, 2018 and 2017

(Dollar Amounts in thousands except per share data)

	2018	2017
Net Income	**$ 7,552**	$ 2,351
Other comprehensive loss:		
Unrealized gains/losses on securities:		
Unrealized holding gain/(loss) arising during the year	**(3,584)**	(263)
Reclassification adjustment for losses/(gains) included in net income	**-**	(302)
Tax effect	**(934)**	(225)
Net of tax	**(2,650)**	(340)
Defined benefit pension plans:		
Net (loss)/gain arising during the period	**(863)**	(161)
Reclassification adjustment for amortization of prior service cost and net loss/(gains) included in net periodic pension cost	**(73)**	(75)
Tax effect	**(208)**	(34)
Net of tax	**(582)**	**(52)**
Deferred compensation liability:		
Unrealized holding gain/(loss)	**(421)**	90
Reclassification adjustment for losses/(gains) included in net income	**-**	-
Tax effect	**(130)**	36
Net of tax	**(291)**	54
Total other comprehensive loss	**(3,523)**	(338)
Total comprehensive income	**$ 4,029**	$ 2,013

See accompanying notes

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

Years Ended December 31, 2018 and 2017

(Dollar amounts in thousands except per share data)

	Common Stock	Surplus	Undivided Profits	Accumulated Other Comprehensive Loss	Treasury Stock	Total
Balance, January 1, 2017	$ 998	$ 70,472	$ 26,591	$ (4,174)	$ (1,504)	$ 92,383
Net income	-	-	2,351	-	-	2,351
Other comprehensive loss, net of taxes	-	-	-	(338)	-	(338)
Cash dividends declared ($0.824 per share)	-	-	(3,225)	-	-	(3,225)
Tax Act adjustment impact			951	(951)	-	-
Issue of restricted stock (8,708 shares)	-	(202)	-	-	202	-
Treasury stock purchased (265 shares)	-	-	-	-	(54)	(54)
Restricted stock expense	-	191	-	-	-	191
Reclassification to reflect effect of stock split	985	(985)	-	-	-	-
Balance, December 31, 2017	1,983	69,476	26,668	(5,463)	(1,356)	91,308
Net income	-	-	7,552	-	-	7,552
Other comprehensive loss, net of taxes	-	-	-	(3,523)	-	(3,523)
Cash dividends declared ($0.80 per share)	-	-	(3,264)	-	-	(3,264)
Issue of restricted stock (8,682 shares)	-	(350)	-	-	350	-
Treasury stock purchased (7,382 shares)	-	-	-	-	(186)	(186)
Restricted stock expense	-	228	-	-	-	228
Issuance of common shares at $29.00 per share (566,783 shares)	283	16,142	-	-	-	16,425
Balance, December 31, 2018	$ 2,266	$ 85,496	$ 30,956	$ (8,986)	$ (1,192)	$ 108,540

See accompanying notes

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31, 2018 and 2017

(Dollar amounts in thousands except per share data)

	2018	2017
Cash flows from operating activities		
Net income	**$ 7,552**	$ 2,351
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	**2,465**	1,780
Depreciation and amortization	**1,112**	1,179
Accretion on loans	**(665)**	(380)
Amortization of intangibles	**286**	286
Deferred income tax provision (benefit)	**(190)**	3,216
Investment securities gains	**-**	(302)
Restricted stock expense	**228**	191
Impairment charge on premises and equipment held for sale	**-**	150
Net amortization of investment premiums	**2,732**	2,944
Net earnings on bank-owned life insurance	**(691)**	(706)
Gain on the sale of other real estate owned	**-**	(28)
Net change in:		
Accrued interest receivable	**(210)**	(213)
Other assets	354	1,241
Other liabilities	**(1,009)**	(3,299)
Net cash from operating activities	**11,963**	8,410
Cash flows from investing activities		
Purchases of investment securities available-for-sale	**(33,706)**	(146,651)
Proceeds from sales of investment securities available-for-sale	**-**	46,465
Proceeds from maturities and calls of investment securities available-for-sal	**69,552**	77,961
Decrease (increase) in restricted investment in bank stocks	**(705)**	2,957
Loans Purchased	**(39,055)**	(11,420)
Principal returned on purchased loans	**5,088**	1,388
Net cash from branch sale	**375**	-
Net increase in loans	**(133,130)**	(28,473)
Additions to premises and equipment	**(1,432)**	(1,552)
Proceeds from sale of other real estate owned	**-**	1,613
Net cash from investing activities	**(133,013)**	**(57,712)**
Cash flows from financing activities		
Net increase in deposits	**96,218**	120,515
Net decrease in deposits held for sale	**(15,433)**	-
Net change in FHLB advances	**15,500**	(65,000)
Repayments of note payable	**(56)**	(52)
Proceeds from issuance of common stock	**16,425**	-
Cash dividends paid	**(3,264)**	(3,225)
Purchases of treasury stock	**(186)**	(54)
Net cash from financing activities	**109,204**	52,184
Net change in cash and cash equivalents	**(11,846)**	2,882
Beginning cash and cash equivalents	**30,220**	27,338
Ending cash and cash equivalents	**$ 18,374**	$ 30,220
Supplementary Cash Flow Information		
Interest paid	**$ 2,720**	$ 3,066
Income taxes paid	**460**	-
Supplementary Schedule of Non Cash Investing Activities		
Transfer of loans from held for sale to portfolio	**$ 3,765**	
Premises and equipment transferred to assets held for sale	**(761)**	933

See accompanying notes

Note 1 - Summary of Significant Accounting Policies

Nature of Operations and Principles of Consolidation: The consolidated financial statements include Orange County Bancorp, Inc. (the Company) and its wholly owned subsidiaries: Orange Bank & Trust Company (the Bank) and Hudson Valley Investment Advisors (HVIA), a Registered Investment Advisor, together referred to as "the Company." Intercompany transactions and balances are eliminated in consolidation.

The Company provides commercial and consumer banking services to individuals, small businesses and local municipal governments as well as trust and investment services through the Bank and HVIA. The Company is headquartered in Middletown, New York, with eight locations in Orange County, New York, five in Westchester County, New York and one in Rockland County, New York. Its primary deposit products are checking, savings, and term certificate accounts, and its primary lending products are commercial real estate, commercial and residential mortgage loans. Substantially all loans are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Commercial loans are expected to be repaid from cash flow from operations of businesses. There are no significant concentrations of loans to any one industry or customer. However, the customers' ability to repay their loans is dependent on the real estate and general economic conditions in the areas in which they operate.

Assets held by the Company in an agency or fiduciary capacity for its customers are excluded from the consolidated financial statements since they do not constitute assets of the Company. Assets held by the Company amounted to $942,298 and $930,728 at December 31, 2018 and 2017, respectively.

Subsequent Events: The Company has evaluated subsequent events for recognition and disclosure through April 30, 2019, which is the date the financial statements were available to be issued.

Use of Estimates: To prepare financial statements in conformity with U.S. generally accepted accounting principles, management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and actual results could differ.

Cash Flows: Cash and cash equivalents include cash, deposits with other financial institutions with maturities fewer than 90 days, and federal funds sold. Net cash flows are reported for customer loan and deposit transactions.

Securities: Debt 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. Debt securities not classified as held to maturity are classified as available for sale. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income, net of tax.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments, except for mortgage backed securities where prepayments are anticipated. Gains and losses on sales are recorded on the trade date and determined using the specific identification method.

On January 1, 2018, the Company adopted the new accounting standard for Financial Instruments, which requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. The adoption of this guidance had no impact on the Company's financials as there were no equity investments during 2018 or 2017.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments, except for mortgage backed securities where prepayments are anticipated. Gains and losses on sales are recorded on the trade date and determined using the specific identification method.

Note 1 - Summary of Significant Accounting Policies (continued)

Management evaluates securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) other-than-temporary impairment (OTTI) related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. For equity securities, the entire amount of impairment is recognized through earnings.

Loans Held for Sale: Loan sales occur in limited circumstances as part of strategic business initiatives. Loans held for sale, including deferred fees and costs, are reported at the lower of cost or fair value as determined by expected bid price from the purchaser. Loans are sold without recourse. When a loan is transferred from the portfolio to held for sale, and the fair value is less than cost, a charge-off is recorded against the allowance for loan loss. Subsequent declines in fair value, if any, are recorded as a valuation allowance and charged against earnings.

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, net of purchase premiums and discounts, deferred loan fees and costs and an allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level-yield method without anticipating prepayments.

Interest income on loans is discontinued and placed on non-accrual status at the time the loan is 120 days (in the case of residential mortgage loans) or 90 days (in the case of commercial loans) delinquent unless the loan is well-secured and in process of collection. Loans are charged off to the extent principal or interest is deemed uncollectible. Secured consumer loans, except those secured by the borrower's primary or secondary residence, are charged off upon becoming 180 days past due, or whenever collection is doubtful, whichever occurs first. All unsecured consumer loans are charged off when they become 180 days delinquent or if it is determined that the debt is uncollectible, whichever occurs first. 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 non-accrual 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.

Concentration of Credit Risk: Most of the Company's business activity is with customers located within the New York counties of Orange, Westchester and Rockland. Therefore, the Company's exposure to credit risk is significantly affected by changes in the economy in these counties. The Company's largest loan segment is non-owner occupied commercial real estate. Property types within this segment include: multi-family properties, retail properties, and general construction loans. Regionally, commercial real estate loans are concentrated within the Company's primary operating footprint, including Orange, Westchester, and Rockland counties. Commercial and industrial loans are concentrated in Orange County, New York and outside of the Company's core market, primarily as a result of purchased loans. While industry exposure is widely dispersed, the Company does have a significant concentration of commercial and industrial loans within the healthcare and social assistance industry.

Allowance for Loan Losses: The allowance for loan losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past

Note 1 - Summary of Significant Accounting Policies (continued)

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.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings (TDRs) and classified as impaired.

Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

All criticized and classified consumer mortgages, commercial loans, and commercial real estate loans are reviewed to determine impairment status. Minimally, loans in which the borrower has filed bankruptcy; loans in non-accrual status; or loans that are considered a TDR would be considered impaired. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, 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. A specific allocation within the allowance for loan losses is established for an impaired loan if its carrying value exceeds its estimated fair value. The estimated fair values of substantially all of the Bank's impaired loans are measured based on the estimated fair value of the loan's collateral.

For commercial loans secured by real estate, estimated fair values of collateral are determined primarily through third-party appraisals. When a real estate secured loan becomes impaired, a decision is made regarding whether an updated certified appraisal of the real estate is necessary. This decision is based on various considerations, including the age of the most recent appraisal, the loan-to-value ratio based on the original appraisal and the condition of the property. Appraised values are discounted to arrive at the estimated selling price of the collateral, which is considered to be the estimated fair value. The discounts also include estimated costs to sell the property.

For commercial and industrial loans secured by non-real estate collateral, such as accounts receivable, inventory and equipment, estimated fair values are determined based on the borrower's financial statements, inventory reports, accounts receivable aging reports, equipment appraisals or invoices. Indications of value from these sources are generally discounted based on the age of the financial information or the quality of the assets.

Credit quality risk ratings include regulatory classifications of special mention, substandard, doubtful and loss. Loans classified special mention have potential weaknesses that deserve management's close attention. If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. Loans classified substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They include loans that are inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified doubtful have all the weaknesses inherent in loans classified substandard with the added characteristic that collection or liquidation in full, on the basis of current conditions and facts, is highly improbable. Loans classified as a loss are considered uncollectible and are charged to the allowance for loan losses. Loans not classified are rated pass.

Troubled debt restructurings are individually evaluated for impairment and included in the separately identified impairment disclosures. TDRs are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. For TDRs that subsequently default, the Company determines the amount of the allowance on that loan in accordance with the accounting policy for the allowance for loan losses on loans individually identified as impaired. The Company incorporates recent historical experience related to TDRs including the performance of TDRs that subsequently default into the calculation of the allowance by loan portfolio segment.

Note 1 - Summary of Significant Accounting Policies (continued)

The general component covers loans that are collectively evaluated for impairment. Large groups of smaller balance homogeneous loans, such as consumer, are collectively evaluated for impairment, and accordingly, they are not included in the separately identified impairment disclosures. The general allowance component also includes loans that are not individually identified for impairment evaluation, such as those loans that are individually evaluated but are not considered impaired. The general component is based on historical loss experience adjusted for current factors. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the most recent 4 years. 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 (including TDRs); levels of and trends in charge-offs and recoveries; migration of loans to the classification of special mention, substandard, or doubtful; 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 concentration.

In addition, federal regulatory agencies and the New York State Department of Financial Services, as an integral part of their examination process, periodically review the Bank's allowance for loan losses and may require the Bank to recognize additions to the allowance based on their judgments about information available to them at the time of their examination, which may not be currently available to management. Based on management's comprehensive analysis of the loan portfolio, management believes the level of the allowance for losses is adequate at December 31, 2018 and 2017.

The loan portfolio is segmented into commercial, residential real estate, home equity, and consumer loans. Commercial loans consist of the following classes: commercial and industrial, commercial real estate and commercial real estate construction.

Commercial and Industrial Lending: The Bank originates commercial and industrial loans primarily to businesses located in its primary market area and surrounding areas. These loans are used for various business purposes which include short-term loans and lines of credit to finance machinery and equipment purchases, inventory and accounts receivable. Generally, the maximum term for loans extended on machinery and equipment is based on the projected useful life of such machinery and equipment. Most business lines of credit are written on demand and may be renewed annually.

Commercial and industrial loans are generally secured with short-term assets; however, in many cases, additional collateral such as real estate is provided as additional security for the loan. Loan-to-value maximum values have been established by the Bank and are specific to the type of collateral. Collateral values may be determined using invoices, inventory reports, accounts receivable aging reports, collateral appraisals, etc.

In underwriting commercial and industrial loans, an analysis of the borrower's character, capacity to repay the loan, the adequacy of the borrower's capital and collateral as well as an evaluation of conditions affecting the borrower is performed. Analysis of the borrower's past, present and future cash flows is also an important aspect of the Bank's analysis.

Commercial loans generally present a higher level of risk than other types of loans due primarily to the effect of general economic conditions.

Commercial Real Estate Lending – The Bank engages in commercial real estate lending in its primary market area and surrounding areas. The Bank's commercial loan portfolio is secured primarily by commercial retail space and office buildings. Generally, commercial real estate loans have maturities that do not exceed 20 years, amortization provisions that do not exceed 30 years, have loan-to-value ratios of up to 75% of the appraised value of the property, and are typically credit enhanced by personal guarantees of the borrowers.

In underwriting these loans, the Bank performs a thorough analysis of the financial condition of the borrower, the borrower's credit history, and the reliability and predictability of the cash flow generated by the property securing the loan. Appraisals on properties securing commercial real estate loans originated by the Bank are performed by independent appraisers.

Commercial real estate loans generally present a higher level of risk than other types of loans due primarily to the effect of general economic conditions.

Note 1 - Summary of Significant Accounting Policies (continued)

Commercial Real Estate Construction Lending: The Bank engages in commercial real estate construction lending in its primary market area and surrounding areas. The Bank's commercial real estate construction lending consists of commercial and residential site development loans as well as commercial building construction and residential housing construction loans.

The Bank's commercial real estate construction loans are generally secured with the subject property. Terms of construction loans depend on the specifics of the project such as, estimated absorption rates, estimated time to complete, etc.

In underwriting commercial real estate construction loans, the Bank performs a thorough analysis of the financial condition of the borrower, the borrower's credit history, the reliability and predictability of the cash flow generated by the project using feasibility studies, market data, etc.

Appraisals on properties securing commercial real estate construction loans originated by the Bank are performed by independent appraisers.

Commercial real estate construction loans generally present a higher level of risk than other types of loans due primarily to the effect of general economic conditions and uncertainties of construction costs.

Residential Real Estate Lending: One-to-four-family residential mortgage loan originations are generated by the Bank's marketing efforts, its present customers, walk-in customers and referrals. These loans originate primarily within the Bank's market area or with customers primarily from the market area.

The Bank offers fixed-rate loans with terms up to a maximum of 20 years for both permanent structures and those under construction. The Bank's one- to four-family residential real estate loan originations are secured primarily by properties located in its primary market area and surrounding areas. The majority of the Bank's residential real estate loans originate with a loan-to-value of 80% or less. Loans in excess of 80% are required to have private mortgage insurance.

In underwriting one- to four-family residential real estate loans, the Bank evaluates both the borrower's ability to make monthly payments and the value of the property securing the loan. Properties securing real estate loans made by the Bank are appraised by independent appraisers. The Bank generally requires borrowers to obtain an attorney's title opinion or title insurance, and fire and property insurance (including flood insurance, if necessary) in an amount not less than the amount of the loan. The Bank has not engaged in sub-prime residential mortgage originations.

Residential real estate loans generally present a lower level of risk than other types of loans because they are secured by the borrower's primary residence.

Home Equity Lending: The Bank originates home equity lines of credit and closed-end loans primarily within the Bank's market area or with customers primarily from the market area.

Home equity lines and loans are secured by the borrower's primary residence with a maximum loan-to-value of 85% and a maximum term of 15 years on home equity loans and a 10-year draw period followed by a 15-year repayment period for home equity lines.

In underwriting home equity lines and loans, a thorough analysis of the borrower's financial ability to repay the loan as agreed is performed. The ability to repay shall be determined by the borrower's employment history, current financial conditions, and credit background. The analysis is based primarily on the customer's ability to repay and secondarily on the collateral or security.

Home equity lines and loans generally present a lower level of risk than other types of consumer loans because they are secured by the borrower's primary residence.

The subordinate nature of some home equity lines and loans may make these loans of higher risk than other residential real estate loans.

Note 1 - Summary of Significant Accounting Policies (continued)

Consumer Lending: The Bank offers a variety of secured and unsecured consumer loans, including vehicle, loans secured by savings deposits as well as other types of consumer loans.

Consumer loan terms vary according to the type and value of collateral and creditworthiness of the borrower. In underwriting consumer loans, a thorough analysis of the borrower's financial ability to repay the loan as agreed is performed. The ability to repay shall be determined by the borrower's employment history, current financial conditions, and credit background.

Consumer loans may entail greater credit risk than do residential real estate loans particularly in the case of consumer loans which are unsecured or are secured by rapidly depreciable assets, such as automobiles or recreational equipment. In such cases, any repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation. In addition, consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be affected by adverse personal circumstances. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount which can be recovered on such loans.

Transfers of Financial Assets: Transfers of financial assets are accounted for as sales, when control over the assets has been relinquished. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Company, 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 the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Foreclosed Assets: Foreclosed assets are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. Physical possession of real estate property collateralizing a 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. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. If fair value declines subsequent to foreclosure, a valuation allowance is recorded through expense. Operating costs after acquisition are expensed.

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 8 to 50 years. Furniture, fixtures and equipment are depreciated using the straight-line (or accelerated) method with useful lives ranging from 3 to 10 years.

Trust and Investment Advisory Income: The Company earns trust revenue and advisory revenue from a variety of sources including fees from trust administration and other related fiduciary services, custody, investment management and advisory services, employee benefit account and IRA administration, estate settlement, tax service fees, shareholder service fees and brokerage. These fees are generally based on asset values and fluctuate with the market. Some revenue is not directly tied to asset value but is based on a flat fee for services provided. For many of our revenue sources, amounts are not received in the same accounting period in which they are earned. However, each source of wealth management fees is recorded on the accrual method of accounting.

Included in other assets on the balance sheet is a receivable for trust fees and advisory fees that have been earned but not yet collected.

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 in 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.

Federal Reserve Bank (FRB) Stock: The Bank is a member of its regional Federal Reserve Bank. FRB 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.

Note 1 - Summary of Significant Accounting Policies (continued)

Bank Owned Life Insurance: The Bank has purchased life insurance policies on certain key executives. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

Goodwill and Other Intangible Assets: Goodwill arises from business combinations and is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, 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 exists that indicate that a goodwill impairment test should be performed. The Company has selected October 1 as the date to perform the annual impairment test. 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 our balance sheet.

Other intangible assets consist of core deposit and acquired customer relationship intangible assets arising from whole bank and branch acquisitions are amortized on an accelerated method over their estimated useful lives, which range from 7 to 10 years.

Loan Commitments and Related Financial Instruments: Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial 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.

Stock-Based Compensation: Compensation cost is recognized for restricted stock awards issued to employees, based on the fair value of these awards at the date of grant. The market price of the Company’s common stock at the date of grant is used for restricted stock awards.

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. The Company’s accounting policy is to recognize forfeitures as they occur.

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. A valuation allowance, if needed, 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 is greater than 50% likely of being realized on examination. For tax positions not meeting the “more likely than not” test, no tax benefit is recorded.

The Company recognizes interest and/or penalties related to income tax matters in miscellaneous expense.

Retirement Plans: Pension expense is the net of service and interest cost, return on plan assets and amortization of gains and losses not immediately recognized. Employee 401(k) and profit sharing plan expense is the amount of matching contributions. Deferred compensation and supplemental retirement plan expense allocates the benefits over years of service.

Earnings per Common Share: Basic earnings per common share is net income divided by the weighted average number of common shares outstanding during the period. All outstanding unvested share-based payment awards that contain rights to non-forfeitable dividends are considered participating securities for this calculation. Earnings and dividends per share are restated for all stock splits and stock dividends through the date of issuance of the financial statements. The average number of shares outstanding during 2018 and 2017 was 4,034,633 and 3,914,197, respectively, as adjusted for the effect of the 2 for 1 stock split completed on February 23, 2018. The Company currently maintains a simple capital structure, which includes restricted stock with participation rights to dividends, thus there are no dilutive effects on earnings per share.

(Dollar amounts in thousands except per share data)

Note 1 - Summary of Significant Accounting Policies (continued)

Comprehensive Income: The components of accumulated other comprehensive loss, net of taxes, as of December 31, 2018 and 2017 are as follows:

	Unrealized loss on Securities	Pension Plan Liability	Deferred Compensation Liability	Accumulated Other Comprehensive Loss
Balance - December 31, 2018	**$ (3,712)**	**$ (5,149)**	**$ (125)**	**$ (8,986)**
Balance - December 31, 2017	$ (1,062)	$ (4,567)	$ 166	$ (5,463)

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale and changes in the funded status of the pension plan, 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. Management does not believe there now are such matters that will have a material effect on the financial statements.

Restrictions on Cash: Cash on hand or on deposit with the Federal Reserve Bank was required to meet regulatory reserve and clearing requirements.

Dividend Restriction: Banking regulations require maintaining certain capital levels and may limit the dividends paid by the bank to the holding company or by the holding company to shareholders.

Fair Value of Financial Instruments: Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in a separate note. 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 these estimates.

Reclassifications: Some items in the prior year financial statements were reclassified to conform to the current presentation. Reclassifications had no effect on prior year net income or shareholders' equity.

Adoption of New Accounting Standards: On January 1, 2018, the Company adopted ASU 2014-09 *Revenue from Contracts with Customers* and all subsequent amendments to the ASU (collectively, "ASC 606"), which (i) creates a single framework for recognizing revenue from contracts with customers that fall within its scope and (ii) revises when it is appropriate to recognize a gain (loss) from the transfer of nonfinancial assets, such as OREO. The majority of the Company's revenues come from interest income and other sources, including loans, leases, securities and derivatives, which are outside the scope of ASC 606. The Company's services that fall within the scope of ASC 606 are presented within Non-Interest Income and are recognized as revenue as the Company satisfies its obligation to the customer. Services within the scope of ASC 606 include service charges on deposit accounts, interchange income, wealth management fees, investment brokerage fees, and the sale of OREO. Refer to Note 15 *Revenue from Contracts with Customers* for further discussion on the Company's accounting policies for revenue sources within the scope of ASC 606. The Company elected the modified retrospective approach of adoption. The impact of this adoption was not material.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments". This guidance amends existing guidance to improve accounting standards for financial instruments including clarification and simplification of accounting and disclosure requirements and the requirement for public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. The Company adopted the guidance effective January 1, 2018. Upon adoption, the fair value of the Company's loan portfolio is now presented using an exit price method.

(Dollar amounts in thousands except per share data)

Note 2 - Investment Securities

The amortized cost and fair value of investment securities at December 31, 2018 and 2017 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale December 31, 2018				
U.S. government agencies	**$ 96,434**	**$ 120**	**$ (1,527)**	**$ 95,027**
Mortgage-backed securities	**115,914**	**-**	**(3,516)**	**$ 112,398**
Obligations of states and political subdivisions	**48,207**	**162**	**(258)**	**$ 48,111**
Total debt securities	**$ 260,555**	**$ 282**	**$ (5,301)**	**$ 255,536**
Available-for-sale December 31, 2017				
U.S. government agencies	$ 93,345	$ 238	$ (578)	$ 93,005
Mortgage-backed securities	141,721	192	(1,701)	140,212
Obligations of states and political subdivisions	64,067	623	(209)	64,481
Total debt securities	$ 299,133	$ 1,053	$ (2,488)	$ 297,698

Proceeds from sales of securities during 2018 and 2017 were $0 and $46,665, respectively. Gross gains in those years were $0 and $302, respectively. Gross losses were $0 in 2018 and 2017.

The amortized cost and fair value of debt securities as of December 31, 2018 are shown by contractual maturity. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Due in one year or less	$ 10,993	$ 10,995
Due after one through five years	44,979	44,807
Due after five through ten years	15,155	15,071
Due after ten years	73,515	72,266
	144,641	143,138
Mortgage-backed securities	115,914	112,398
Total debt securities	$ 260,555	$ 255,536

Securities pledged at year-end 2018 and 2017 had a carrying amount of $116,364 and $141,599 and were pledged to secure public deposits.

Mortgage-backed securities are issued by FNMA, FHMC, or GNMA. Obligations of states and political subdivisions consist of general obligations of municipalities in the state of New York.

At year-end 2018 and 2017, there were no holdings of securities of any one issuer, other than the US Government and its agencies, in an amount greater than 10% of shareholders' equity.

The following table summarizes securities with unrealized and unrecognized losses at December 31, 2018 and 2017, aggregated by major security types and length of time in continuous loss position:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-sale December 31, 2018						
U.S. government agencies	**$ 29,708**	**$ (447)**	**$ 45,362**	**$ (1,080)**	**$ 75,070**	**$ (1,527)**
Mortgage-backed securities	**1,527**	**(27)**	**110,870**	**(3,489)**	**112,397**	**(3,516)**
Obligations of states and political subdivisions	**4,863**	**(25)**	**20,896**	**(233)**	**25,759**	**(258)**
Total debt securities	**$ 36,098**	**$ (499)**	**$ 177,128**	**$ (4,802)**	**$ 213,226**	**$ (5,301)**
Available-for-sale December 31, 2017						
U.S. government agencies	$ 27,843	$ (127)	$ 29,849	$ (451)	$ 57,692	$ (578)
Mortgage-backed securities	89,144	(876)	41,851	(825)	130,995	(1,701)
Obligations of states and political subdivisions	17,980	(119)	5,677	(90)	23,657	(209)
Total debt securities	$ 134,967	$ (1,122)	$ 77,377	$ (1,366)	$ 212,344	$ (2,488)

There was no other than temporary impairment loss recognized on any securities at December 31, 2018 or 2017.

(Dollar amounts in thousands except per share data)

Note 2 - Investment Securities (continued)

As of December 31, 2018, the Company's security portfolio consisted of 255 securities, 150 of which were in an unrealized loss position. The majority of unrealized losses are related to the Company's mortgage backed and U.S. government agency securities as discussed below.

At December 31, 2018, 100% of the mortgage-backed securities held by the company were issues by U.S. government sponsored entities and agencies. Because the decline in fair value is attributable to changes in interest rates and illiquidity, and not credit quality, and because the Company does not have the intent to sell these mortgage-backed securities, and it is likely that it will not be required to sell the securities before their anticipated recovery, the Company does not consider these securities to be other than temporarily impaired at December 31, 2018.

The Company's unrealized losses on U.S. government agency securities relate primarily to its investment in Small Business Agency ("SBA") issued securities. Because the decline in fair value is attributable to changes in interest rates and illiquidity, and not credit quality, and because the Company does not have the intent to sell these mortgage-backed securities, and it is likely that it will not be required to sell the securities before their anticipated recovery, the Company does not consider these securities to be other than temporarily impaired at December 31, 2018

Note 3 - Loans

Loans at year-end were as follows:

	2018	2017
Commercial and industrial	**$ 179,278**	$ 127,874
Commercial real estate	**456,838**	357,734
Commercial real estate construction	**28,863**	18,912
Residential real estate	**59,215**	51,176
Home equity	**10,641**	9,192
Consumer	**2,241**	661
Total	**$ 737,076**	$ 565,549

The following table presents the activity in the allowance for loan losses by portfolio segment for each of the years ending December 31, 2018 and 2017:

	Commercial and Industrial	Commercial Real Estate	Commercial Real Estate Construction	Residential Real Estate	Home Equity	Consumer	Total
December 31, 2018							
Allowance for loan losses:							
Beginning balance	$ 2,906	$ 4,858	$ 538	$ 180	$ 27	$ 17	$ 8,526
Provision for loan losses (benefits)	1,204	829	29	137	236	30	2,465
Loans charged-off	(232)	(33)	-	(52)	(158)	(10)	(485)
Recoveries	5	54	-	88	-	10	157
Ending balance	$ 3,883	$ 5,708	$ 567	$ 353	$ 105	$ 47	$ 10,663

	Commercial and Industrial	Commercial Real Estate	Commercial Real Estate Construction	Residential Real Estate	Home Equity	Consumer	Total
December 31, 2017							
Allowance for loan losses:							
Beginning balance	$ 2,115	$ 4,843	$ 512	$ 224	$ 44	$ 1	$ 7,739
Provision for loan losses (benefits)	1,761	(104)	26	74	(9)	32	1,780
Loans charged-off	(986)	(36)	-	(129)	(9)	(20)	(1,180)
Recoveries	16	155	-	11	1	4	187
Ending balance	$ 2,906	$ 4,858	$ 538	$ 180	$ 27	$ 17	$ 8,526

(Dollar amounts in thousands except per share data)

Note 3 – Loans (continued)

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31, 2018 and 2017:

	Commercial and Industrial	Commercial Real Estate	Commercial Real Estate Construction	Residential Real Estate	Home Equity	Consumer	Total
December 31, 2018							
Allowance for loan losses:							
Ending balance:							
individually evaluated for impairment	**$ 104**	**$ 874**	**$ -**	**$ 101**	**$ 66**	**$ 4**	**$ 1,149**
collectively evaluated for impairment	**3,779**	**4,834**	**567**	**252**	**39**	**43**	**9,514**
Total ending allowance balance	**$ 3,883**	**$ 5,708**	**$ 567**	**$ 353**	**$ 105**	**$ 47**	**$ 10,663**
Loans:							
Ending balance:							
individually evaluated for impairment	**$ 362**	**$ 13,757**	**$ -**	**$ 345**	**$ 98**	**$ 141**	**$ 14,703**
collectively evaluated for impairment	**178,916**	**443,081**	**28,863**	**58,870**	**10,543**	**2,100**	**722,373**
Total ending loans balance	**$ 179,278**	**$ 456,838**	**$ 28,863**	**$ 59,215**	**$ 10,641**	**$ 2,241**	**$ 737,076**
December 31, 2017							
Allowance for loan losses:							
Ending balance:							
individually evaluated for impairment	$ 42	$ 606	$ 70	$ 69	$ -	$ 4	$ 791
collectively evaluated for impairment	2,864	4,252	468	111	27	13	7,735
Total ending allowance balance	$ 2,906	$ 4,858	$ 538	$ 180	$ 27	$ 17	$ 8,526
Loans:							
Ending balance:							
individually evaluated for impairment	$ 446	$ 16,300	$ 268	$ 322	$ 172	$ 148	$ 17,656
collectively evaluated for impairment	127,428	341,434	18,644	50,854	9,020	513	547,893
Total ending loans balance	$ 127,874	$ 357,734	$ 18,912	$ 51,176	$ 9,192	$ 661	$ 565,549

(Dollar amounts in thousands except per share data)

Note 3 – Loans (continued)

The following table presents information related to impaired loans by class of loans as of and for the year ended December31, 2018 and 2017:

	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
December 31, 2018					
With no related allowance recorded					
Commercial and industrial	$ 258	$ 258	$ -	$ 568	$ 21
Commercial real estate	8,486	6,971	-	9,427	529
Commercial real estate construction	-	-	-	-	-
Residential real estate	-	-	-	-	-
Home equity	-	-	-	-	-
Consumer	-	-	-	22	-
Total	$ 8,744	$ 7,229	$ -	$ 10,017	$ 550
With an allowance recorded:					
Commercial and industrial	$ 104	$ 104	$ 104	$ 103	$ 1
Commercial real estate	6,786	6,786	874	7,209	435
Commercial real estate construction	-	-	-	-	-
Residential real estate	345	345	101	356	10
Home equity	120	98	66	98	-
Consumer	141	141	4	145	7
Total	$ 7,496	$ 7,474	$ 1,149	$ 7,911	$ 453

	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
December 31, 2017					
With no related allowance recorded					
Commercial and industrial	$ 108	$ 108	$ -	$ 102	$ 10
Commercial real estate	10,894	9,331	-	8,570	610
Commercial real estate construction	-	-	-	-	-
Residential real estate	67	67	-	34	3
Home equity	172	172	-	125	-
Consumer	-	-	-	37	-
Total	$ 11,241	$ 9,678	$ -	$ 8,829	$ 623
With an allowance recorded					
Commercial and industrial	$ 338	$ 338	$ 42	$ 766	$ 6
Commercial real estate	6,970	6,970	606	8,269	380
Commercial real estate construction	268	268	70	272	9
Residential real estate	254	254	69	138	8
Home equity	-	-	-	222	-
Consumer	148	148	4	103	7
Total	$ 7,978	$ 7,978	$ 791	$ 9,768	$ 410

The cash basis income received on the impaired loans is approximately equal to interest income recognized on these loans.

(Dollar amounts in thousands except per share data)

Note 3 – Loans (continued)

The following tables present the recorded investment in non-accrual and loans past due over 89 days still on accrual by class of loans as of December 31, 2018 and December 31, 2017.

	Non-accrual		Loans Past Due Over 89 Days Still Accruing	
	2018	2017	**2018**	2017
Commercial and industrial	**$ 104**	$ 40	**$ 145**	$ 237
Commercial real estate	**1,419**	1,733	**30**	1,196
Commercial real estate construction			**-**	-
Residential real estate	**204**	175	**9**	12
Home equity	**98**	172	**-**	-
Consumer	**-**	-	**-**	-
Total	**$ 1,825**	$ 2,120	**$ 184**	$ 1,445

The following table presents the aging of the recorded investment in past-due loans as of December 31, 2018 and 2017 by class of loans:

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 89 Days	Total Past Due	Loans Not Past Due	Total
December 31, 2018						
Commercial and industrial	**$ 738**	**$ 117**	**$ 169**	**$ 1,024**	**$ 178,254**	**$ 179,278**
Commercial real estate	**1,413**	**-**	**1,449**	**2,862**	**453,976**	**456,838**
Commercial real estate construction	**-**	**-**	**-**	**-**	**28,863**	**28,863**
Residential real estate	**896**	**504**	**115**	**1,515**	**57,700**	**59,215**
Home equity	**1,098**	**47**	**98**	**1,243**	**9,398**	**10,641**
Consumer	**-**	**13**	**-**	**13**	**2,228**	**2,241**
Total	**$ 4,145**	**$ 681**	**$ 1,831**	**$ 6,657**	**$ 730,419**	**$ 737,076**
December 31, 2017						
Commercial and industrial	$ 167	$ 200	$ 277	$ 644	$ 127,230	127,874
Commercial real estate	-	-	2,930	2,930	354,804	357,734
Commercial real estate construction	-	442	-	442	18,470	18,912
Residential real estate	156	26	186	368	50,808	51,176
Home equity	137	-	172	309	8,883	9,192
Consumer	1	-	-	1	660	661
Total	$ 461	$ 668	$ 3,565	$ 4,694	$ 560,855	$ 565,549

(Dollar amounts in thousands except per share data)

Note 3 – **Loans** (continued)

Troubled Debt Restructuring:

The following table presents loans by class modified as troubled debt restructurings that were outstanding as of December 31, 2018 and 2017:

December 31, 2018	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Current Recorded Investment
Commercial and industrial	2	**$ 409**	**$ 409**	**$ 297**
Commercial real estate	13	**15,718**	**15,718**	**13,757**
Commercial real estate construction	0	**-**	**-**	**-**
Residential real estate	1	**153**	**153**	**142**
Consumer	1	**155**	**155**	**141**
Total	**17**	**$ 16,435**	**$ 16,435**	**$ 14,337**

	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Current Recorded Investment
December 31, 2017				
Commercial and industrial	3	$ 819	$ 819	$ 446
Commercial real estate	15	18,126	18,126	16,300
Commercial real estate construction	1	293	293	268
Residential real estate	1	153	153	147
Consumer	1	155	155	148
Total	21	$ 19,546	$ 19,546	$ 17,309

There were no restructured loans that defaulted within twelve months of restructure during 2018 or 2017. As of December 31, 2018, there were no commitments to lend additional funds to borrowers whose loans were classified as troubled debt restructurings.

In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Company's internal underwriting policy.

There were no loans whose terms were modified resulting in a troubled debt restructuring during the year ending December 31, 2018. The following table summarizes loans whose terms have been modified resulting in troubled debt restructurings during the year ending December 31, 2017:

	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Pre-Modification Outstanding Recorded Investment	Current Recorded Investment
2017				
Commercial and industrial	1	$ 310	$ 310	$ 298
Residential real estate	1	153	153	147
Consumer	1	155	155	148
	3	$ 618	$ 618	$ 593

As of December 31, 2018, loans in the process of foreclosure were $1,623, of which $205 were secured by residential real estate.

Credit Quality Indicators: The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis includes loans with an outstanding balance greater than $350 and non-homogeneous loans, such as commercial and commercial real estate loans. This analysis is performed on an annual basis. The company uses the following definitions for risk ratings:

Note 3 – Loans (continued)

Special Mention. Loans classified as special mention 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 the institution's credit position at some future date.

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

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

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass-rated loans.

Based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

	Pass	Special Mention	Substandard	Doubtful	Loss	Total
December 31, 2018						
Commercial and industrial	**$ 175,422**	**$ 563**	**$ 3,293**	**$ -**	**$ -**	**$ 179,278**
Commercial real estate	**436,406**	**8,771**	**11,661**	**-**	**-**	**456,838**
Commercial real estate construction	**28,863**	**-**	**-**	**-**	**-**	**28,863**
Residential real estate	**59,109**	**-**	**106**	**-**	**-**	**59,215**
Home equity	**10,543**	**-**	**98**	**-**	**-**	**10,641**
Consumer	**2,100**	**-**	**141**	**-**	**-**	**2,241**
Total	**$ 712,443**	**$ 9,334**	**$ 15,299**	**$ -**	**$ -**	**$ 737,076**

(in thousands)	Pass	Special Mention	Substandard	Doubtful	Loss	Total
December 31, 2017						
Commercial and industrial	$ 123,236	$ 818	$ 3,820	$ -	$ -	$ 127,874
Commercial real estate	337,920	6,302	13,512	-	-	357,734
Commercial real estate construction	18,644	-	268	-	-	18,912
Residential real estate	51,002	-	174	-	-	51,176
Home equity	9,020	-	172	-	-	9,192
Consumer	513	148	-	-	-	661
Total	$ 540,335	$ 7,268	$ 17,946	$ -	$ -	$ 565,549

Loans to certain directors and principal officers of the Company, including their immediate families and companies in which they are principal owners (more than 10%), amounted to $418 and $459 at December 31, 2018 and December 31, 2017. Activity for these loans for the years ended December 31, 2018 and 2017 are as follows:

	2018	2017
Balance, beginning of year	**$ 459**	$ 385
Additions	**-**	212
Repayments	**(41)**	(138)
Balance, end of year	**$ 418**	$ 459

Note 4 - Fair Value

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 company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The Company used the following methods and significant assumptions to estimate fair value:

Investment Securities: The fair values for investment securities are determined by quoted market prices, if available (Level 1). For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2), using matrix pricing. Matrix pricing is a mathematical technique commonly used to price debt securities that are not actively traded, values 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). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3).

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 and resulted in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted in accordance with the allowance policy.

Appraisals for both collateral-dependent impaired loans and real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by a third-party appraisal management company that the Company has engaged in accordance with internal vendor management policies and approval of the Company's Board of Directors. Once received, the appraisal review function is conducted by the appraisal management company and consists of a review of the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics. Through this review, the appraisal management company evaluates the validity of the appraised value and the strength of the conclusions; which are subsequently confirmed by a member of the Credit Department. Discounts to the appraised value are then applied to recognize the carrying costs incurred until disposition, realtor fees, deterioration in the quality of the asset, and the age of the appraisal. A discount of 20% is typically applied to properties with appraisals performed within 12 months while a discount of 25% is typically applied to properties with appraisals performed longer than 12 months prior to the impairment analysis. The net effect of these adjustments were included in the charge-off to the allowance upon acquisition of the foreclosed property and/or upon partial charge-off of the impaired loan. The most recent analysis of property appraisals including the appropriate discount rates are incorporated into the allowance methodology for the respective loan portfolio segments.

Loans Held For Sale: Loans held for sale are carried at the lower of cost or fair value, which is determined by the expected bid price from the purchaser. Subsequent declines in fair value, if any, are recorded as a valuation allowance and charged against earnings.

(Dollar amounts in thousands except per share data)

Note 4 - Fair Value (continued)

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

		Fair Value Measurements Using:		
	Total at December 31, 2018	**Quoted Prices in Active Markets for Identicle Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
U.S. government agencies	**95,027**	**$ -**	**$ 95,027**	**$ -**
Mortgage-backed securities	**112,398**	**-**	**112,398**	**-**
Obligations of states and political subdivisions	**48,111**	**-**	**48,111**	**-**
Total securities available for sale	**$ 255,536**	**$ -**	**$ 255,536**	**$ -**

		Fair Value Measurements Using:		
	Total at December 31, 2017	Quoted Prices in Active Markets for Identicle Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. government agencies	$ 93,005	$ -	$ 93,005	$ -
Mortgage-backed securities	140,212	-	140,212	-
Obligations of states and political subdivisions	64,481	-	64,481	-
Total securities available for sale	$ 297,698	$ -	$ 297,698	$ -

There were no transfers between Level 1 and Level 2 during 2018 or 2017.

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

		Fair Value Measurements Using:		
	Total at December 31, 2018	**Quoted Prices in Active Markets for Identicle Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Impaired loans	**$ 3,640**	**$ -**	**$ -**	**$ 3,640**

		Fair Value Measurements Using:		
	Total at December 31, 2017	Quoted Prices in Active Markets for Identicle Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	$ 7,187	$ -	$ -	$ 7,187

The fair value amounts shown in the above table are impaired loans net of reserves allocated to said loans. The total reserves allocated to these impaired loans are $1,011 and $791 for December 31, 2018 and 2017 respectively.

(Dollar amounts in thousands except per share data)

Note 4 - Fair Value (continued)

The following table presents additional quantitative information about level 3 fair value measured at fair value on a non-recurring basis at December31, 2018 and 2017:

December 31, 2018	Fair Value Value	Valuation Technique	Unobservable Input	Range (Average)
Impaired loans	**$ 3,640**	**Appraisal of collateral (1)**	**Appraisal and liquidation adjustments (2)**	**5-20% (10%)**

December 31, 2017	Fair Value	Valuation Technique	Unobservable Input	Range (Average)
Impaired loans	$ 7,187	Appraisal of collateral (1)	Appraisal and liquidation adjustments (2)	5-20% **(10%)**

(1) Fair value is generally determined through independent appraisals of the underlying collateral that generally include various level 3 inputs which are not identifiable.

(2) Appraisals may be adjusted downward by management for qualitative factors such as economic conditions and estimated liquidation expenses. The range of liquidation expenses and other appraisal adjustments are presented as a percent of the appraisal.

The carrying amounts and estimated fair values of financial instruments not carried at fair value, at December 31, 2018 and 2017 are as follows:

		Fair Value Measurements at December 31, 2018 Using:			
	Carrying Amount	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets:					
Cash and due from banks	**$ 18,374**	**$ 18,374**	**$ -**	**$ -**	**$ 18,374**
Loans, net	**726,413**	**-**	**-**	**716,082**	**716,082**
Financial liabilities:					
Deposits (excluding noninterest bearing deposits)	**664,576**	**-**	**663,880**	**-**	**663,880**
FHLB advances	**35,500**	**-**	**35,386**	**-**	**35,386**
Note payable	**3,057**	**-**	**-**	**3,057**	**3,057**

		Fair Value Measurements at December 31, 2017 Using:			
	Carrying Amount	Level 1	Level 2	Level 3	Total
Financial assets:					
Cash and due from banks	$ 30,220	$ 30,220	$ -	$ -	$ 30,220
Loans held for sale	11,614	-	-	11,614	11,614
Loans, net	557,023	-	-	552,885	552,885
Financial liabilities:					
Deposits (excluding noninterest bearing deposits)	606,854	-	606,323	-	606,323
Deposits for sale (excluding noninterest bearing deposits)	22,171	-	-	22,171	22,171
FHLB advances	20,000	-	19,850	-	19,850
Note payable	3,113			3,113	

(Dollar amounts in thousands except per share data)

Note 5 - Premises and Equipment

Year-end premises and equipment were as follows:

	2018	2017
Land	**$ 3,202**	$ 3,152
Buildings and improvements	**11,223**	10,647
Furniture and equipment	**5,742**	5,662
Leasehold improvements	**5,380**	4,799
	25,547	24,260
Accumulated depreciation and amortization	**(11,613)**	(10,574)
Premises and equipment, net	**$ 13,934**	$ 13,686

Depreciation and amortization included in operating expenses amounted to $1,112 in 2018 and $1,179 in 2017.

Certain premises are leased under agreements which are renewable for varying periods and are subject to minimum lease payments as well as additional rent. Rent expense for all operating leases was $642 in 2018 and $700 in 2017.

As of December 31, 2018 future minimum lease payments are as follows:

Years Ending December 31,	
2019	$ 412
2020	381
2021	387
2022	376
2023	344
Thereafter	523
	$ 2,423

As described in Note 14 - Branch Sale, the Company transferred leasehold improvements and equipment in the amount of $933 from premises and equipment to premises and equipment held for sale as of December 31, 2017.

(Dollar amounts in thousands except per share data)

Note 6 - Goodwill and Intangible Assets

Goodwill: The change in goodwill during the year is as follows:

	2018	2017
Beginning of year	$ 5,359	$ 5,359
Acquired goodwill impairment	-	-
End of year	$ 5,359	$ 5,359

Impairment exits when a reporting unit's carrying value of goodwill exceeds its fair value. At October 1, 2018, the Company's reporting unit had positive equity and the company elected to perform a qualitative assessment to determine if it was more likely than not that the fair value of the reporting unit exceeded its carrying value, including goodwill. The qualitative assessment indicated that it was more likely than not that the fair value of the reporting unit exceeded its carrying value, resulting in no impairment.

The company also performed a Step 1 quantitative analysis which determined that the fair value of the reporting unit exceeded its carrying value, including goodwill, confirming the qualitative assessment and resulting in no impairment.

Acquired Intangible Assets: Acquired intangible assets were as follows at year-end:

	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
December 31, 2018			
Customer lists	**$ 3,101**	**$ (1,269)**	**$ 1,832**
Non-compete agreements	**951**	**(386)**	**565**
Trade name	**232**	**(94)**	**138**
	$ 4,284	**$ (1,749)**	**$ 2,535**
December 31, 2017			
Customer lists	$ 3,101	$ (1,063)	$ 2,038
Non-compete agreements	951	(322)	629
Trade name	232	(79)	153
	$ 4,284	$ (1,464)	$ 2,820

Aggregate amortization expense was $286 and $286 for 2018 and 2017.

Estimated amortization expense for each of the next five years:

2019	$ 286
2020	286
2021	286
2022	286
2023	286

(Dollar amounts in thousands except per share data)

Note 7 - Deposits

A summarized analysis of the Bank's deposits at December 31, 2018 and 2017 follows:

	2018	2017
Non-interest bearing demand accounts	**$ 240,432**	$ 201,936
Interest-bearing demand accounts	**159,465**	124,833
Money market accounts	**294,497**	271,702
Savings accounts	**111,936**	101,602
Certificates of Deposit	**98,678**	108,717
Total deposits	**$ 905,008**	$ 808,790

Time deposits that meet or exceed the FDIC insurance limit of $250 at year-end 2018 and 2017 were $29,649 and $32,199 respectively.

Scheduled maturities of time deposits for the next five years are as follows:

2019	$ 1,505
2020	84,267
2021	7,835
2022	5,071
2023	-
	$ 98,678

Deposits of executive officers, directors and principal officers of the Company, including their immediate families and companies, in which they are principal owners (more than 10%), amounted to $4,312 and $7,000 at December 31, 2018 and 2017, respectively.

Note 8 - FHLB Advances

At year-end, FHLB Advances were as follows:

	2018		2017	
	Amount	**Rate**	Amount	Rate
Federal Home Loan Bank (FHLB) advances	**$ 35,500**	**2.27%**	$ 20,000	1.35%

Each FHLB advance is payable at its maturity date, with a prepayment penalty for fixed rate advances. The advances were collateralized by $267,820 and $77,462 of securities and first mortgage loans on commercial and residential properties under a blanket lien arrangement at year-end 2018 and 2017. All FHLB advances mature during 2019.

Based on the collateral and the Company’s holding of FHLB stock, the Company is eligible to borrow up to a total of $183,842 at year-end 2018.

Note 9 - Note Payable

At year-end, the Note Payable was as follows:

	2018		2017	
	Amount	**Rate**	Amount	Rate
Note payable	**$ 3,057**	**6.00%**	$ 3,113	6.00%

The note payable is payable in monthly installments of $20 of principal and interest, is unsecured, and matures with a balloon payment in November, 2019.

(Dollar amounts in thousands except per share data)

Note 10 - Pension and other Post Retirement Plans

The Bank has a funded noncontributory defined benefit pension plan that covers substantially all employees meeting certain eligibility requirements. The pension plan was closed to new participants and benefit accruals were frozen as of December 31, 2015. The plan provides defined benefits based on years of service and final average salary. The Company uses December 31 as the measurement date for its pension plans.

Information about changes in obligations and plan assets of the defined benefit pension plan follows:

	2018	2017
Change in projected benefit obligation:		
Beginning of year	**$ 26,447**	$ 24,772
Service cost	**156**	158
Interest cost	**1,010**	1,058
Benefits paid	**(1,636)**	(1,326)
Actuarial (gain) loss	**(2,148)**	1,785
End of year	**$ 23,829**	$ 26,447
Change in fair value of assets:		
Beginning of year	**$ 25,075**	$ 18,539
Contributions	**2,949**	5,083
Actual return on plan assets	**(1,428)**	2,778
Benefits paid and expenses	**(1,641)**	(1,325)
End of year	**$ 24,955**	$ 25,075

	2018	2017
Funded status at end of year (plan assets less benefit obligation)	**$ 1,125**	$ (1,372)

Amounts recognized in accumulated other comprehensive loss at December 31 consist of:

	2018	2017
Total net actuarial loss	**$ (7,063)**	$ (6,321)
Transistion asset	**171**	219
	$ (6,892)	$ (6,102)

The accumulated benefit obligation was $23,829 and $26,447 at year-end 2018 and 2017.

Components of Net Periodic Benefit Cost and Other Amounts Recognized in Other Comprehensive Income:

	2018	2017
Service cost	**$ 156**	$ 158
Interest cost	**1,010**	1,058
Expected return on plan assets	**(1,577)**	(1,154)
Amortization of transition cost	**(48)**	(48)
Amortization of net loss	**121**	123
Net periodic benefit cost	**$ (338)**	$ 137
Net loss	**$ 863**	$ 161
Amortization of transition asset	**48**	48
Amortization of prior service cost	**(121)**	(123)
Total recognized in other comprehensive loss	**$ 790**	86
Total recognized in net periodic benefit cost and other comprehensive loss	**$ 451**	$ 223

The estimated net loss and prior service costs for the defined benefit pension plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $159 and $(48).

(Dollar amounts in thousands except per share data)

Note 10 - Pension and other Post Retirement Plans (continued)

Assumptions

Weighted-average assumptions used to determine the benefit obligations at year-end:

	2018	2017
Discount rate	**4.53%**	3.94%
Rate of compensation increase	**0.00%**	0.00%

Weighted-average assumptions used to determine net periodic pension cost:

	2018	2017
Discount rate	**3.94%**	4.41%
Expected long-term rate of return on plan assets	**6.50%**	6.50%
Rate of compensation increase	**0.00%**	0.00%

Investment Strategy and Allocation

The Company is a participant in the New York State Bankers Retirement System (the "System"). The System's overall investment strategy is to achieve a mix of approximately 97% of investments for long-term growth and 3% for near-term benefit payments with a wide diversification of asset types, fund strategies, and fund managers. The target allocations for the System assets are shown in the table below. Cash equivalents consist primarily of government issues (maturing in less than three months) and short term investment funds. Equity securities primarily include investments in common stock, depository receipts, preferred stock, commingled pension trust funds, exchange traded funds and real estate investment trusts. Fixed income securities include corporate bonds, government issues, credit card receivables, mortgage backed securities, municipals, commingled pension trust funds and other asset backed securities. Other investments are real estate interests and related investments held within a commingled pension trust fund.

The weighted average expected long-term rate of return is estimated based on current trends in the System's assets as well as projected future rates of return on those assets and reasonable actuarial assumptions based on the guidance provided by Actuarial Standard of Practice ("ASOP") No. 27 "Selection of Economic Assumptions for Measuring Pension Obligations" for long term inflation, and the real and nominal rate of investment return for a specific mix of asset classes.

The following assumptions were used in determining the long-term rate of return:

Equity securities	Dividend discount model, the smoothed earnings yield model and the equity risk premium model
Fixed income securities	Current yield-to-maturity and forecasts of future yields
Other financial instruments	Comparison of the specific investment's risk to that of fixed income and equity instruments and other judgments

The long-term rate of return considers historical returns. Adjustments were made to historical returns in order to reflect 333expectations of future returns. These adjustments were due to factor forecasts by economists and long-term U.S. Treasury yields to forecast long-term inflation. In addition, forecasts by economists and others for long-term GDP growth were factored into the development of assumptions for earnings growth and per capita income.

The System currently prohibits its investment managers from purchasing any security greater than 5% of the portfolio at the time of purchase or greater than 8% at market value in any one issuer. Effective June 25, 2013, the issuer of any security purchased must be located in a country in the MSCI (Morgan Stanley Capital International) World Index. In addition, the following are prohibited: Short sales, unregistered stocks and margin purchases of equity securities, mortgage backed derivatives that have an inverse floating rate coupon or that are interest only securities, any asset backed security that is not issued by the U.S. Government or its agencies or its instrumentalities, securities of less than Baa2/BBB quality may not be purchased, securities of less than A-quality may not in the aggregate exceed 13% of the investment manager's portfolio. An investment manager's portfolio of commercial mortgage-backed securities and asset backed securities shall not exceed 10% of the portfolio at the time of purchase. In addition, unhedged currency exposure in countries not defined as "high income economies" by the World Bank is prohibited.

(Dollar amounts in thousands except per share data)

Note 10 - Pension and other Post Retirement Plans (continued)

The target allocation range below is both historic and prospective in that it has not changed since prior to 2013. It is the asset allocation range that the investment managers have been advised to adhere to and within which they may make tactical asset allocation decisions.

The Company's pension plan asset allocation at year-end 2018 and 2017, target allocation and expected long-term rate of return by asset class are as follows:

	Target Allocation	**2018**	2017	Weighted Average Expected Long-term Rate of Return
Asset category:				
Cash equivalents	0-20%	**4.20%**	6.40%	0.11%
Equity securities	40 - 60%	**46.10%**	50.20%	3.71%
Fixed income securities	40 - 60%	**45.80%**	40.20%	2.24%
Other financial instruments	0-5%	**3.90%**	3.20%	0.30%
Total		**100.00%**	100.00%	

Fair Value of Plan Assets

The Company used the following valuation methods and assumptions to estimate the fair value of assets held by the plan:

Equity Securities: The fair values for equity securities are determined by quoted market prices, if available (Level 1). For securities where quoted prices are not available, fair values are calculated on market prices of similar securities (Level 2).

Fixed Income Securities: Certain fixed income securities are valued at the closing price in the active market in which the bond is traded (Level 1 inputs). Other debt securities are valued on recent bid prices or the average of recent bid and ask price when available (Level 2 inputs) and if not available, they are valued through matrix pricing models developed by sources considered by management to be reliable. Matrix pricing, which is a mathematical technique commonly used to price debt securities that are not actively traded, values 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). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3). Discounted cash flows are calculated using spread to swap and LIBOR curves that are updated to incorporate loss severities, volatility, credit spread and optionality.

Commingled Pension Trust Funds (CPTF): The fair values of CPTF use valuation techniques based on market, income approach, debt service and sales comparison. Unobservable inputs include credit spreads, discount rates, loan to value ratio, terminal capitalization rate and value per square foot (Level 3 inputs).

(Dollar amounts in thousands except per share data)

Note 10 - Pension and other Post Retirement Plans (continued)

The fair value of the plan assets at December 31, 2018, by asset class, is as follows:

		Fair Value Measurements at December 31, 2018 Using:		
	Total	Quoted Prices in Active Markets for Identicle Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash equivalents:				
Foreign currencies	**$ 23**	**$ 23**	**$ -**	**$ -**
Equities:				
Common stock	**10,067**	**10,067**	**-**	**-**
Depository receipts	**171**	**171**	**-**	**-**
Preferred stock	**81**	**81**	**-**	**-**
	10,319	**10,319**	**-**	**-**
Fixed income securities:				
Collateralized mortgage obligations	**633**	**-**	**633**	**-**
Corporate Bonds	**2,470**	**-**	**2,470**	**-**
Government National Mortgage Assoc II	**122**	**-**	**122**	**-**
Government Securities	**8,943**	**-**	**8,943**	**-**
	12,168	**-**	**12,168**	**-**
Other investments				
Commingled pension trust funds-realty	**2,445**	**-**	**-**	**2,445**
	2,445	**-**	**-**	**2,445**
Total plan assets	**$ 24,955**	**$ 10,342**	**$ 12,168**	**$ 2,445**

The fair value of the plan assets at December 31, 2017, by asset class, is as follows:

		Fair Value Measurements at December 31, 2017 Using:		
	Total	Quoted Prices in Active Markets for Identicle Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash equivalents:				
Foreign currencies	$ 247	$ 247	$ -	$ -
Short term investment funds	68	-	68	-
	315	247	68	-
Equities:				
Common Stock	4,940	4,940	-	-
Depository Receipts	125	125	-	-
Exchange Traded Funds	109	109		
Commingled pension trust funds	7,769	-	7,769	-
	12,943	5,174	7,769	-
Fixed income securities:				
Collateralized mortgage obligations	199	-	199	-
Commingled pension trust funds	6,158	-	6,158	-
Corporate Bonds	1,043	-	1,043	-
Federal National Mortgage Assoc	57	-	57	-
Government Securities	3,441	-	3,441	-
Mortgage Backed Securities	21	-	21	-
	10,919	-	10,919	-
Other Investments				
Commingled pension trust funds-realty	898	-	-	898
	898	-	-	898
Total plan assets	$ 25,075	$ 5,421	$ 18,756	$ 898

(Dollar amounts in thousands except per share data)

Note 10 - Pension and other Post Retirement Plans (continued)

Contributions: The Company contributed $2,949 to its pension plan and $2,343 to other plans during 2018.

Estimated Future Payments: The following benefit payments which reflect future service, are expected:

Estimated future payments	Pension Benefits	Other Benefits
2019	$ 1,316	$ 79
2020	1,315	79
2021	1,319	79
2022	1,393	79
2023	1,450	79
Following 5 years	$ 7,507	$ 396

Supplemental Executive Retirement Plans

The Bank maintains a Supplemental Executive Retirement Plan for two former Chief Executive Officers to restore pension benefits that are limited due to Internal Revenue Service regulations. The benefits accrued under this plan, which are included in accrued expenses and other liabilities in the Consolidated Statements of Condition, were $751 and $772 as of December 31, 2018 and 2017. The Bank recorded expense of $59 and $59 in 2018 and 2017 in relation to this plan. Supplemental benefits for this plan expected to be paid in each year from 2019 to 2023 are $79, $79, $79, $79, $79, respectively. The aggregate supplemental benefits expected to be paid in the five years from 2024 to 2028 are $396.

The Bank also maintains a performance based Supplemental Executive Retirement Plan for the Chief Executive Officer and two Executive Vice Presidents. Contributions to this plan are based on achieving certain growth and profitability targets. The Bank recorded expense of $360 for the year ended 2018. No expense for these plans was recognized during 2017.

Deferred Directors' Fee Plan

The Bank and the Parent Company maintain unfunded Deferred Director's Fee Plans within which each director may defer the receipt of meeting fees. The benefits accrued under these plans totaled $5,261 and $4,572 at December 31, 2018 and 2017. The Bank and the Parent Company recorded an expense of $736 and $625 in 2018 and 2017 in relation to these plans.

Deferred Compensation Plan

The Bank and HVIA maintain unfunded Deferred Compensation Plans for certain officers. The benefits accrued under these plans totaled $624 and $836 at December 31, 2018 and 2017. The Bank and HVIA recorded an expense of $48 and $59 in 2018 and 2017, respectively.

Deferred Incentive Retirement Plan

The Bank maintains an unfunded Deferred Incentive Retirement Plan for certain executive officers. The benefits accrued under this plan totaled $810 and $890 at December 31, 2018 and 2017. The Bank recorded an expense of $42 and $46 in 2018 and 2017, respectively.

401(k) Savings Plan

The Company has a 401(k) Plan (Plan) to provide retirement and incidental benefits for its employees. Employees may contribute up to 100% of their annual compensation to the Plan, limited to a maximum annual amount as set periodically by the Internal Revenue Service. Effective for Plan Years beginning January 1, 2016, the Company makes a safe harbor nonelective contribution equal to 3% of annual compensation for each eligible employee whether or not the employee elects to defer compensation to the plan. All safe harbor nonelective contributions vest immediately. In addition, effective for Plan Years beginning January 1, 2016, for those employees hired before April 1, 2016, the Plan provides for discretionary contributions according to the following schedule:

(Dollar amounts in thousands except per share data)

Note 10 - Pension and other Post Retirement Plans (continued)

Percentage of Compensation	Participant Age Range
1.0%	Under age 35
2.0%	35 years of age, but less than 45
5.0%	45 years of age, but less than age 55
8.5%	55 years of age or older

Employees are eligible for the discretionary contribution after completing one year of service. All discretionary contributions vest immediately.

Discretionary contributions were $509 and $528 for 2018 and 2017, respectively.

Restricted Stock Grants

The Company has a time based restricted stock plan. For the years ended December 31, 2018 and 2017 the Company's recognized stock-based compensation costs of $203 and $191, respectively. The Company uses the fair value of the common stock on the date of award to measure compensation cost for restricted stock unit awards. Compensation cost is recognized over the vesting period of the award using the straight line method. There were 7,823 and 4,354 restricted stock units granted for the years ended December 31, 2018 and 2017, respectively. The grants generally vest at the rate of 33% per year with full vesting on the third anniversary date of the grant. Unamortized expense at December 31, 2018 was $178.

A summary of the status of the Company's non-vested restricted stock awards as of December 31, 2018, and changes during the year ended December 31, 2018 are presented below:

	Shares	Weighted Average Fair Value
Non-vested at December 31, 2017	16,954	$ 23.12
Granted	7,823	$ 28.00
Vested	(5,378)	$ 23.20
Non-vested at December 31, 2018	19,399	$ 25.08

(Dollar amounts in thousands except per share data)

Note 11 - Income Taxes

Income tax expense was as follows:

	2018	2017
Current expense		
Federal	**$ 1,698**	$ 806
State	**120**	130
Total	**1,818**	936
Deferred expense (benefit)		
Federal	**(78)**	3,256
State	**(607)**	(516)
Total	**(685)**	2,740
Change in valuation allowance	**495**	476
Total provision for income taxes	**$ 1,628**	$ 4,152

Effective tax rates differ from the federal statutory rate of 21% for 2018 and 34% for 2017 applied to income before taxes due to the following:

	2018	2017
Tax expense at statutory rate	**$ 1,928**	$ 2,211
(Decrease) increase in taxes resulting from:		
Net earnings on bank-owned life insurance	**(145)**	(240)
Tax-exempt municipal bond income, net of disallowed interest expense	**(288)**	(647)
State income tax, net of federal tax benefit	**(430)**	(169)
Valuation allowance	**495**	475
Other	**68**	118
Impact of Tax Cuts and Jobs Act ("TCJA")	**-**	2,404
Total provision for income tax	**$ 1,628**	$ 4,152

Year-end deferred tax assets and liabilities were due to the following:

	2018	2017
Deferred tax assets:		
Allowance for loan losses	**$ 2,777**	$ 2,218
Reserve for unfunded commitments and other real estate owned	**217**	170
Deferred loan fees	**466**	440
Deferred compensation	**285**	811
Contribution carryover	**-**	21
Available for sale securities	**1,307**	373
Accumulated depreciation	**101**	-
Non accrual interest	**395**	406
State NOL	**1,133**	892
Pension/deferred compensation OCI	**1,738**	1,530
	8,419	6,861
Deferred tax liabilities:		
Intangible assets	**(581)**	(488)
Organization costs - holding company	**(14)**	(12)
Organization costs - HVIA	**(14)**	(12)
Accumulated depreciation	**-**	(67)
Accretion	**(29)**	(22)
	(638)	(601)
Net deferred tax asset before valuation allowance	**7,781**	6,260
Valuation allowance	**(2,449)**	(1,954)
Net deferred tax asset	**$ 5,332**	$ 4,306

(Dollar amounts in thousands except per share data)

Note 11 - Income Taxes (continued)

The Company has recorded a federal deferred tax asset that based upon an analysis of the evidence, it expects such federal deferred tax asset to be recoverable. The federal deferred tax asset is included in other assets on the balance sheet. However, due to the change in New York State tax legislation passed in March 2014, management has determined that a full valuation allowance, totaling $2,449, against the New York State portion of the deferred tax asset, which includes state net operating losses, at December 31, 2018 and 2017 is appropriate. At December 31, 2018, the Company has net operating loss carryforwards available for state income tax purposes of approximately $22.4 million; of which $4.8 million expires in 2025, $6.2 million expires in 2026, and $6.8 million expires in 2027 and $4.6 million in 2028.

The Company did not have any uncertain tax positions at December 31, 2018 and 2017. The Company's policy is to recognize interest and penalties on unrecognized tax benefits in income tax expense in the Consolidated Statements of Income.

The Company and its subsidiaries are subject to U.S. federal income tax as well as income tax of the state of New York. The Company is no longer subject to examination by taxing authorities for years before 2015.

Note 12 – Accumulated Other Comprehensive Income (Loss)

The following is changes in accumulated other comprehensive income (loss) by component, net of tax, for the years ending December 31, 2018 and 2017.

	Unrealized Gains and Losses on Available-for-Sale Securities	Defined Benefit Pension Items	Deferred Compensation Liability	Total
December 31, 2018				
Beginning balance	$ (1,062)	$ (4,567)	$ 166	$ (5,463)
Other comprehensive income before reclassification	(2,650)	(645)	(291)	(3,586)
Amounts reclassified from accumulated other comprehensive income	0	63	0	63
Net current period other comprehensive income	(2,650)	(582)	(291)	(3,523)
Ending balance	$ (3,712)	$ (5,149)	$ (125)	$ (8,986)

(Dollar amounts in thousands except per share data)

Note 12 – Accumulated Other Comprehensive Income (Loss) (continued)

	Unrealized Gains and Losses on Available-for-Sale Securities	Defined Benefit Pension Items	Deferred Compensation Liability	Total
December 31, 2017				
Beginning balance	$ (525)	(3,730)	81	(4,174)
Other comprehensive income before reclassification	(158)	(97)	54	(201)
Amounts reclassified from accumulated other comprehensive income	(182)	45	0	(137)
Net current period other comprehensive income	(340)	(52)	54	(338)
Reclassification for ASU 2018-02 Tax Act Adjustment	(197)	(785)	31	(951)
Ending balance	$ (1,062)	$ (4,567)	$ 166	$ (5,463)

The following is significant amounts reclassified out of each component of accumulated other comprehensive income (loss) for the years ending December 31, 2018 and 2017.

Details about Accumulated Other Comprehensive Income Components	Amount Reclassified from Accumulated Other Comprehensive Income		Affected Line Item in the Statement where Net Income is Presented
	2018	2017	
Unrealized gains and losses on available-for-sale securities			
Realized gains on securities available-for-sale	$ -	$ 302	Investment security gains
Total before tax	-	302	
Tax effect	-	120	Provision for income taxes
Net of tax	$ -	$ 182	
Amortization of defined benefit pension items			
Transition asset	(48)	(48)	Other expense
Actuarial gains (losses)	$ 121	$ 123	Other expense
Total before tax	73	75	
Tax effect	10	30	Provision for income taxes
Net of tax	$ 63	$ 45	
Total reclassifications for the period, net of tax	$ 63	$ 137	

(Dollar amounts in thousands except per share data)

Note 13 - Regulatory Capital Matters

Banks and bank holding companies are subject to regulatory capital requirements administered by the federal banking agencies. Capital adequacy guidelines and additionally for banks, prompt corrective regulations, involve quantitative measures of assets, liabilities and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgements by regulators. Failure to meet the minimum capital requirements can initiate regulatory action. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks, (Basel III rules), became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Under the Basel III rules, the Bank must hold a capital conservation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer is being phased in at a rate of 0.625% per year from 0.0% in 2015 to 2.5% for 2019. The capital conservation buffer for 2018 is 1.875% and for 2017 is 1.25%. The net unrealized gain or loss on available for sale securities is included in computing regulatory capital. Management believes as of December 31, 2018, the Company and the Bank meet all capital adequacy requirements to which they are subject. The Company is not currently subject to capital requirements.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion and capital restoration plans are required. At year-end 2018 and 2017, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes changed that category.

Actual and required capital amounts and ratios are presented below at year-end.

Bank	Actual		For Capital Adequacy Purposes		For Capital Adequacy Purposes with Capital Buffer		To be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
2018								
Total capital to risk weighted assets	**111,932**	**14.93%**	**59,988**	**≥8.0%**	**74,048**	**≥9.875%**	**74,985**	**≥10.0%**
Tier 1 (Core) capital to risk weighted assets	**102,533**	**13.67%**	**44,991**	**≥6.0%**	**59,051**	**≥7.875%**	**59,988**	**≥8.0%**
Common Tier 1 (CET1) to risk weighted assets	**102,533**	**13.67%**	**33,743**	**≥4.5%**	**47,803**	**≥6.375%**	**48,741**	**≥6.5%**
Tier 1 (Core) Capital to average assets	**102,533**	**9.67%**	**42,420**	**≥4.0%**	**N/A**	**N/A**	**53,025**	**≥5.0%**
2017								
Total capital to risk weighted assets	97,799	16.08%	48,660	≥8.0%	56,263	≥9.25%	60,825	≥10.0%
Tier 1 (Core) capital to risk weighted assets	90,176	14.83%	36,495	≥6.0%	44,098	≥7.25%	48,660	≥8.0%
Common Tier 1 (CET1) to risk weighted assets	90,176	14.83%	27,371	≥4.5%	34,975	≥5.75%	39,537	≥6.5%
Tier 1 (Core) Capital to average assets	90,176	9.29%	38,812	≥4.0%	N/A	N/A	48,515	≥5.0%

Dividend Restrictions: The Company'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. As of Decemebr31, 2018, $3,838 of retained earnings is available to pay dividends.

(Dollar amounts in thousands except per share data)

Note 14 - Branch Sale

On December 13, 2017, the Company entered into Purchase and Assumption Agreement with Salisbury Bank and Trust Company ("Salisbury) whereby Salisbury agreed to purchase the assets and assume the liabilities of the Company's Fishkill, NY branch. Under the terms of the agreement, Salisbury purchased the branch assets, with the exception of leasehold improvements and equipment, and assumed the liabilities at the Company's carrying value at the date of the acquisition. In addition to assuming the deposits held by the branch, Salisbury also assumed the remaining obligations under the operating lease in existence at closing. Leasehold improvements and equipment were purchased at the Company's carrying value net of a $150 discount, at the acquisition date. At December 31, 2017, the Company reclassified loans in the amount of $11,614 from the loan portfolio to loans held for sale, leasehold improvements and equipment in the amount of $933 from premises and equipment to premises and equipment held for sale, and deposits in the amount of $23,755 to deposits held for sale. In 2017, the Company recorded a $150 impairment charge on the premises and equipment held for sale, to reflect the contractual discount, which was recorded as other expense in the Company's consolidated statement of income. The purchase and assumption closed on April 13, 2018 in accordance with the terms of the agreement. At the time of the closing Salisbury acquired loans in the amount of $7,849, leasehold improvements and equipment in the amount of $761, other assets in the amount of approximately $83, and deposits in the amount of $8,323. The Company received a cash payment, from Salisbury, in the amount of approximately $375 at closing.

Note 15 - Revenue from Contracts with Customers

All of the Company's revenue from contracts with customers in the scope of ASC 606 is recognized within Other Operating Income. The following table presents the Company's sources of Other Operating Income for the twelve months ended December 31, 2018. Items outside the scope of ASC 606 are noted as such.

	Year Ended December 31, 2018	Year Ended December 31, 2017
Other Operating Income		
Service charges on deposit accounts	**$ 932**	$ 966
Trust income	**3,165**	2,987
Investment advisory income	**4,332**	4,158
Investment securities gains [(a)]	**-**	302
Earnings on bank-owned life insurance [(a)]	**691**	706
Gain on the sale of other real estate owned	**-**	28
Other [(b)]	**899**	772
Total Other Operating Income	**$ 10,019**	$ 9,919

(a) Not within the scope of ASC 606.

(b) The Other category includes safe deposit income, checkbook fees, and debit card fee income, totaling $633 that are within the scope of ASC 606 and loan related fee income and miscellaneous income, totaling $266 which are outside the scope of ASC 606.

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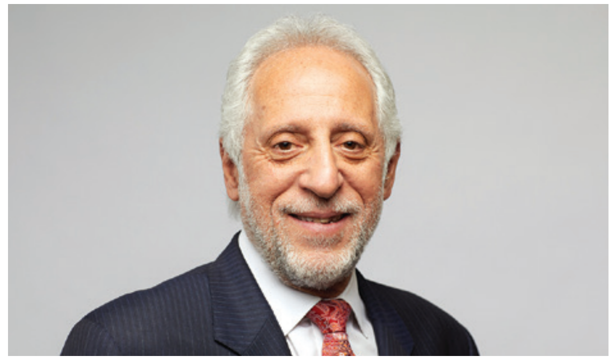
President & CEO



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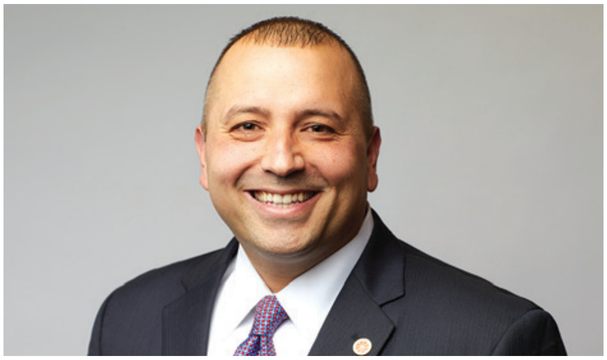

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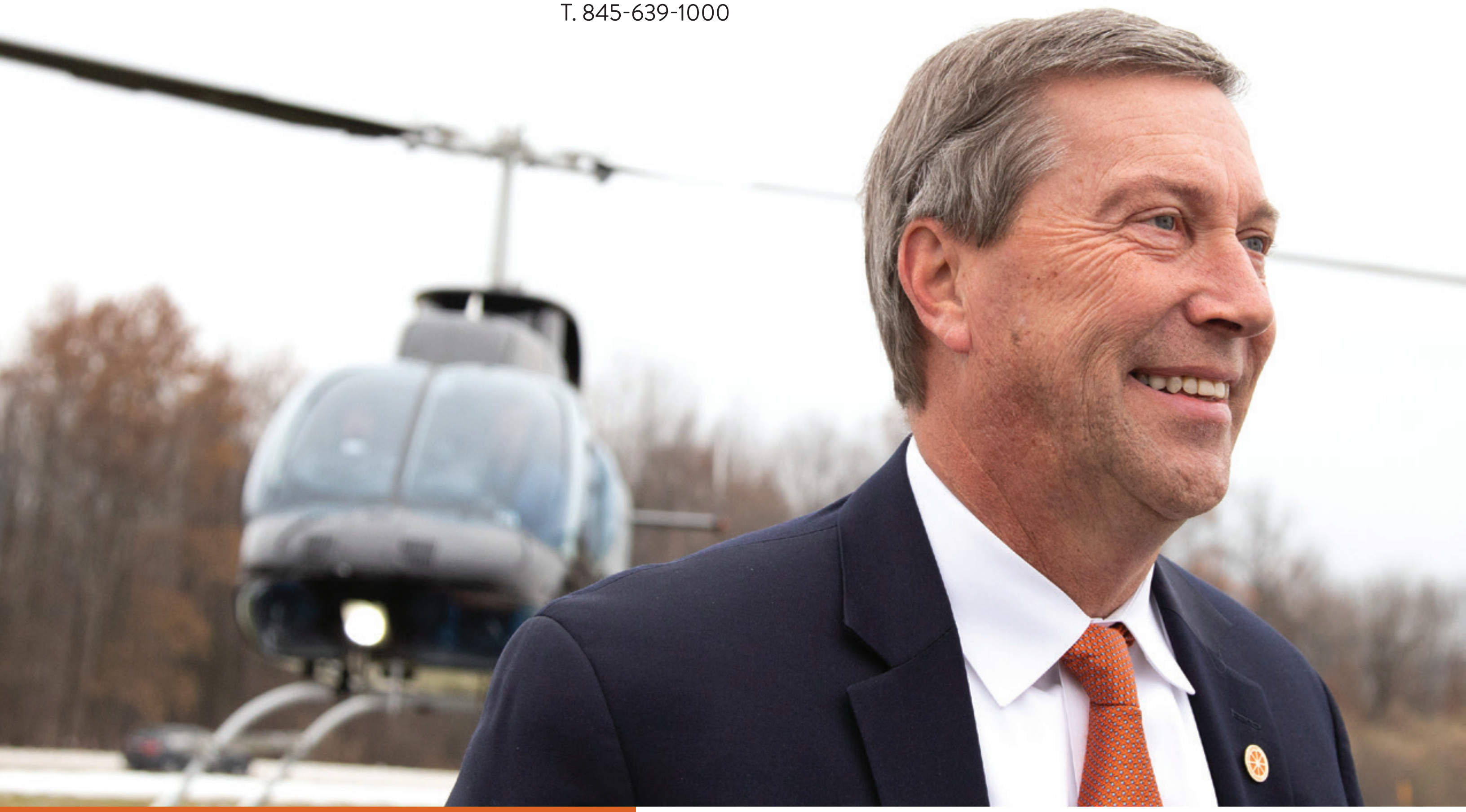

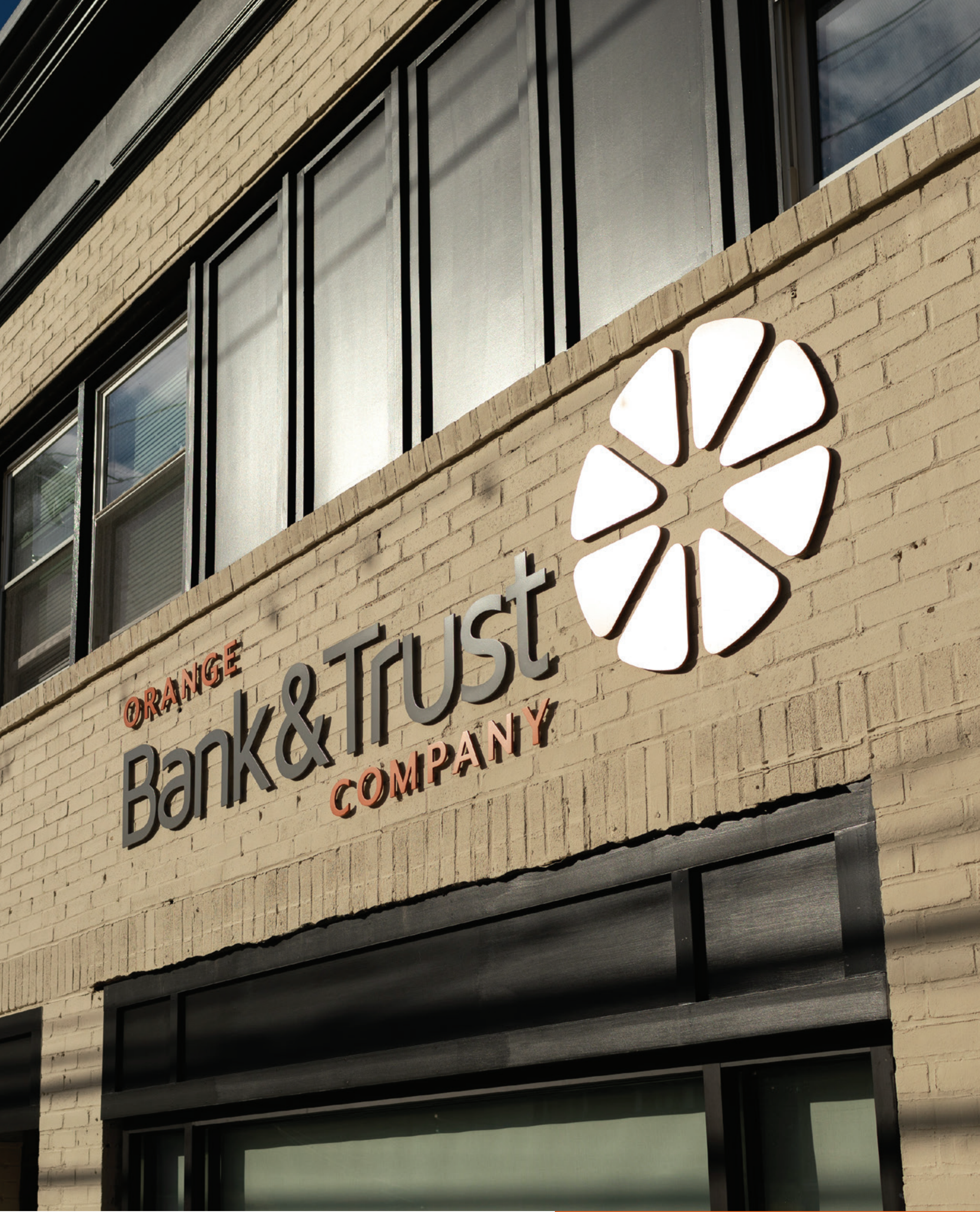
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