Section 1: 10-Q (10-Q)

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)
[X] **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2019

OR

[ ] **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

ENB Financial Corp
(Exact name of registrant as specified in its charter)

Pennsylvania	000-53297	51-0661129
(State or Other Jurisdiction of Incorporation)	(Commission File Number)	(IRS Employer Identification No)
31 E. Main St., Ephrata, PA	17522-0457	
(Address of principal executive offices)	(Zip Code)	

Registrant’s telephone number, including area code (717) 733-4181

Former name, former address, and former fiscal year, if changed since last report Not Applicable

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
None.	N/A	N/A

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.)

Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☐	Accelerated filer	☐
Non-accelerated filer	☐	Smaller reporting company	☒
		Emerging growth company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ☐ No ☒

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date. As of **November 1, 2019,** the registrant had **5,638,362** shares of $0.10 (par) Common Stock outstanding.

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September 30, 2019

Part I - Financial Information
Item 1. Financial Statements

CONSOLIDATED BALANCE SHEETS (UNAUDITED)
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	September 30, 2019 $	December 31, 2018 $	September 30, 2018 $
ASSETS			
Cash and due from banks	**23,856**	26,675	17,097
Interest-bearing deposits in other banks	**17,334**	14,690	11,091
Total cash and cash equivalents	**41,190**	41,365	28,188
Securities available for sale (at fair value)	**298,983**	294,065	295,335
Equity securities (at fair value)	**6,108**	5,934	5,789
Loans held for sale	**1,578**	1,429	2,804
Loans (net of unearned income)	**738,104**	694,073	667,769
Less: Allowance for loan losses	**9,474**	8,666	8,428
Net loans	**728,630**	685,407	659,341
Premises and equipment	**25,247**	25,551	25,730
Regulatory stock	**7,200**	6,348	6,392
Bank owned life insurance	**28,610**	28,085	27,901
Other assets	**8,452**	9,658	10,715
Total assets	**1,145,998**	1,097,842	1,062,195
LIABILITIES AND STOCKHOLDERS' EQUITY			
Liabilities:			
Deposits:			
Noninterest-bearing	**347,929**	369,081	346,827
Interest-bearing	**599,062**	550,653	544,099
Total deposits	**946,991**	919,734	890,926
Short-term borrowings	—	7,870	1,074
Long-term debt	**79,989**	65,386	68,361
Other liabilities	**3,381**	2,050	2,632
Total liabilities	**1,030,361**	995,040	962,993
Stockholders' equity:			
Common stock, par value $0.10 as of 9/30/19; $0.20 as of 12/31/18 and 9/30/18			
Shares: Authorized 24,000,000 as of 9/30/19; 12,000,000 as of 12/31/18 and 9/30/18			
Issued 5,739,114 and Outstanding 5,677,161 as of 9/30/19			
Issued 2,869,557 and Outstanding 2,852,532 as of 12/31/18			
Issued 2,869,557 and Outstanding 2,861,274 as of 9/30/18	**574**	574	574
Capital surplus	**4,471**	4,435	4,436
Retained earnings	**110,067**	104,067	102,670
Accumulated other comprehensive income (loss) net of tax	**1,685**	(5,678)	(8,200)
Less: Treasury stock cost on 61,953 shares as of 9/30/19 17,025 shares as of 12/31/18 and 8,283 shares as of 9/30/18	**(1,160)**	(596)	(278)
Total stockholders' equity	**115,637**	102,802	99,202
Total liabilities and stockholders' equity	**1,145,998**	1,097,842	1,062,195

See Notes to the Unaudited Consolidated Interim Financial Statements

ENB FINANCIAL CORP

CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	Three Months ended September 30,		Nine Months ended September 30,	
	2019	2018	**2019**	2018
	$	$	**$**	$
Interest and dividend income:				
Interest and fees on loans	**8,501**	7,157	**24,833**	20,259
Interest on securities available for sale				
Taxable	**1,179**	1,207	**3,696**	3,494
Tax-exempt	**605**	701	**1,860**	2,196
Interest on deposits at other banks	**128**	141	**294**	388
Dividend income	**177**	142	**531**	432
Total interest and dividend income	**10,590**	9,348	**31,214**	26,769
Interest expense:				
Interest on deposits	**889**	512	**2,626**	1,503
Interest on borrowings	**412**	360	**1,158**	985
Total interest expense	**1,301**	872	**3,784**	2,488
Net interest income	**9,289**	8,476	**27,430**	24,281
Provision for loan losses	**630**	190	**840**	470
Net interest income after provision for loan losses	**8,659**	8,286	**26,590**	23,811
Other income:				
Trust and investment services income	**538**	449	**1,580**	1,477
Service fees	**701**	853	**2,024**	2,351
Commissions	**734**	658	**2,145**	1,899
Gains (losses) on the sale of debt securities, net	**42**	4	**229**	(24)
Gains on equity securities, net	**7**	3	**51**	50
Gains on sale of mortgages	**606**	515	**1,370**	1,102
Earnings on bank-owned life insurance	**186**	186	**543**	1,477
Other income	**129**	119	**307**	463
Total other income	**2,943**	2,787	**8,249**	8,795
Operating expenses:				
Salaries and employee benefits	**5,227**	5,197	**15,520**	15,378
Occupancy	**605**	624	**1,825**	1,889
Equipment	**297**	296	**871**	875
Advertising & marketing	**205**	147	**621**	583
Computer software & data processing	**620**	590	**1,886**	1,708
Shares tax	**233**	226	**698**	669
Professional services	**448**	438	**1,479**	1,376
Other expense	**493**	553	**1,727**	1,644
Total operating expenses	**8,128**	8,071	**24,627**	24,122
Income before income taxes	**3,474**	3,002	**10,212**	8,484
Provision for federal income taxes	**550**	425	**1,596**	960
Net income	**2,924**	2,577	**8,616**	7,524
Earnings per share of common stock	**0.51**	0.45	**1.51**	1.32
Cash dividends paid per share	**0.155**	0.145	**0.46**	0.43
Weighted average shares outstanding	**5,685,679**	5,716,004	**5,690,788**	5,708,020

See Notes to the Unaudited Consolidated Interim Financial Statements

ENB FINANCIAL CORP

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)
(DOLLARS IN THOUSANDS)

	Three Months ended September 30,		Nine Months ended September 30,	
	2019	2018	**2019**	2018
	$	$	$	$
Net income	**2,924**	2,577	**8,616**	7,524
Other comprehensive income (loss), net of tax:				
Securities available for sale not other-than-temporarily impaired:				
Unrealized gains (losses) arising during the period	**1,798**	(1,796)	**9,549**	(5,562)
Income tax effect	**(378)**	377	**(2,005)**	1,172
	1,420	(1,419)	**7,544**	(4,390)
(Gains) losses recognized in earnings	**(42)**	(4)	**(229)**	24
Income tax effect	**9**	1	**48**	(5)
	(33)	(3)	**(181)**	19
Other comprehensive income (loss), net of tax	**1,387**	(1,422)	**7,363**	(4,371)
Comprehensive Income	**4,311**	1,155	**15,979**	3,153

See Notes to the Unaudited Consolidated Interim Financial Statements

ENB FINANCIAL CORP

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (UNAUDITED)
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	Common Stock $	Capital Surplus $	Retained Earnings $	Accumulated Other Comprehensive Income (Loss) $	Treasury Stock $	Total Stockholders' Equity $
Balances, June 30, 2018	574	4,424	100,922	(6,778)	(399)	98,743
Net income	—	—	2,577	—	—	2,577
Other comprehensive income net of tax	—	—	—	(1,422)	—	(1,422)
Treasury stock issued - 7,140 shares	—	12	—	—	121	133
Cash dividends paid, $0.145 per share	—	—	(829)	—	—	(829)
Balances, September 30, 2018	574	4,436	102,670	(8,200)	(278)	99,202
Balances, June 30, 2019	574	4,454	108,024	298	(836)	112,514
Net income	**—**	**—**	**2,924**	**—**	**—**	**2,924**
Other comprehensive income net of tax	**—**	**—**	**—**	**1,387**	**—**	**1,387**
			—			
Treasury stock purchased - 22,400 shares	**—**	**—**	**—**	**—**	**(457)**	**(457)**
Treasury stock issued - 7,177 shares	**—**	**17**	**—**	**—**	**133**	**150**
Cash dividends paid, $0.155 per share	**—**	**—**	**(881)**	**—**	**—**	**(881)**
Balances, September 30, 2019	**574**	**4,471**	**110,067**	**1,685**	**(1,160)**	**115,637**
Balances, December 31, 2017	574	4,415	98,629	(3,195)	(664)	99,759
Net income	—	—	7,524	—	—	7,524
Other comprehensive loss net of tax	—	—	—	(4,371)	—	(4,371)
			—			
Change in accounting principal for adoption of ASU 2017-08	—	—	(1,663)	—	—	(1,663)
Reclassification of certain income tax effects from accumulated other comprehensive loss	—	—	634	(634)	—	—
Treasury stock issued - 22,902 shares	—	21	—	—	386	407
Cash dividends paid, $0.43 per share	—	—	(2,454)	—	—	(2,454)
Balances, September 30, 2018	574	4,436	102,670	(8,200)	(278)	99,202
Balances, December 31, 2018	574	4,435	104,067	(5,678)	(596)	102,802
Net income	**—**	**—**	**8,616**	**—**	**—**	**8,616**
Other comprehensive income net of tax	**—**	**—**	**—**	**7,363**	**—**	**7,363**
			—			
Treasury stock purchased - 51,766 shares	**—**	**—**	**—**	**—**	**(991)**	**(991)**
Treasury stock issued - 23,863 shares	**—**	**36**	**—**	**—**	**427**	**463**

Cash dividends paid, $0.46 per share	**—**	**—**	**(2,616)**	**—**	**—**	**(2,616)**
Balances, September 30, 2019	**574**	**4,471**	**110,067**	**1,685**	**(1,160)**	**115,637**

See Notes to the Unaudited Consolidated Interim Financial Statements

ENB FINANCIAL CORP

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(DOLLARS IN THOUSANDS)

	Nine Months Ended September 30,	
	2019	2018
	$	$
Cash flows from operating activities:		
Net income	**8,616**	7,524
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization of securities premiums and discounts and loan fees	**2,592**	3,024
Amortization of operating leases right-of-use assets	**131**	—
Increase in interest receivable	**(76)**	(36)
Increase in interest payable	**119**	33
Provision for loan losses	**840**	470
(Gain) loss on sale of debt securities, net	**(229)**	24
Gain on equity securities, net	**(51)**	(50)
Gains on sale of mortgages	**(1,370)**	(1,102)
Loans originated for sale	**(35,657)**	(32,227)
Proceeds from sales of loans	**36,878**	33,417
Earnings on bank-owned life insurance	**(543)**	(1,477)
Depreciation of premises and equipment and amortization of software	**1,171**	1,217
Deferred income tax	**(416)**	(10)
Other assets and other liabilities, net	**828**	2,267
Net cash provided by operating activities	**12,833**	13,074
Cash flows from investing activities:		
Securities available for sale:		
Proceeds from maturities, calls, and repayments	**20,908**	13,048
Proceeds from sales	**35,818**	45,734
Purchases	**(54,437)**	(49,968)
Equity securities		
Proceeds from sales	**168**	222
Purchases	**(163)**	(311)
Purchase of regulatory bank stock	**(2,749)**	(1,860)
Redemptions of regulatory bank stock	**1,897**	1,262
Net increase in loans	**(44,441)**	(70,880)
Purchases of premises and equipment, net	**(787)**	(1,135)
Purchase of computer software	**(68)**	(58)
Net cash used for investing activities	**(43,854)**	(63,946)
Cash flows from financing activities:		
Net increase in demand, NOW, and savings accounts	**23,701**	35,324
Net increase (decrease) in time deposits	**3,556**	(10,875)
Net (decrease) increase in short-term borrowings	**(7,870)**	1,074
Proceeds from long-term debt	**24,723**	14,161
Repayments of long-term debt	**(10,120)**	(11,650)
Dividends paid	**(2,616)**	(2,454)
Proceeds from sale of treasury stock	**463**	407
Treasury stock purchased	**(991)**	—
Net cash provided by financing activities	**30,846**	25,987
Decrease in cash and cash equivalents	**(175)**	(24,885)
Cash and cash equivalents at beginning of period	**41,365**	53,073
Cash and cash equivalents at end of period	**41,190**	28,188
Supplemental disclosures of cash flow information:		
Interest paid	**3,664**	2,457
Income taxes paid	**1,300**	375
Supplemental disclosure of non-cash investing and financing activities:		
Fair value adjustments for securities available for sale	**(9,320)**	5,479
Initial recognition of operating right-of-use assets	**1,075**	—
Initial recognition of operating lease liabilities	**1,075**	—

See Notes to the Unaudited Consolidated Interim Financial Statements

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited consolidated interim financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and to general practices within the banking industry. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all significant adjustments considered necessary for fair presentation have been included. Certain items previously reported have been reclassified to conform to the current period's reporting format. Such reclassifications did not affect net income or stockholders' equity.

ENB Financial Corp ("the Corporation") is the bank holding company for its wholly-owned subsidiary Ephrata National Bank (the "Bank"). This Form 10-Q, for the third quarter of 2019, is reporting on the results of operations and financial condition of ENB Financial Corp.

Operating results for the three and nine months ended September 30, 2019, are not necessarily indicative of the results that may be expected for the year ended December 31, 2019. For further information, refer to the consolidated financial statements and footnotes thereto included in ENB Financial Corp's Annual Report on Form 10-K for the year ended December 31, 2018.

Revenue from Contracts with Customers

The Company records revenue from contracts with customers in accordance with Accounting Standards Topic 606, *Revenue from Contracts with Customers (Topic 606).* Under Topic 606, the Corporation must identify contracts with customers, identify the performance obligations in the contract, determine the transaction price, allocate the transaction price to the performance obligations in the contract, and recognize revenue when the Corporation satisfies a performance obligation. Significant revenue has not been recognized in the current reporting period that results from performance obligations satisfied in previous periods.

The Corporation's primary sources of revenue are derived from interest and dividends earned on loans, investment securities, and other financial instruments that are not within the scope of Topic 606. The Corporation has evaluated the nature of its contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is presented in the Consolidated Statements of Income was not necessary. The Corporation generally fully satisfies its performance obligations on its contracts with customers as services are rendered and the transaction prices are typically fixed; charged either on a periodic basis or based on activity. Because performance obligations are satisfied as services are rendered and the transaction prices are fixed, there is little judgment involved in applying Topic 606 that significantly affects the determination of the amount and timing of revenue from contracts with customers.

Leases

ASU 2016-02, "Leases (Topic 842)." ASU 2016-02, among other things, requires lessees to recognize a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. ASU 2016-02 does not significantly change lease accounting requirements applicable to lessors; however, certain changes were made to align, where necessary, lessor accounting with the lessee accounting model and *ASC Topic 606, "Revenue from Contracts with Customers*." ASU 2016-02 became effective for the Corporation on January 1, 2019 and initially required transition using a modified retrospective approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. In July 2018, the FASB issued ASU 2018-11, *"Leases (Topic 842) - Targeted Improvements,"* which, among other things, provided an additional transition method that allowed entities to not apply the guidance in ASU 2016-02 in the comparative periods presented in the financial statements and instead recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. In December 2018, the FASB also issued *ASU 2018-20, "Leases (Topic 842) - Narrow-Scope Improvements for Lessors,"* which provided for certain policy elections and changed lessor accounting for sales and similar taxes and certain lessor costs. Upon adoption of ASU 2016-02, ASU 2018-11 and ASU 2018-20 on January 1, 2019, the Corporation recognized right-of-use assets and related lease liabilities of $1,075,000.

2. Securities Available for Sale

The amortized cost, gross unrealized gains and losses, and fair value of securities held at September 30, 2019, and December 31, 2018, are as follows:

(DOLLARS IN THOUSANDS)	Amortized Cost $	Gross Unrealized Gains $	Gross Unrealized Losses $	Fair Value $
September 30, 2019				
U.S. government agencies	**35,398**	**42**	**(124)**	**35,316**
U.S. agency mortgage-backed securities	**46,354**	**121**	**(564)**	**45,911**
U.S. agency collateralized mortgage obligations	**54,510**	**352**	**(202)**	**54,660**
Asset-backed securities	**19,787**	**—**	**(219)**	**19,568**
Corporate bonds	**54,672**	**176**	**(176)**	**54,672**
Obligations of states and political subdivisions	**86,129**	**2,729**	**(2)**	**88,856**
Total securities available for sale	**296,850**	**3,420**	**(1,287)**	**298,983**
December 31, 2018				
U.S. government agencies	31,025	5	(910)	30,120
U.S. agency mortgage-backed securities	46,363	2	(1,726)	44,639
U.S. agency collateralized mortgage obligations	55,182	74	(1,166)	54,090
Asset-backed securities	11,440	—	(41)	11,399
Corporate bonds	61,085	—	(1,893)	59,192
Obligations of states and political subdivisions	96,157	69	(1,601)	94,625
Total securities available for sale	301,252	150	(7,337)	294,065

The amortized cost and fair value of securities available for sale at September 30, 2019, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities due to certain call or prepayment provisions.

CONTRACTUAL MATURITY OF DEBT SECURITIES
(DOLLARS IN THOUSANDS)

	Amortized Cost $	Fair Value $
Due in one year or less	**26,772**	**26,709**
Due after one year through five years	**137,835**	**137,620**
Due after five years through ten years	**26,759**	**26,747**
Due after ten years	**105,484**	**107,907**
Total debt securities	**296,850**	**298,983**

Securities available for sale with a par value of $61,463,000 and $58,668,000 at September 30, 2019, and December 31, 2018, respectively, were pledged or restricted for public funds, borrowings, or other purposes as required by law. The fair value of these pledged securities was $63,115,000 at September 30, 2019, and $58,914,000 at December 31, 2018.

Proceeds from active sales of securities available for sale, along with the associated gross realized gains and gross realized losses, are shown below. Realized gains and losses are computed on the basis of specific identification.

PROCEEDS FROM SALES OF SECURITIES AVAILABLE FOR SALE
(DOLLARS IN THOUSANDS)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
	$	$	$	$
Proceeds from sales	**7,169**	13,092	**35,818**	45,734
Gross realized gains	**43**	20	**261**	130
Gross realized losses	**(1)**	(16)	**(32)**	(154)

Management evaluates all of the Corporation's securities for other than temporary impairment (OTTI) on a periodic basis. No securities in the portfolio had other-than-temporary impairment recorded in the first nine months of 2019 or 2018.

Information pertaining to securities with gross unrealized losses at September 30, 2019, and December 31, 2018, aggregated by investment category and length of time that individual securities have been in a continuous loss position follows:

TEMPORARY IMPAIRMENTS OF SECURITIES
(DOLLARS IN THOUSANDS)

	Less than 12 months		More than 12 months		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
	$	$	$	$	$	$
As of September 30, 2019						
U.S. government agencies	**—**	**—**	**18,873**	**(124)**	**18,873**	**(124)**
U.S. agency mortgage-backed securities	**2,024**	**(11)**	**29,147**	**(553)**	**31,171**	**(564)**
U.S. agency collateralized mortgage obligations	**14,627**	**(17)**	**22,122**	**(185)**	**36,749**	**(202)**
Asset-backed securities	**17,643**	**(219)**	**—**	**—**	**17,643**	**(219)**
Corporate bonds	**5,088**	**(14)**	**25,017**	**(162)**	**30,105**	**(176)**
Obligations of states & political subdivisions	**511**	**(2)**	**—**	**—**	**511**	**(2)**
Total temporarily impaired securities	**39,893**	**(263)**	**95,159**	**(1,024)**	**135,052**	**(1,287)**
As of December 31, 2018						
U.S. government agencies	—	—	28,116	(910)	28,116	(910)
U.S. agency mortgage-backed securities	—	—	42,041	(1,726)	42,041	(1,726)
U.S. agency collateralized mortgage obligations	8,055	(85)	40,735	(1,081)	48,790	(1,166)
Asset-backed securities	5,563	(41)	—	—	5,563	(41)
Corporate bonds	20,228	(455)	38,964	(1,438)	59,192	(1,893)
Obligations of states & political subdivisions	12,367	(104)	68,982	(1,497)	81,349	(1,601)
Total temporarily impaired securities	46,213	(685)	218,838	(6,652)	265,051	(7,337)

In the debt security portfolio there were 69 positions that were carrying unrealized losses as of September 30, 2019. There were no instruments considered to be other-than-temporarily impaired at September 30, 2019.

The Corporation evaluates fixed maturity positions for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic and market concerns warrant such evaluation. U.S. generally accepted accounting principles provide for the bifurcation of OTTI into two categories: (a) the amount of the total OTTI related to a decrease in cash flows expected to be collected from the debt security (the credit loss), which is recognized in earnings, and (b) the amount of total OTTI related to all other factors, which is recognized, net of taxes, as a component of accumulated other comprehensive income.

3. Equity Securities

The following table summarizes the amortized cost, gross unrealized gains and losses, and fair value of equity securities held at September 30, 2019 and December 31, 2018.

(DOLLARS IN THOUSANDS)	Amortized Cost $	Gross Unrealized Gains $	Gross Unrealized Losses $	Fair Value $
September 30, 2019				
CRA-qualified mutual funds	**5,529**	**—**	**—**	**5,529**
Bank stocks	**601**	**10**	**(32)**	**579**
Total equity securities	**6,130**	**10**	**(32)**	**6,108**

(DOLLARS IN THOUSANDS)	Amortized Cost $	Gross Unrealized Gains $	Gross Unrealized Losses $	Fair Value $
December 31, 2018				
CRA-qualified mutual funds	5,410	—	—	5,410
Bank stocks	591	—	(67)	524
Total equity securities	6,001	—	(67)	5,934

The following table presents the net gains and losses on the Corporation's equity investments recognized in earnings during the three and nine months ended September 30, 2019 and 2018, and the portion of unrealized gains and losses for the period that relates to equity investments held as of September 30, 2019 and 2018.

NET GAINS AND LOSSES ON EQUITY INVESTMENTS RECOGNIZED IN EARNINGS
(DOLLARS IN THOUSANDS)

	Three Months Ended		Nine Months Ended	
	September 30, 2019 $	September 30, 2018 $	September 30, 2019 $	September 30, 2018 $
Net gains recognized in equity securities during the period	**(9)**	(7)	**35**	10
Less: Net gains realized on the sale of equity securities during the period	**16**	10	**16**	40
Unrealized gains recognized in equity securities held at reporting date	**7**	3	**51**	50

4. Loans and Allowance for Loan Losses

The following table presents the Corporation’s loan portfolio by category of loans as of September 30, 2019, and December 31, 2018:

LOAN PORTFOLIO
(DOLLARS IN THOUSANDS)

	September 30, 2019 $	December 31, 2018 $
Commercial real estate		
Commercial mortgages	**113,744**	101,419
Agriculture mortgages	**173,697**	165,926
Construction	**17,661**	18,092
Total commercial real estate	**305,102**	285,437
Consumer real estate (a)		
1-4 family residential mortgages	**250,898**	219,037
Home equity loans	**11,366**	10,271
Home equity lines of credit	**69,113**	64,413
Total consumer real estate	**331,377**	293,721
Commercial and industrial		
Commercial and industrial	**56,690**	61,043
Tax-free loans	**16,575**	22,567
Agriculture loans	**20,918**	20,512
Total commercial and industrial	**94,183**	104,122
Consumer	**5,651**	9,197
Gross loans prior to deferred fees	**736,313**	692,477
Less:		
Deferred loan costs, net	**1,791**	1,596
Allowance for loan losses	**(9,474)**	(8,666)
Total net loans	**728,630**	685,407

(a) Real estate loans serviced for others, which are not included in the Consolidated Balance Sheets, totaled $146,154,000 and $126,916,000 as of September 30, 2019, and December 31, 2018, respectively.

The Corporation grades commercial credits differently than consumer credits. The following tables represent all of the Corporation’s commercial credit exposures by internally assigned grades as of September 30, 2019 and December 31, 2018. The grading analysis estimates the capability of the borrower to repay the contractual obligations under the loan agreements as scheduled. The Corporation's internal commercial credit risk grading system is based on experiences with similarly graded loans.

The Corporation's internally assigned grades for commercial credits are as follows:

- Pass – loans which are protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral.
- Special Mention – loans where a potential weakness or risk exists, which could cause a more serious problem if not corrected.
- Substandard – loans that have a well-defined weakness based on objective evidence and characterized by the distinct possibility that the Corporation will sustain some loss if the deficiencies are not corrected.

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

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

COMMERCIAL CREDIT EXPOSURE
CREDIT RISK PROFILE BY INTERNALLY ASSIGNED GRADE
(DOLLARS IN THOUSANDS)

September 30, 2019	Commercial Mortgages $	Agriculture Mortgages $	Construction $	Commercial and Industrial $	Tax-free Loans $	Agriculture Loans $	Total $
Grade:							
Pass	**111,374**	**157,213**	**16,098**	**50,668**	**16,575**	**18,548**	**370,476**
Special Mention	**836**	**5,685**	**—**	**4,336**	**—**	**1,048**	**11,905**
Substandard	**1,534**	**10,799**	**1,563**	**1,139**	**—**	**1,322**	**16,357**
Doubtful	**—**	**—**	**—**	**547**	**—**	**—**	**547**
Loss	**—**	**—**	**—**	**—**	**—**	**—**	**—**
Total	**113,744**	**173,697**	**17,661**	**56,690**	**16,575**	**20,918**	**399,285**

December 31, 2018	Commercial Mortgages $	Agriculture Mortgages $	Construction $	Commercial and Industrial $	Tax-free Loans $	Agriculture Loans $	Total $
Grade:							
Pass	99,013	154,132	17,567	59,348	22,367	19,487	371,914
Special Mention	176	3,478	525	518	200	453	5,350
Substandard	2,230	8,316	—	1,177	—	572	12,295
Doubtful	—	—	—	—	—	—	—
Loss	—	—	—	—	—	—	—
Total	101,419	165,926	18,092	61,043	22,567	20,512	389,559

Both special mention and substandard loans have increased from December 31, 2018 to September 30, 2019, with the increase in special mention loans more pronounced. Special mention loans increased by $6.5 million over the nine-month period from $5.4 million to $11.9 million, while substandard loans increased by $4.1 million, from $12.3 million to $16.4 million. The larger $6.5 million year-to-date increase in special mention loans was caused by a combination of $2.2 million of dairy mortgages, and a $3.8 million loan to a leasing company migrating from a pass rating to special mention. The smaller $4.1 million increase in substandard loans since December 31, 2018 was due to several dairy loans migrating from special mention to substandard, and a $1.6 million construction loan being reclassified as substandard in the third quarter of 2019 until the conversion to permanent financing can be assured. The Corporation expects this construction loan to be paid off completely in the fourth quarter of 2019.

For the third quarter of 2019, special mention loans increased by $2.1 million, while substandard loans increased by $2.3 million. The additional increases in special mention loans during the third quarter were caused by several dairy farmers migrating from a pass rating to special mention, while the increase in substandard loans was primarily due to the addition of the construction loan mentioned in the year-to-date changes above. The remainder of the substandard loan increase during the third quarter of 2019 was caused by increases in agricultural mortgages and other agricultural loans that were largely offset by decreases in commercial mortgages and C&I loans. The increase in agricultural mortgages was the most pronounced of these with several dairy farm loans being added to substandard during the quarter.

For consumer loans, the Corporation evaluates credit quality based on whether the loan is considered performing or non-performing. Non-performing loans consist of those loans greater than 90 days delinquent and nonaccrual loans. The following tables present the balances of consumer loans by classes of the loan portfolio based on payment performance as of September 30, 2019 and December 31, 2018:

CONSUMER CREDIT EXPOSURE
CREDIT RISK PROFILE BY PAYMENT PERFORMANCE
(DOLLARS IN THOUSANDS)

September 30, 2019 Payment performance:	1-4 Family Residential Mortgages $	Home Equity Loans $	Home Equity Lines of Credit $	Consumer $	Total $
Performing	**250,578**	**11,366**	**69,113**	**5,649**	**336,706**
Non-performing	**320**	**—**	**—**	**2**	**322**
Total	**250,898**	**11,366**	**69,113**	**5,651**	**337,028**

December 31, 2018 Payment performance:	1-4 Family Residential Mortgages $	Home Equity Loans $	Home Equity Lines of Credit $	Consumer $	Total $
Performing	218,641	10,271	64,413	9,196	302,521
Non-performing	396	—	—	1	397
Total	219,037	10,271	64,413	9,197	302,918

The following tables present an age analysis of the Corporation's past due loans, segregated by loan portfolio class, as of September 30, 2019 and December 31, 2018:

AGING OF LOANS RECEIVABLE
(DOLLARS IN THOUSANDS)

September 30, 2019	30-59 Days Past Due $	60-89 Days Past Due $	Greater than 90 Days $	Total Past Due $	Current $	Total Loans Receivable $	Loans Receivable > 90 Days and Accruing $
Commercial real estate							
Commercial mortgages	**—**	**—**	**824**	**824**	**112,920**	**113,744**	**—**
Agriculture mortgages	**437**	**—**	**1,095**	**1,532**	**172,165**	**173,697**	**—**
Construction	**—**	**—**	**—**	**—**	**17,661**	**17,661**	**—**
Consumer real estate							
1-4 family residential mortgages	**557**	**154**	**320**	**1,031**	**249,867**	**250,898**	**320**
Home equity loans	**58**	**—**	**—**	**58**	**11,308**	**11,366**	**—**
Home equity lines of credit	**154**	**—**	**—**	**154**	**68,959**	**69,113**	**—**
Commercial and industrial							
Commercial and industrial	**7**	**—**	**—**	**7**	**56,683**	**56,690**	**—**
Tax-free loans	**—**	**—**	**—**	**—**	**16,575**	**16,575**	**—**
Agriculture loans	**—**	**—**	**—**	**—**	**20,918**	**20,918**	**—**
Consumer	**24**	**4**	**2**	**30**	**5,621**	**5,651**	**2**
Total	**1,237**	**158**	**2,241**	**3,636**	**732,677**	**736,313**	**322**

December 31, 2018	30-59 Days Past Due $	60-89 Days Past Due $	Greater than 90 Days $	Total Past Due $	Current $	Total Loans Receivable $	Loans Receivable > 90 Days and Accruing $
Commercial real estate							
Commercial mortgages	—	—	237	237	101,182	101,419	—
Agriculture mortgages	326	—	816	1,142	164,784	165,926	—
Construction	—	—	—	—	18,092	18,092	—
Consumer real estate							
1-4 family residential mortgages	455	201	396	1,052	217,985	219,037	396
Home equity loans	62	35	—	97	10,174	10,271	—
Home equity lines of credit	95	—	—	95	64,318	64,413	—
Commercial and industrial							
Commercial and industrial	24	—	—	24	61,019	61,043	—
Tax-free loans	—	—	—	—	22,567	22,567	—
Agriculture loans	118	—	—	118	20,394	20,512	—
Consumer	10	15	1	26	9,171	9,197	1
Total	1,090	251	1,450	2,791	689,686	692,477	397

The following table presents nonaccrual loans by classes of the loan portfolio as of September 30, 2019 and December 31, 2018:

NONACCRUAL LOANS BY LOAN CLASS
(DOLLARS IN THOUSANDS)

	September 30, 2019 $	December 31, 2018 $
Commercial real estate		
Commercial mortgages	**824**	1,017
Agriculture mortgages	**1,095**	816
Construction	**—**	—
Consumer real estate		
1-4 family residential mortgages	**—**	—
Home equity loans	**—**	—
Home equity lines of credit	**—**	—
Commercial and industrial		
Commercial and industrial	**547**	—
Tax-free loans	**—**	—
Agriculture loans	**—**	—
Consumer	**—**	—
Total	**2,466**	1,833

As of September 30, 2019 and December 31, 2018, all of the Corporation's commercial loans on nonaccrual status were also considered impaired. Information with respect to impaired loans for the three and nine months ended September 30, 2019 and September 30, 2018, is as follows:

IMPAIRED LOANS
(DOLLARS IN THOUSANDS)

	Three months ended September 30,		Nine months ended September 30,	
	2019 $	2018 $	2019 $	2018 $
Average recorded balance of impaired loans	**3,721**	1,388	**3,278**	2,153
Interest income recognized on impaired loans	**11**	11	**32**	42

There were no loan modifications made during the third quarter of 2019, however, there was one loan modification that occurred during the first quarter of 2019. A modification of the payment terms to a loan customer is considered a troubled debt restructuring (TDR) if a concession was made to a borrower that is experiencing financial difficulty. A concession is generally defined as more favorable payment or credit terms granted to a borrower in an effort to improve the likelihood of the lender collecting principal in its entirety. Concessions usually are in the form of interest only for a period of time, or a lower interest rate offered in an effort to enable the borrower to continue to make normally scheduled payments.

In the first quarter 2019, a loan modification was made on a $717,000 agricultural mortgage which moved the timing of the annual principal payment and changed interest payments from monthly to annually. The farmer had suffered a fire loss in late 2018 impacting one year's harvest. The principal and interest payment are now due on November 15, 2019. No other loans were modified during 2019. There was one loan modification made in the first nine months of 2018. An agricultural mortgage loan was modified in the first quarter of 2018, where a concession on principal payment was made.

Included in the impaired loan portfolio are two loans that are being reported as TDRs that were restructured in prior periods. The balance of these two TDR loans was $1,157,000 as of September 30, 2019. One of these TDR loans with a balance of $439,000 is also on nonaccrual and is included under agricultural mortgages shown in the nonaccrual table above. For both of these TDR loans the borrowers have a history of being delinquent. Management will continue to report these loans as TDR loans until they have been paid off or charged off.

The following tables summarize information regarding impaired loans by loan portfolio class as of September 30, 2019, and December 31, 2018:

IMPAIRED LOAN ANALYSIS
(DOLLARS IN THOUSANDS)
September 30, 2019

	Recorded Investment $	Unpaid Principal Balance $	Related Allowance $	Average Recorded Investment $	Interest Income Recognized $
With no related allowance recorded:					
Commercial real estate					
Commercial mortgages	**732**	**767**	**—**	**903**	**—**
Agriculture mortgages	**1,945**	**1,947**	**—**	**1,685**	**32**
Construction	**—**	**—**	**—**	**—**	**—**
Total commercial real estate	**2,677**	**2,714**	**—**	**2,588**	**32**
Commercial and industrial					
Commercial and industrial	**—**	**—**	**—**	**—**	**—**
Tax-free loans	**—**	**—**	**—**	**—**	**—**
Agriculture loans	**—**	**—**	**—**	**—**	**—**
Total commercial and industrial	**—**	**—**	**—**	**—**	**—**
Total with no related allowance	**2,677**	**2,714**	**—**	**2,588**	**32**
With an allowance recorded:					
Commercial real estate					
Commercial mortgages	**92**	**100**	**49**	**93**	**—**
Agriculture mortgages	**718**	**718**	**—**	**519**	**—**
Construction	**—**	**—**	**—**	**—**	**—**
Total commercial real estate	**810**	**818**	**49**	**612**	**—**
Commercial and industrial					
Commercial and industrial	**547**	**549**	**547**	**78**	**—**
Tax-free loans	**—**	**—**	**—**	**—**	**—**
Agriculture loans	**—**	**—**	**—**	**—**	**—**
Total commercial and industrial	**547**	**549**	**547**	**78**	**—**
Total with a related allowance	**1,357**	**1,367**	**596**	**690**	**—**
Total by loan class:					
Commercial real estate					
Commercial mortgages	**824**	**867**	**49**	**996**	**—**
Agriculture mortgages	**2,663**	**2,665**	**—**	**2,204**	**32**
Construction	**—**	**—**	**—**	**—**	**—**
Total commercial real estate	**3,487**	**3,532**	**49**	**3,200**	**32**
Commercial and industrial					
Commercial and industrial	**547**	**549**	**547**	**78**	**—**
Tax-free loans	**—**	**—**	**—**	**—**	**—**
Agriculture loans	**—**	**—**	**—**	**—**	**—**
Total commercial and industrial	**547**	**549**	**547**	**78**	**—**
Total	**4,034**	**4,081**	**596**	**3,278**	**32**

IMPAIRED LOAN ANALYSIS
(DOLLARS IN THOUSANDS)
December 31, 2018

	Recorded Investment $	Unpaid Principal Balance $	Related Allowance $	Average Recorded Investment $	Interest Income Recognized $
With no related allowance recorded:					
Commercial real estate					
Commercial mortgages	370	901	—	396	—
Agriculture mortgages	1,692	1,692	—	1,063	45
Construction	—	—	—	—	—
Total commercial real estate	2,062	2,593	—	1,459	45
Commercial and industrial					
Commercial and industrial	—	—	—	—	—
Tax-free loans	—	—	—	—	—
Agriculture loans	—	—	—	—	—
Total commercial and industrial	—	—	—	—	—
Total with no related allowance	2,062	2,593	—	1,459	45
With an allowance recorded:					
Commercial real estate					
Commercial mortgages	647	694	132	484	—
Agriculture mortgages	—	—	—	—	—
Construction	—	—	—	—	—
Total commercial real estate	647	694	132	484	—
Commercial and industrial					
Commercial and industrial	—	—	—	—	—
Tax-free loans	—	—	—	—	—
Agriculture loans	—	—	—	124	6
Total commercial and industrial	—	—	—	124	6
Total with a related allowance	647	694	132	608	6
Total by loan class:					
Commercial real estate					
Commercial mortgages	1,017	1,595	132	880	—
Agriculture mortgages	1,692	1,692	—	1,063	45
Construction	—	—	—	—	—
Total commercial real estate	2,709	3,287	132	1,943	45
Commercial and industrial					
Commercial and industrial	—	—	—	—	—
Tax-free loans	—	—	—	—	—
Agriculture loans	—	—	—	124	6
Total commercial and industrial	—	—	—	124	6
Total	2,709	3,287	132	2,067	51

The following table details activity in the allowance for loan losses by portfolio segment for the nine months ended September 30, 2019:

ALLOWANCE FOR CREDIT LOSSES
(DOLLARS IN THOUSANDS)

	Commercial Real Estate $	Consumer Real Estate $	Commercial and Industrial $	Consumer $	Unallocated $	Total $
Allowance for credit losses:						
Beginning balance - December 31, 2018	**4,296**	**2,408**	**1,428**	**102**	**432**	**8,666**
Charge-offs	**—**	**—**	**—**	**(17)**	**—**	**(17)**
Recoveries	**44**	**—**	**13**	**—**	**—**	**57**
Provision	**148**	**(140)**	**128**	**16**	**28**	**180**
Balance - March 31, 2019	**4,488**	**2,268**	**1,569**	**101**	**460**	**8,886**
Charge-offs	**—**	**—**	**—**	**(6)**	**—**	**(6)**
Recoveries	**43**	**—**	**1**	**3**	**—**	**47**
Provision	**(114)**	**122**	**(204)**	**(22)**	**248**	**30**
Ending Balance - June 30, 2019	**4,417**	**2,390**	**1,366**	**76**	**708**	**8,957**
Charge-offs	**(122)**	**—**	**(63)**	**(3)**	**—**	**(188)**
Recoveries	**41**	**1**	**33**	**—**	**—**	**75**
Provision	**229**	**156**	**740**	**(19)**	**(476)**	**630**
Balance - September 30, 2019	**4,565**	**2,547**	**2,076**	**54**	**232**	**9,474**

During the three months ended September 30, 2019, management charged off $188,000 in loans while recovering $75,000 and added $630,000 to the provision. The unallocated portion of the allowance decreased from 5.3% of total reserves as of December 31, 2018, to 2.5% as of September 30, 2019, after being higher at the end of the first and second quarters. Management monitors the unallocated portion of the allowance with a desire to maintain it at approximately 5% or less, with a requirement of it not exceeding 10%.

During the three months ended September 30, 2019, net provision expense was recorded for all sectors except consumer, which had a net credit provision. In the third quarter of 2019, management recorded charge-offs in commercial real estate and the C&I sector, unlike in the first two quarters of 2019. This also pushed up the historic loss rate and caused higher allocations in the third quarter for those sectors. The total amount of substandard and special mention loans at the end of the second and third quarters of 2019 were similar for commercial mortgages, but agricultural mortgages increased for both special mention and substandard loans, requiring more provision. The Corporation’s commercial and industrial allocation for credit losses was increased by $740,000 in the third quarter of 2019, primarily due to the classification of one $547,000 loan to doubtful status, which caused a specific provision for the same amount. This C&I loan customer is current as to payment of interest on a commercial line of credit but the line has not revolved for several years. The Corporation does have a general UCC filing against all business assets but the majority of their inventory assets are already covered by a purchase money security interest of the manufacturer. Management will continue to classify the loan as doubtful until it can be determined that sufficient collateral exists to cover the loan, or sustainable principal payments can be made on the line.

Increases to the provision allocations for the three main loan sectors were consistent with the increases in special mention and substandard loans from June 30, 2019 to September 30, 2019, as well as an increase in nonaccrual loans. Provision allocations also increased as the size of the loan portfolio grew.

The Corporation’s commercial real estate loan segment experienced an increase in delinquencies during the first nine months of 2019 with most of this increase occurring in the third quarter of 2019. This was primarily due to two commercial borrowers being placed on nonaccrual status with $498,000 of loans. The increase in nonaccrual loans, along with the $547,000 doubtful loan mentioned above, were responsible for the larger $740,000 provision in the third quarter of 2019. The other loan segments experienced relatively small changes in delinquencies. Placing loans on nonaccrual and doubtful status, along with the level of charge-offs, have a larger impact to the provision allocations than the absolute delinquency levels. The commercial real estate loans experienced an increase in balances and higher levels of charge-offs, which was responsible for the additional $229,000 of third quarter provision. Commercial real estate delinquencies, including agricultural mortgage delinquencies increased during the third quarter and have increased since December 31, 2018. The agricultural mortgage delinquencies accounted for the vast majority of commercial real estate delinquencies. The agricultural mortgage delinquencies have increased due to higher past due and nonaccrual loans on several dairy farmers. While milk prices have improved, the local dairy industry continues to slowly consolidate based on longer-term trends impacting the industry. The consumer real estate segment continued to grow rapidly in the third quarter of 2019, while the absolute level of delinquencies remaining relatively stable. This caused $156,000 of additional provision for this segment.

As of September 30, 2019, the Corporation's total delinquencies were 0.56%, up from 0.44% as of June 30, 2019, and 0.46% as of December 31, 2018. However, total delinquencies were as high as 0.70% during the first quarter of 2019 and finished the first quarter at 0.59%. The Corporation's total delinquencies still compares favorably to the national uniform bank performance group which was at 0.64% as of June 30, 2019.

Outside of the above measurements and indicators, management continues to utilize nine qualitative factors to continually refine the potential credit risks across the Corporation's various loan types. In addition, the loan portfolio is sectored out into nine different categories to evaluate these qualitative factors. A total score of the qualitative factors for each loan sector is calculated to utilize in the allowance for loan loss calculation. The agricultural dairy sector carries the highest level of qualitative factors due to the continued stress that the dairy farmers are under. However, the environment for dairy has improved slightly as milk prices have improved. As a result, the total qualitative factors for dairy agriculture declined slightly from December 31, 2018 and June 30, 2019. The non-dairy agriculture sector carries the second highest level of qualitative factors, pointing to other challenges in agricultural lending. Outside of the agricultural sectors, the business loan and business mortgages carry the next highest levels of qualitative factors. The qualitative factors for business loans did increase for the third quarter due to the trend of delinquency, nonaccruals, and charge-offs and increases in industry concentrations. While the qualitative factors surrounding delinquencies, nonaccrual loans, and criticized and classified loans were adjusted higher for the segments that experienced increases, there were other qualitative factors that were adjusted lower due to other reasons such as slower growth rates or if industry conditions improved. As a result, all of the loan segments outside of C&I lending either had no change or experienced minor changes since both December 31, 2018 and June 30, 2019.

The following table details activity in the allowance for loan losses by portfolio segment for the nine months ended September 30, 2018:

ALLOWANCE FOR CREDIT LOSSES
(DOLLARS IN THOUSANDS)

	Commercial Real Estate $	Consumer Real Estate $	Commercial and Industrial $	Consumer $	Unallocated $	Total $
Allowance for credit losses:						
Beginning balance - December 31, 2017	3,863	2,052	1,829	98	398	8,240
Charge-offs	(224)	—	(110)	(18)	—	(352)
Recoveries	—	—	4	1	—	5
Provision	408	137	(422)	(9)	76	190
Balance - March 31, 2018	4,047	2,189	1,301	72	474	8,083
Charge-offs	—	—	—	(8)	—	(8)
Recoveries	—	—	2	4	—	6
Provision	(43)	(7)	(21)	63	98	90
Balance - June 30, 2018	4,004	2,182	1,282	131	572	8,171
Charge-offs	—	(20)	—	—	—	(20)
Recoveries	30	—	55	2	—	87
Provision	90	192	90	(16)	(166)	190
Ending Balance - September 30, 2018	4,124	2,354	1,427	117	406	8,428

During the nine months ended September 30, 2018, management charged off $380,000 in loans while recovering $98,000 and added $470,000 to the provision. The level of charge-offs along with the growth in the loan portfolio was primarily responsible for the $470,000 of additional provision.

During the nine months ended September 30, 2018, provision expenses were recorded for the commercial real estate, consumer real estate, and consumer segments with a credit provision recorded for the commercial and industrial segment. The increase in the allowance for commercial real estate loans was primarily a result of higher levels of charge-offs in the first nine months of 2018 as well as the addition of $116,000 of specific reserves allocated to this loan segment. The increase in the amount of the allowance for loan losses allocated to the consumer real estate and consumer segment was primarily a result of growth in these portfolios during the nine months ended September 30, 2018. The decrease in commercial and industrial loans from December 31, 2017 to September 30, 2018, was caused by a qualitative factor change across the portfolio and also by the declining level of substandard commercial and industrial loans. The qualitative factors were adjusted across the loan portfolio to better reflect the forward risk in each portfolio. Commercial and consumer real estate carried heavier risk factors, while commercial and industrial was adjusted down. While commercial and industrial did have charge-offs in the first quarter of 2018 they were relative to the size of the allowance and sufficiently covered with prior provisions. There was no commercial and industrial charge-offs in the second or third quarters of 2018, and the amount of commercial and industrial loans rated substandard declined from $2.5 million on December 31, 2017, to $1.5 million on September 30, 2018. While the balances of commercial and industrial loans increased moderately from December 31, 2017 to September 30, 2018, the required allowance and related provision for these loans is influenced more heavily by the amount of classified loans.

The following tables present the balance in the allowance for credit losses and the recorded investment in loans receivable by portfolio segment based on impairment method as of September 30, 2019 and December 31, 2018:

ALLOWANCE FOR CREDIT LOSSES AND RECORDED INVESTMENT IN LOANS RECEIVABLE
(DOLLARS IN THOUSANDS)

As of September 30, 2019:	Commercial Real Estate $	Consumer Real Estate $	Commercial and Industrial $	Consumer $	Unallocated $	Total $
Allowance for credit losses:						
Ending balance: individually evaluated for impairment	**49**	**—**	**547**	**—**	**—**	**596**
Ending balance: collectively evaluated for impairment	**4,516**	**2,547**	**1,529**	**54**	**232**	**8,878**
Loans receivable:						
Ending balance	**305,102**	**331,377**	**94,183**	**5,651**		**736,313**
Ending balance: individually evaluated for impairment	**3,487**	**—**	**547**	**—**		**4,034**
Ending balance: collectively evaluated for impairment	**301,615**	**331,377**	**93,636**	**5,651**		**732,279**

As of December 31, 2018:	Commercial Real Estate $	Consumer Real Estate $	Commercial and Industrial $	Consumer $	Unallocated $	Total $
Allowance for credit losses:						
Ending balance: individually evaluated for impairment	132	—	—	—	—	132
Ending balance: collectively evaluated for impairment	4,164	2,408	1,428	102	432	8,534
Loans receivable:						
Ending balance	285,437	293,721	104,122	9,197		692,477
Ending balance: individually evaluated for impairment	2,709	—	—	—		2,709
Ending balance: collectively evaluated for impairment	282,728	293,721	104,122	9,197		689,768

5. Fair Value Presentation

U.S. generally accepted accounting principles establish a hierarchal disclosure framework associated with the level of observable pricing utilized in measuring assets and liabilities at fair value. The three broad levels defined by the hierarchy are as follows:

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

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

Level III: Assets and liabilities that have little to no observable pricing as of the reported date. These items do not have two-way markets and are measured using management's best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation.

The following tables provide the fair market value for assets required to be measured and reported at fair value on a recurring basis on the Consolidated Balance Sheets as of September 30, 2019, and December 31, 2018, by level within the fair value hierarchy. As required by U.S. generally accepted accounting principles, financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

ASSETS MEASURED ON A RECURRING BASIS
(DOLLARS IN THOUSANDS)

	September 30, 2019			
	Level I $	Level II $	Level III $	Total $
U.S. government agencies	—	**35,316**	—	**35,316**
U.S. agency mortgage-backed securities	—	**45,911**	—	**45,911**
U.S. agency collateralized mortgage obligations	—	**54,660**	—	**54,660**
Asset-backed securities	—	**19,568**	—	**19,568**
Corporate bonds	—	**54,672**	—	**54,672**
Obligations of states & political subdivisions	—	**88,856**	—	**88,856**
Equity securities	**6,108**	—	—	**6,108**
Total securities	**6,108**	**298,983**	—	**305,091**

On September 30, 2019, the Corporation held no securities valued using level III inputs. All of the Corporation's debt instruments were valued using level II inputs, where quoted prices are available and observable, but not necessarily quotes on identical securities traded in active markets on a daily basis. The Corporation's CRA fund investments and bank stocks are fair valued utilizing level I inputs because the funds have their own quoted prices in an active market. As of September 30, 2019, the CRA fund investments had a $5,529,000 book and fair market value and the bank stock portfolio had a book value of $601,000, and fair market value of $579,000.

Financial instruments are considered level III when their values are determined using pricing models, discounted cash flow methodologies, or similar techniques, and at least one significant model assumption or input is unobservable. In addition to these unobservable inputs, the valuation models for level III financial instruments typically also rely on a number of inputs that are readily observable either directly or indirectly. Level III financial instruments also include those for which the determination of fair value requires significant management judgment or estimation.

ASSETS MEASURED ON A RECURRING BASIS
(DOLLARS IN THOUSANDS)

	December 31, 2018			
	Level I $	Level II $	Level III $	Total $
U.S. government agencies	—	30,120	—	30,120
U.S. agency mortgage-backed securities	—	44,639	—	44,639
U.S. agency collateralized mortgage obligations	—	54,090	—	54,090
Asset-backed securities	—	11,399	—	11,399
Corporate bonds	—	59,192	—	59,192
Obligations of states & political subdivisions	—	94,625	—	94,625
Equity securities	5,934	—	—	5,934
Total securities	5,934	294,065	—	299,999

On December 31, 2018, the Corporation held no securities valued using level III inputs. All of the Corporation’s debt instruments were valued using level II inputs, where quoted prices are available and observable but not necessarily quotes on identical securities traded in active markets on a daily basis. The Corporation’s CRA fund investments and bank stocks are fair valued utilizing level I inputs because the funds have their own quoted prices in an active market. As of December 31, 2018, the CRA fund investments had a $5,410,000 book and market value and the bank stocks had a book value of $591,000 and a market value of $524,000.

The following tables provide the fair value for each class of assets required to be measured and reported at fair value on a nonrecurring basis on the Consolidated Balance Sheets as of September 30, 2019 and December 31, 2018, by level within the fair value hierarchy:

ASSETS MEASURED ON A NONRECURRING BASIS
(DOLLARS IN THOUSANDS)

	September 30, 2019			
	Level I $	Level II $	Level III $	Total $
Assets:				
Impaired Loans	**$ —**	**$ —**	**$ 3,438**	**$ 3,438**
Total	**$ —**	**$ —**	**$ 3,438**	**$ 3,438**

	December 31, 2018			
	Level I $	Level II $	Level III $	Total $
Assets:				
Impaired Loans	$ —	$ —	$ 2,577	$ 2,577
Total	$ —	$ —	$ 2,577	$ 2,577

The Corporation had a total of $4,034,000 of impaired loans as of September 30, 2019, with $596,000 of specific allocation against these loans and $2,709,000 of impaired loans as of December 31, 2018, with $132,000 of specific allocation against these loans. The value of impaired loans is generally determined through independent appraisals of the underlying collateral.

The following table presents additional quantitative information about assets measured at fair value on a nonrecurring basis for which the Corporation has utilized level III inputs to determine fair value:

QUANTITATIVE INFORMATION ABOUT LEVEL III FAIR VALUE MEASUREMENTS
(DOLLARS IN THOUSANDS)

	September 30, 2019			
	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range (Weighted Avg)
Impaired loans	**3,438**	**Appraisal of collateral (1)**	**Appraisal adjustments (2)**	**-20% (-20%)**
			Liquidation expenses (2)	**-10% (-10%)**

	December 31, 2018			
	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range (Weighted Avg)
Impaired loans	2,577	Appraisal of collateral (1)	Appraisal adjustments (2)	-20% (-20%)
			Liquidation expenses (2)	-10% (-10%)

(1) Fair value is generally determined through independent appraisals of the underlying collateral, which generally include various level III inputs which are not identifiable.
(2) Appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated liquidation expenses. The range and weighted average of liquidation expenses and other appraisal adjustments are presented as a percent of the appraisal.

The following table provides the carrying amount for each class of assets and liabilities and the fair value for certain financial instruments that are not required to be measured or reported at fair value on the Consolidated Balance Sheets as of September 30, 2019 and December 31, 2018:

FINANCIAL INSTRUMENTS NOT REQUIRED TO BE MEASURED OR REPORTED AT FAIR VALUE
(DOLLARS IN THOUSANDS)

	September 30, 2019				
	Carrying Amount $	Fair Value $	Quoted Prices in Active Markets for Identical Assets (Level 1) $	Significant Other Observable Inputs (Level II) $	Significant Unobservable Inputs (Level III) $
Financial Assets:					
Cash and cash equivalents	**41,190**	**41,190**	**41,190**	—	—
Regulatory stock	**7,200**	**7,200**	**7,200**	—	—
Loans held for sale	**1,578**	**1,578**	**1,578**	—	—
Loans, net of allowance	**728,630**	**732,715**	—	—	**732,715**
Mortgage servicing assets	**812**	**823**	—	—	**823**
Accrued interest receivable	**3,830**	**3,830**	**3,830**	—	—
Bank owned life insurance	**28,610**	**28,610**	**28,610**	—	—
Financial Liabilities:					
Demand deposits	**347,929**	**347,929**	**347,929**	—	—
Interest-bearing demand deposits	**19,275**	**19,275**	**19,275**	—	—
NOW accounts	**90,444**	**90,444**	**90,444**	—	—
Money market deposit accounts	**148,863**	**148,863**	**148,863**	—	—
Savings accounts	**203,706**	**203,706**	**203,706**	—	—
Time deposits	**136,774**	**138,457**	—	—	**138,457**
Total deposits	**946,991**	**948,674**	**810,217**	—	**138,457**
Long-term debt	**79,989**	**78,823**	—	—	**78,823**
Accrued interest payable	**517**	**517**	**517**	—	—

FINANCIAL INSTRUMENTS NOT REQUIRED TO BE MEASURED OR REPORTED AT FAIR VALUE
(DOLLARS IN THOUSANDS)

	December 31, 2018				
	Carrying Amount $	Fair Value $	Quoted Prices in Active Markets for Identical Assets (Level 1) $	Significant Other Observable Inputs (Level II) $	Significant Unobservable Inputs (Level III) $
Financial Assets:					
Cash and cash equivalents	41,365	41,365	41,365	—	—
Regulatory stock	6,348	6,348	6,348	—	—
Loans held for sale	1,429	1,429	1,429	—	—
Loans, net of allowance	685,407	687,844	—	—	687,844
Mortgage servicing assets	905	997	—	—	997
Accrued interest receivable	3,754	3,754	3,754	—	—
Bank owned life insurance	28,085	28,085	28,085	—	—
Financial Liabilities:					
Demand deposits	369,081	369,081	369,081	—	—
Interest-bearing demand deposits	20,104	20,104	20,104	—	—
NOW accounts	89,072	89,072	89,072	—	—
Money market deposit accounts	108,594	108,594	108,594	—	—
Savings accounts	199,665	199,665	199,665	—	—
Time deposits	133,218	132,351	—	—	132,351
Total deposits	919,734	918,867	786,516	—	132,351
Short-term borrowings	7,870	7,870	7,870	—	—
Long-term debt	65,386	65,286	—	—	65,286
Accrued interest payable	397	397	397	—	—

7. Commitments and Contingent Liabilities

In order to meet the financing needs of its customers in the normal course of business, the Corporation makes various commitments that are not reflected in the accompanying consolidated financial statements. These commitments include firm commitments to extend credit, unused lines of credit, and open letters of credit. As of September 30, 2019, firm loan commitments were $65.8 million, unused lines of credit were $258.6 million, and open letters of credit were $9.6 million. The total of these commitments was $334.0 million, which represents the Corporation's exposure to credit loss in the event of nonperformance by its customers with respect to these financial instruments. The actual credit losses that may arise from these commitments are expected to compare favorably with the Corporation's loan loss experience on its loan portfolio taken as a whole. The Corporation uses the same credit policies in making commitments and conditional obligations as it does for balance sheet financial instruments.

8. Accumulated Other Comprehensive Income (Loss)

The activity in accumulated other comprehensive income (loss) for the nine months ended September 30, 2019 and 2018 is as follows:

ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS) (1) (2)
(DOLLARS IN THOUSANDS)

	Unrealized Gains (Losses) on Securities Available-for-Sale $
Balance at December 31, 2018	**(5,678)**
Other comprehensive income before reclassifications	**2,553**
Amount reclassified from accumulated other comprehensive income	**(64)**
Period change	**2,489**
Balance at March 31, 2019	**(3,189)**
Other comprehensive income before reclassifications	**3,571**
Amount reclassified from accumulated other comprehensive income	**(84)**
Period change	**3,487**
Balance at June 30, 2019	**298**
Other comprehensive income before reclassifications	**1,420**
Amount reclassified from accumulated other comprehensive income	**(33)**
Period change	**1,387**
Balance at September 30, 2019	**1,685**
Balance at December 31, 2017	(3,195)
Other comprehensive loss before reclassifications	(2,685)
Amount reclassified from accumulated other comprehensive loss	(27)
Reclassification of certain income tax effects from accumulated other comprehensive loss	(634)
Period change	(3,346)
Balance at March 31, 2018	(6,541)
Other comprehensive loss before reclassifications	(286)
Amount reclassified from accumulated other comprehensive loss	49
Period change	(237)
Balance at June 30, 2018	(6,778)
Other comprehensive loss before reclassifications	(1,419)
Amount reclassified from accumulated other comprehensive loss	(3)
Period change	(1,422)
Balance at September 30, 2018	(8,200)

(1) All amounts are net of tax. Related income tax expense or benefit is calculated using a Federal income tax rate of 21%.
(2) Amounts in parentheses indicate debits.

DETAILS ABOUT ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS) COMPONENTS (1)
(DOLLARS IN THOUSANDS)

	Amount Reclassified from Accumulated Other Comprehensive Income (Loss) For the Three Months Ended September 30,		
	2019	2018	Affected Line Item in the
	$	$	Consolidated Statements of Income
Securities available-for-sale:			
Net securities gains,	**42**	4	Gains (losses) on the sale of
reclassified into earnings			debt securities, net
Related income tax expense	**(9)**	(1)	Provision for federal income taxes
Net effect on accumulated other comprehensive			
income for the period	**33**	3	

(1) Amounts in parentheses indicate debits.

	Amount Reclassified from Accumulated Other Comprehensive Income (Loss) For the Nine Months Ended September 30,		
	2019	2018	Affected Line Item in the
	$	$	Consolidated Statements of Income
Securities available-for-sale:			
Net securities gains (losses),	**229**	(24)	Gains (losses) on the sale of
reclassified into earnings			debt securities, net
Related income tax expense	**(48)**	5	Provision for federal income taxes
Net effect on accumulated other comprehensive			
income for the period	**181**	(19)	

(1) Amounts in parentheses indicate debits.

9. Leases

A lease is defined as a contract, or part of a contract, that conveys the right to control the use of identified property, plant or equipment for a period of time in exchange for consideration. On January 1, 2019, the Corporation adopted ASU No. 2016-02 “Leases” (Topic 842) and all subsequent ASUs that modified Topic 842. For the Corporation, Topic 842 primarily affected the accounting treatment for operating lease agreements in which the Corporation is the lessee.

All of these leases in which the Corporation is the lessee are comprised of real estate property for branches and office space with terms extending through 2026. All of the Corporation’s leases are classified as operating leases, and therefore, were previously not recognized on the Corporation’s Consolidated Balance Sheets. With the adoption of Topic 842, operating lease agreements are required to be recognized on the Consolidated Balance Sheets as a right-of use (“ROU”) asset and a corresponding lease liability.

The following table represents the Consolidated Balance Sheet classification of the Corporation’s ROU assets and lease liabilities.

Lease Consolidated Balance Sheets Classification (Dollars in Thousands)	Classification		September 30, 2019
Lease Right-of-Use Assets			
Operating lease right-of use assets	Other Assets	$	**952**
Lease Liabilities			
Operating lease liabilties	Other Liabilities	$	**959**

The calculated amount of the ROU assets and lease liabilities in the table above are impacted by the length of the lease term and the discount rate used to determine the present value of the minimum lease payments. The Corporation's lease agreements often include one or more options to renew at the Corporation's discretion. If at lease inception, the Corporation considers the exercising of a renewal option to be reasonably certain, the Corporation will include the extended term in the calculation of the ROU asset and lease liability. Regarding the discount rate, Topic 842 requires the use of the rate implicit in the lease whenever this rate is readily determinable. As the rate is rarely determinable, the Corporation utilizes its incremental borrowing rate at lease inception, on a collateralized basis, over a similar term. For operating leases existing prior to January 1, 2019, the rate for the remaining lease term as of January 1, 2019 was used.

	September 30, 2019
Weighted-average remaining lease term	
Operating leases	**5.5 years**
Weighted-average discount rate	
Operating leases	**3.09%**

The following table represents lease costs and other lease information. As the Corporation elected, for all classes of underlying assets, not to separate lease and non-lease components and instead to account for them as a single lease component, the variable lease cost primarily represents variable payments such as common area maintenance and utilities.

Future minimum payments for operating leases with initial or remaining terms of one year or more as of September 30, 2019 were as follows:

Lease Payment Schedule (Dollars in Thousands)		Operating Leases
Twelve Months Ended:		
September 30, 2020	$	**202**
September 30, 2021		**203**
September 30, 2022		**183**
September 30, 2023		**151**
September 30, 2024		**155**
Thereafter		**151**
Total Future Minimum Lease Payments		**1,045**
Amounts Representing Interests		**(86)**
Present Value of Net Future Minimum Lease Payments	$	**959**

10. Change in Capital Structure

On April 17, 2019 ENB Financial Corp announced the Board of Directors declared a two-for-one stock split of the Corporation's issued and outstanding common stock pursuant to which one (1) additional share of common stock was issued for each share of common stock held by shareholders of record as of the close of business on May 31, 2019. The additional shares were issued on June 28, 2019. The stock split was effected pursuant to articles of amendment to the articles of incorporation to reduce the par value of the common stock from $0.20 to $0.10 and increase the authorized shares of common stock proportionately from 12,000,000 to 24,000,000. Per share data reflected on the Corporation's consolidated statements of income are restated as if the stock split had occurred at the beginning of the earliest period presented.

11. Recently Issued Accounting Standards

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments - Credit Losses: Measurement of Credit Losses on Financial Instruments*, which changes the impairment model for most financial assets. This Update is intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The underlying premise of the Update is that financial assets measured at amortized cost should be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. The allowance for credit losses should reflect management's current estimate of credit losses that are expected to occur over the remaining life of a financial asset. The income statement will be effected for the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. ASU 2016-13 is effective for annual and interim periods beginning after December 15, 2019, and early adoption is permitted for annual and interim periods beginning after December 15, 2018. With certain exceptions, transition to the new requirements will be through a cumulative effect adjustment to opening retained earnings as of the beginning of the first reporting period in which the guidance is adopted. On October 16, 2019, the FASB voted to defer the effective date for ASC 326, *Financial Instruments – Credit Losses*, for smaller reporting companies to fiscal years beginning after December 15, 2022, and interim periods within those fiscal years. The final ASU is expected to be issued in mid-November. We expect to recognize a one-time cumulative effect adjustment to the allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective, but cannot yet determine the magnitude of any such one-time adjustment or the overall impact of the new guidance on the consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework – Changes the Disclosure Requirements for Fair Value Measurements*. The Update removes the requirement to disclose the amount of and reasons for transfers between Level I and Level II of the fair value hierarchy; the policy for timing of transfers between levels; and the valuation processes for Level III fair value measurements. The Update requires disclosure of changes in unrealized gains and losses for the period included in other comprehensive income (loss) for recurring Level III fair value measurements held at the end of the reporting period and the range and weighted average of significant unobservable inputs used to develop Level III fair value measurements. This Update is effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. This Update is not expected to have a significant impact on the Corporation's financial statements.

In April 2019, the FASB issued ASU 2019-04, *Codification Improvements to Topic 326, Financial Instruments – Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments,* which affects a variety of topics in the Codification and applies to all reporting entities within the scope of the affected accounting guidance. *Topic 326, Financial Instruments – Credit Losses* amendments are effective for SEC registrants for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. For all other public business entities, the effective date is for fiscal years beginning after December 15, 2020, and for all other entities, the effective date is for fiscal years beginning after December 15, 2021. On October 16, 2019, the FASB voted to defer the effective date for ASC 326, *Financial Instruments – Credit Losses*, for smaller reporting companies to fiscal years beginning after December 15, 2022, and interim periods within those fiscal years. The final ASU is expected to be issued in mid-November. *Topic 815, Derivatives and Hedging* amendments are effective for public business entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2019, and interim periods beginning after December 15, 2020. For entities that have adopted the amendments in Update 2017-12, the effective date is as of the beginning of the first annual period beginning after the issuance of this Update. *Topic 825, Financial Instruments* amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years. This Update is not expected to have a significant impact on the Corporation's financial statements.

In May 2019, the FASB issued ASU 2019-05, *Financial Instruments – Credit Losses, Topic 326*, which allows entities to irrevocably elect the fair value option for certain financial assets previously measured at amortized cost upon adoption of the new credit losses standard. To be eligible for the transition election, the existing financial asset must otherwise be both within the scope of the new credit losses standard and eligible for the applying the fair value option in ASC 825-10.3. The election must be applied on an instrument-by-instrument basis and is not available for either available-for-sale or held-to-maturity debt securities. For entities that elect the fair value option, the difference between the carrying amount and the fair value of the financial asset would be recognized through a cumulative-effect adjustment to opening retained earnings as of the date an entity adopted ASU 2016-13. Changes in fair value of that financial asset would subsequently be reported in current earnings. For entities that have not yet adopted ASU 2016-13, the effective dates and transition requirements are the same as those in ASU 2016-13. For entities that have adopted ASU 2016-13, ASU 2019-05 is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted once ASU 2016-13 has been adopted On October 16, 2019, the FASB voted to defer the effective date for ASC 326, *Financial Instruments – Credit Losses*, for smaller reporting companies to fiscal years beginning after December 15, 2022, and interim periods within those fiscal years. The final ASU is expected to be issued in mid-November. This Update is not expected to have a significant impact on the Corporation's financial statements.

In July 2019, the FASB issued ASU 2019-07, *Codification Updates to SEC Sections, Amendments to SEC Paragraphs Pursuant to SEC Final Rule Releases No. 33-10532, Disclosure Update and Simplification, and Nos. 33-10231 and 33-10442, Investment Company Reporting Modernization, and Miscellaneous Updates.* This ASU amends various SEC paragraphs pursuant to the issuance of SEC Final Rule Releases No. 33-10532, *Disclosure Update and Simplification*, and Nos. 33-10231 and 33-10442, *Investment Company Reporting Modernization*. Other miscellaneous updates to agree to the electronic Code of Federal Regulations also have been incorporated.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis represents management's view of the financial condition and results of operations of the Corporation. This discussion and analysis should be read in conjunction with the consolidated financial statements and other financial schedules included in this quarterly report, and in conjunction with the 2018 Annual Report to Shareholders of the Corporation. The financial condition and results of operations presented are not indicative of future performance.

Forward-Looking Statements

The U.S. Private Securities Litigation Reform Act of 1995 provides safe harbor in regards to the inclusion of forward-looking statements in this document and documents incorporated by reference. Forward-looking statements pertain to possible or assumed future results that are made using current information. These forward-looking statements are generally identified when terms such as: "believe," "estimate," "anticipate," "expect," "project," "forecast," and other similar wordings are used. The readers of this report should take into consideration that these forward-looking statements represent management's expectations as to future forecasts of financial performance, or the likelihood that certain events will or will not occur. Due to the very nature of estimates or predications, these forward-looking statements should not be construed to be indicative of actual future results. Additionally, management may change estimates of future performance, or the likelihood of future events, as additional information is obtained. This document may also address targets, guidelines, or strategic goals that management is striving to reach but may not be indicative of actual results.

Readers should note that many factors affect this forward-looking information, some of which are discussed elsewhere in this document and in the documents that are incorporated by reference into this document. These factors include, but are not limited to, the following:

- National and local economic conditions
- Effects of slow economic conditions or prolonged economic weakness, specifically the effect on loan customers to repay loans
- Health of the housing market
- Real estate valuations and its impact on the loan portfolio
- Interest rate and monetary policies of the Federal Reserve Board
- Volatility of the securities markets including the valuation of securities
- Future actions or inactions of the United States government, including a failure to increase the government debt limit or a prolonged shutdown of the federal government
- Political changes and their impact on new laws and regulations
- Competitive forces
- Impact of mergers and acquisition activity in the local market and the effects thereof
- Potential impact from continually evolving cybersecurity and other technological risks and attacks, including additional costs, reputational damage, regulatory penalties, and financial losses
- Changes in customer behavior impacting deposit levels and loan demand
- Changes in accounting principles, policies, or guidelines as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board, and other accounting standards setters
- Ineffective business strategy due to current or future market and competitive conditions
- Management's ability to manage credit risk, liquidity risk, interest rate risk, and fair value risk
- Operation, legal, and reputation risk
- Results of the regulatory examination and supervision process
- The impact of new laws and regulations, including the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and the regulations issued thereunder
- Possible changes to the capital and liquidity requirements of the current Basel III standards and other regulatory pronouncements, regulations and rules
- Disruptions due to flooding, severe weather, or other natural disasters
- The risk that our analyses of these risks and forces could be incorrect and/or that the strategies developed to address them could be unsuccessful

Readers should be aware if any of the above factors change significantly, the statements regarding future performance could also change materially. The safe harbor provision provides that the Corporation is not required to publicly update or revise forward-looking statements to reflect events or circumstances that arise after the date of this report. Readers should review any changes in risk factors in documents filed by the Corporation periodically with the Securities and Exchange Commission, including Item 1A of Part II of this Quarterly Report on Form 10-Q, Annual Reports on Form 10-K, and Current Reports on Form 8-K.

Results of Operations

Overview

The Corporation recorded net income of $2,924,000 and $8,616,000 for the three and nine-month periods ended September 30, 2019, a 13.5% and 14.5% increase respectively, from the $2,577,000 and $7,524,000 earned during the same periods in 2018. The earnings per share, basic and diluted, were $0.51 and $1.51 for the three and nine months ended September 30, 2019, compared to $0.45 and $1.32 for the same periods in 2018, a 13.3% and 14.4% increase, respectively. The increase in the Corporation's 2019 earnings was caused primarily by growth in net interest income (NII), as well as limited increases in operating expenses, resulting in improved efficiency.

The Corporation's NII increased by $813,000, or 9.6%, and $3,149,000, or 13.0%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018. The increase in NII primarily resulted from an increase in interest and fees on loans of $1,344,000, or 18.8%, and $4,574,000, or 22.6%, for the three and nine-month periods ended September 30, 2019. The increase in NII was partially offset by an increase in interest expense. The Corporation's interest expense on deposits and borrowings increased by $429,000, or 49.2%, and $1,296,000, or 52.1%, for the three and nine-month periods ended September 30, 2019, compared to 2018.

The Corporation recorded a $440,000 additional provision expense in the third quarter of 2019 compared to the same quarter of 2018, with $630,000 of provision compared to $190,000 of provision for the third quarter of 2018. For the nine-month period ended September 30, 2019, the Corporation recorded a $370,000 additional provision expense, with $840,000 of provision expense compared to $470,000 in the same period of 2018. The gains from the sale of debt securities were $42,000 for the three months ended September 30, 2019, and $229,000 for the nine months ended September 30, 2019, compared to gains of $4,000 for the third quarter of 2018, and losses of $24,000 for the year-to-date period in 2018. Market interest rates were lower in 2019, making it more conducive to achieving gains from the sale of securities. The gain on the sale of mortgages increased by $91,000, or 17.7%, and $268,000, or 24.3%, for the three and nine-month periods ended September 30, 2019, compared to the prior year's periods. The volume of mortgages sold was higher during the first nine months of 2019 compared to the same period in the prior year. Total operating expenses increased marginally by $57,000, or 0.7%, and $505,000, or 2.1%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018.

The financial services industry uses two primary performance measurements to gauge performance: return on average assets (ROA) and return on average equity (ROE). ROA measures how efficiently a bank generates income based on the amount of assets or size of a company. ROE measures the efficiency of a company in generating income based on the amount of equity or capital utilized. The latter measurement typically receives more attention from shareholders. The ROA and ROE increased for the three and nine months ended September 30, 2019, compared to the same periods in the prior year due primarily to higher earnings.

Key Ratios	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Return on Average Assets	**1.02%**	0.97%	**1.03%**	0.97%
Return on Average Equity	**10.22%**	10.33%	**10.64%**	10.28%

The results of the Corporation's operations are best explained by addressing, in further detail, the five major sections of the income statement, which are as follows:

- Net interest income
- Provision for loan losses
- Other income
- Operating expenses
- Provision for income taxes

The following discussion analyzes each of these five components.

Net Interest Income

NII represents the largest portion of the Corporation's operating income. In the first nine months of 2019, NII generated 76.9% of the Corporation's gross revenue stream, which consists of net interest income and non-interest income, compared to 73.4% in the first nine months of 2018. The overall performance of the Corporation is highly dependent on the changes in net interest income since it comprises such a significant portion of operating income.

The following table shows a summary analysis of net interest income on a fully taxable equivalent (FTE) basis. For analytical purposes and throughout this discussion, yields, rates, and measurements such as NII, net interest spread, and net yield on interest earning assets are presented on an FTE basis. The FTE net interest income shown in both tables below will exceed the NII reported on the consolidated statements of income, which is not shown on an FTE basis. The amount of FTE adjustment totaled $182,000 and $575,000 for the three and nine months ended September 30, 2019, compared to $217,000 and $670,000 for the same periods in 2018.

NET INTEREST INCOME
(DOLLARS IN THOUSANDS)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
	$	$	$	$
Total interest income	**10,590**	9,348	**31,214**	26,769
Total interest expense	**1,301**	872	**3,784**	2,488
Net interest income	**9,289**	8,476	**27,430**	24,281
Tax equivalent adjustment	**182**	217	**575**	670
Net interest income (fully taxable equivalent)	**9,471**	8,693	**28,005**	24,951

NII is the difference between interest income earned on assets and interest expense incurred on liabilities. Accordingly, two factors affect net interest income:

- The rates earned on interest earning assets and paid on interest bearing liabilities
- The average balance of interest earning assets and interest bearing liabilities

The Federal funds rate, the Prime rate, the shape of the U.S. Treasury curve, and other wholesale funding curves, all affect NII. The Federal Reserve controls the Federal funds rate, which is one of a number of tools available to the Federal Reserve to conduct monetary policy. The Federal funds rate, and guidance on when the rate might be changed, is often the focal point of discussion regarding the direction of interest rates. Until December 16, 2015, the Federal funds rate had not changed since December 16, 2008, a period of seven years. Since December 16, 2015, a period over three and a half years, the Federal funds rate has been increased nine (9) times from 0.25% to 2.50%. Four of those rate increases occurred in 2018, with the final increase on December 15, 2018. In the first half of 2019, no Federal Reserve rate actions took place, however on July 31, 2019 and September 18, 2019, the Federal Reserve lowered the Federal Funds rate by 0.25% with a rate of 2.00% as of September 30, 2019. Subsequent to September 30, 2019, but prior to the filing of this report, the Fed lowered the Federal Funds target rate by another 0.25% on October 30, 2019, so the rate stands at 1.75% currently. This was done out of concern of a slowing economy.

The expectations for the remainder of the year are that there will be no further rate drops. It should be noted that it was ten years ago that the Federal Reserve last decreased rates in July of 2009 after concern of economic slowdown after the great recession. Management anticipates a reduction in interest income in the fourth quarter of 2019 as a result of the recent Federal Reserve rate decreases. All of the Corporation's Prime-based floating rate loans will reset lower.

The shape of the U.S. Treasury curve also directly impacts the Corporation's net interest income. During the first nine months of 2019, the U.S. Treasury curve has been very flat. This is generally not beneficial to banks as funding sources are typically shorter terms than the assets invested in. A sharper yield curve is beneficial to financial institutions as a larger spread can be made on the asset versus the liability utilized. Throughout most of the first nine months of 2019, the spread between the 2-year and 10-year U.S. Treasury averaged around 16 basis points. This is a very low spread in terms of historical performance. Additionally, the yield curve has been very flat between the 2-year and 5-year terms. There has also been an inversion on the U.S. Treasury curve as the 3-month U.S. Treasury yields have been higher than the 2-year U.S. Treasury yields.

The combination of lower overnight rates, an inverted yield curve on the short end, and a generally flat yield curve out to longer rates, makes it more difficult for the Corporation to generate higher net interest income. The Corporation's net interest margin declined slightly in the third quarter of 2019 and it is likely it will decline a little more in the fourth quarter and any increase in net interest income will need to come from growth of interest earning assets.

The Prime rate is generally used by commercial banks to extend variable rate loans to business and commercial customers. For many years, the Prime rate has been set at 300 basis points, or 3.00% higher, than the Federal funds rate and typically moves when the Federal funds rate changes. As such, the Prime rate was 5.00% as of September 30, 2019. As of October 31, 2019, the Prime rate changed to 4.75%. The Corporation's Prime-based loans, including home equity lines of credit and some variable rate commercial loans, reprice a day after the Federal Reserve rate movement.

As a result of the prior Federal Reserve rate increases and the significant growth of the loan portfolio, the Corporation's NII on a tax equivalent basis has been increasing significantly. The Corporation's margin decreased in the beginning of 2018 primarily as a result of lower tax-equivalent yields on the Corporation's municipal securities, which were negatively impacted by the lower corporate tax rate. Subsequent to the tax rate change, the Corporation's net interest margin began increasing again. The net interest margin for the first quarter of 2019 was 3.59% and declined slightly to 3.56% for the second quarter of 2019, and declined again to 3.55% for the third quarter of 2019 due to lower asset yields resulting from the lower Prime rate. The Corporation's NII on a tax-equivalent basis increased for the three months ended September 30, 2019, by $778,000, or 8.9%, and for the nine months ended September 30, 2019, by $3,054,000, or 12.2%, over the same periods in 2018. Management's asset liability sensitivity measurements continue to show a benefit to both margin and NII given Federal Reserve rate increases. Actual results over the past two years have confirmed the asset sensitivity of the Corporation's balance sheet. Management expects that any remaining Federal Reserve rate decreases in 2019 would have a negative impact on both margin and NII. Any improvements in NII will be driven primarily by loan growth.

The extended extremely low Federal funds rate had enabled management to reduce the average cost of funds over a period of years. However, in 2018, this trend reversed with slight increases in both deposit and borrowings interest expense as the cost to replace maturing borrowings increased and rates paid on deposits increased slightly. The cost of funds increased even further in the first nine months of 2019 due to a change in classification of a cash management product and as a result of higher rates paid on time deposits and long-term borrowings. While the low Prime rate reduced the average yield on the Corporation's loans for many years, the rate increases in 2018, did act to enhance interest income. With a lower Prime rate projected throughout the remainder of 2019, the Corporation's asset yields will see a decrease, but helping to offset this decline could be a stabilization of costs on the interest expense side. The potential of Federal Reserve rate decreases acts to lower the Corporation's NII and net interest margin (NIM) because of the variable rate portion of the loan portfolio, which resets every time the Prime rate changes.

Security yields will generally fluctuate more rapidly than loan yields based on changes to the U.S. Treasury rates and yield curve. With lower Treasury rates in the first nine months of 2019 compared to the same period in 2018, security reinvestment has been occurring at lower levels as cash flows from the securities portfolio are generally being reallocated into loan portfolio growth. Because of the lower market interest rates and very flat yield curve, it is difficult to achieve substantially higher yields in the investment portfolio.

The Corporation’s loan portfolio yield has increased over prior years’ periods as the variable rate portion of the loan portfolio repriced higher with each Federal Reserve rate movement prior to the third quarter of 2019. The vast majority of the Corporation’s commercial Prime-based loans were priced at the Prime rate, which was 5.50%, throughout the first six months of 2019 and then 5.00% as of September 30, 2019. The pricing for the most typical five-year fixed rate commercial loans is currently very similar to the Prime rate. With the July, September, and October Federal Reserve 0.25% rate reductions, adding variable rate loans to the portfolio means they will immediately reprice down when the Fed lowers rates. There are elements of the Corporation’s Prime-based commercial loans priced above the Prime rate based on the level of credit risk of the borrower. Management does price a portion of consumer variable rate loans above the Prime rate, which also helps to improve loan yield. Both commercial and consumer Prime-based pricing continues to be influenced by local competition.

Mid-term and long-term interest rates on average were lower in 2019 compared to 2018. The average rate of the 10-year U.S. Treasury was 2.26% in the first nine months of 2019 compared to 2.87% in the first nine months of 2018, and it stood at 1.68% on September 30, 2019, compared to 3.05% on September 30, 2018. The slope of the yield curve has been compressed throughout 2018 and even inverted through the first nine months of 2019, with the 10-year U.S. Treasury rate lower than the overnight Fed funds rate by 32 basis points. As of September 30, 2018, the 10-year U.S. Treasury rate was 80 basis points higher than the Fed funds rate. The slope of the yield curve has fluctuated many times in the past two years with the 10-year U.S. Treasury yield as high as 2.79% in the first nine months of 2019 and 3.11% in the first nine months of 2018, and as low as 1.47% in 2019, and 2.44% in 2018.

While the Corporation’s overall cost of funds remains low, there were increases in 2018 and through the first nine months of 2019 due to higher interest expense on both deposits and borrowings. Core deposit interest rates are still very low and have not been increased significantly, although time deposit rates have increased for two odd-month CD specials that were initiated in the fourth quarter of 2018 and discontinued in the fourth quarter of 2019. The Corporation increased interest rates marginally on the Corporation’s interest bearing core accounts. Further rate increases are not as likely given the recent Federal Reserve rate decreases in the third and fourth quarters of 2019. Typically, financial institutions will make small systematic moves on core interest bearing accounts while making larger rate increases in the pricing of new or reissued time deposits. Borrowing costs, and the wholesale borrowing curves that they are based on, generally follow the direction and slope of the U.S. Treasury curve. However, these curves can be quicker to rise and slower to fall as the providers of these funds seek to protect themselves from rate movements. The Corporation refinanced the majority of borrowings at higher rates in 2018 and 2019 as lower-priced borrowings matured with no ability to refinance at lower rates, so the interest rates on borrowings increased during 2018 and during the first nine months of 2019.

Management currently anticipates that the overnight interest rate and Prime rate will stay at the current level after the Federal Reserve rate decrease that was effective October 30, 2019. It is likely that mid and long-term U.S. Treasury rates will remain relatively suppressed throughout the remainder of the year. This flat yield curve makes it more difficult for management to lend out or reinvest at higher interest rates out further on the yield curve. However, the anticipation of declining rates provides some ability to hold deposit rates at current levels to control the increase in interest expense.

The following table provides an analysis of year-to-date changes in net interest income by distinguishing what changes were a result of average balance increases or decreases and what changes were a result of interest rate increases or decreases.

RATE/VOLUME ANALYSIS OF CHANGES IN NET INTEREST INCOME
(TAXABLE EQUIVALENT BASIS, DOLLARS IN THOUSANDS)

	Nine Months Ended September 30 2019 vs. 2018			Nine Months Ended September 30, 2018 vs. 2017		
	Increase (Decrease) Due To Change In			Increase (Decrease) Due To Change In		
	Average Balances $	Interest Rates $	Net Increase (Decrease) $	Average Balances $	Interest Rates $	Net Increase (Decrease) $
INTEREST INCOME						
Interest on deposits at other banks	**(13)**	**(81)**	**(94)**	(92)	223	131
Securities available for sale:						
Taxable	**(54)**	**285**	**230**	307	394	701
Tax-exempt	**(414)**	**(19)**	**(432)**	(662)	(1,495)	(2,157)
Total securities	**(468)**	**266**	**(202)**	(355)	(1,101)	(1,456)
Loans	**3,254**	**1,322**	**4,576**	1,451	760	2,211
Regulatory stock	**37**	**33**	**70**	24	97	121
Total interest income	**2,810**	**1,540**	**4,350**	1,028	(21)	1,007
INTEREST EXPENSE						
Deposits:						
Demand deposits	**84**	**818**	**902**	16	91	107
Savings deposits	**3**	**—**	**2**	4	—	4
Time deposits	**(63)**	**281**	**219**	(92)	46	(46)
Total deposits	**24**	**1,099**	**1,123**	(72)	137	65
Borrowings:						
Total borrowings	**16**	**157**	**173**	30	206	236
Total interest expense	**40**	**1,256**	**1,296**	(42)	343	301
NET INTEREST INCOME	**2,770**	**284**	**3,054**	1,070	(364)	706

During the first nine months of 2019, the Corporation's NII on an FTE basis increased by $3,054,000, or 12.2%, over the same period in 2018. Total interest income on an FTE basis for the nine months ended September 30, 2019, increased $4,350,000, or 15.9%, from 2018, while interest expense increased $1,296,000, or 52.1%, for the nine months ended September 30, 2019, compared to the same period in 2018. The FTE interest income from the securities portfolio decreased by $202,000, or 3.2%, while loan interest income increased $4,576,000, or 22.4%. During the first nine months of 2019, additional loan volume caused by loan growth added $3,254,000 to net interest income, and the higher yields caused a $1,322,000 increase, resulting in a total increase of $4,576,000. Lower balances in the securities portfolio caused a decrease of $468,000 in NII, while higher yields on securities caused a $266,000 increase, resulting in a net decrease of $202,000. The Corporation sold a number of municipal bonds throughout 2018 and 2019 due to the reduction in the Federal Corporate tax rate as well as a desire to fund loan growth with security sales to achieve higher overall asset yields.

The average balance of interest bearing liabilities increased by 6.7% during the nine months ended September 30, 2019, compared to the prior year driven by growth in deposit balances. The higher cost on deposit accounts resulted in an increase in interest expense. Higher interest rates on all deposit groups except savings deposits caused a $1,099,000 increase in interest expense while slightly higher balances of demand and savings deposits caused an increase in expense of $24,000 resulting in a total increase of $1,123,000.

Out of all the Corporation's deposit types, interest-bearing demand deposits reprice the most rapidly, as nearly all accounts are immediately affected by rate changes. Time deposit balances decreased resulting in a $63,000 reduction to expense, and time deposits repricing to higher interest rates increased interest expense by $281,000, causing a net total increase of $219,000 in time deposit interest expense. Even with the low rate environment, the Corporation was successful in increasing balances of other deposit types.

The average balance of outstanding borrowings increased by 2.1% from the prior year, which resulted in an increase in interest expense of $16,000. The higher market interest rates increased interest expense on the Corporation's borrowings by $157,000, as long-term borrowings at lower interest rates matured and were replaced with new advances at higher rates. The aggregate of these amounts was an increase in interest expense of $173,000 related to total borrowings.

The following table shows a more detailed analysis of net interest income on an FTE basis with all the major elements of the Corporation's balance sheet, which consists of interest earning and non-interest earning assets and interest bearing and non-interest bearing liabilities. Additionally, the analysis provides the net interest spread and the net yield on interest earning assets. The net interest spread is the difference between the yield on interest earning assets and the interest rate paid on interest bearing liabilities. The net interest spread has the deficiency of not giving credit for the non-interest bearing funds and capital used to fund a portion of the total interest earning assets. For this reason, management emphasizes the net yield on interest earning assets, also referred to as the NIM. The NIM is calculated by dividing net interest income on an FTE basis into total average interest earning assets. The NIM is generally the benchmark used by analysts to measure how efficiently a bank generates NII.

COMPARATIVE AVERAGE BALANCE SHEETS AND NET INTEREST INCOME
(DOLLARS IN THOUSANDS)

	For the Three Months Ended September 30,					
	2019			2018		
	Average Balance $	Interest $	(c) Annualized Yield/Rate %	Average Balance $	Interest $	(c) Annualized Yield/Rate %
ASSETS						
Interest earning assets:						
Federal funds sold and interest on deposits at other banks	**23,790**	**128**	**2.13**	15,247	142	3.68
Securities available for sale:						
Taxable	**212,921**	**1,227**	**2.31**	217,193	1,246	2.29
Tax-exempt	**90,824**	**750**	**3.30**	102,967	873	3.39
Total securities (d)	**303,745**	**1,977**	**2.60**	320,160	2,119	2.65
Loans (a)	**729,674**	**8,538**	**4.67**	644,652	7,202	4.47
Regulatory stock	**7,270**	**129**	**7.12**	6,391	102	6.38
Total interest earning assets	**1,064,479**	**10,772**	**4.04**	986,450	9,565	3.87
Non-interest earning assets (d)	**71,738**			64,297		
Total assets	**1,136,217**			1,050,747		
LIABILITIES & STOCKHOLDERS' EQUITY						
Interest bearing liabilities:						
Demand deposits	**253,706**	**387**	**0.61**	213,018	134	0.25
Savings deposits	**205,331**	**26**	**0.05**	198,884	25	0.05
Time deposits	**136,249**	**476**	**1.39**	140,292	354	1.00
Borrowed funds	**79,151**	**412**	**2.07**	75,549	359	1.89
Total interest bearing liabilities	**674,437**	**1,301**	**0.77**	627,743	872	0.55
Non-interest bearing liabilities:						
Demand deposits	**344,179**			321,100		
Other	**4,043**			2,949		
Total liabilities	**1,022,659**			951,792		
Stockholders' equity	**113,558**			98,955		
Total liabilities & stockholders' equity	**1,136,217**			1,050,747		
Net interest income (FTE)		**9,471**			8,693	
Net interest spread (b)			**3.27**			3.32
Effect of non-interest bearing deposits			**0.28**			0.20
Net yield on interest earning assets (c)			**3.55**			3.52

(a) Includes balances of nonaccrual loans and the recognition of any related interest income. The quarter-to-date average balances include net deferred loan costs of $1,772,000 as of September 30, 2019, and $1,485,000 as of September 30, 2018. Such fees and costs recognized through income and included in the interest amounts totaled ($125,000) in 2019, and ($145,000) in 2018.
(b) Net interest spread is the arithmetic difference between the yield on interest earning assets and the rate paid on interest bearing liabilities.
(c) Net yield, also referred to as net interest margin, is computed by dividing net interest income (FTE) by total interest earning assets.
(d) Securities recorded at amortized cost. Unrealized holding gains and losses are included in non-interest earning assets.

COMPARATIVE AVERAGE BALANCE SHEETS AND NET INTEREST INCOME
(DOLLARS IN THOUSANDS)

	For the Nine Months Ended September 30,					
	2019			2018		
	Average Balance $	Interest $	(c) Annualized Yield/Rate %	Average Balance $	Interest $	(c) Annualized Yield/Rate %
ASSETS						
Interest earning assets:						
Federal funds sold and interest on deposits at other banks	**19,186**	**294**	**2.05**	19,899	388	2.61
Securities available for sale:						
Taxable	**211,397**	**3,835**	**2.42**	214,579	3,605	2.24
Tax-exempt	**91,782**	**2,305**	**3.35**	108,270	2,737	3.37
Total securities (d)	**303,179**	**6,140**	**2.70**	322,849	6,342	2.62
Loans (a)	**718,780**	**24,963**	**4.64**	623,462	20,387	4.36
Regulatory stock	**6,879**	**392**	**7.60**	6,205	322	6.92
Total interest earning assets	**1,048,024**	**31,789**	**4.05**	972,415	27,439	3.76
Non-interest earning assets (d)	**68,328**			65,067		
Total assets	**1,116,352**			1,037,482		
LIABILITIES & STOCKHOLDERS' EQUITY						
Interest bearing liabilities:						
Demand deposits	**254,256**	**1,265**	**0.67**	212,371	363	0.23
Savings deposits	**203,104**	**77**	**0.05**	196,173	75	0.05
Time deposits	**136,083**	**1,284**	**1.26**	144,210	1,065	0.99
Borrowed funds	**75,396**	**1,158**	**2.05**	73,845	985	1.78
Total interest bearing liabilities	**668,839**	**3,784**	**0.76**	626,599	2,488	0.53
Non-interest bearing liabilities:						
Demand deposits	**335,653**			310,201		
Other	**3,585**			2,828		
Total liabilities	**1,008,077**			939,628		
Stockholders' equity	**108,275**			97,854		
Total liabilities & stockholders' equity	**1,116,352**			1,037,482		
Net interest income (FTE)		**28,005**			24,951	
Net interest spread (b)			**3.29**			3.23
Effect of non-interest bearing deposits			**0.27**			0.19
Net yield on interest earning assets (c)			**3.56**			3.42

(a) Includes balances of nonaccrual loans and the recognition of any related interest income. The year-to-date average balances include net deferred loan costs of $1,684,000 as of September 30, 2019, and $1,375,000 as of September 30, 2018. Such fees and costs recognized through income and included in the interest amounts totaled ($374,000) in 2019, and ($382,000) in 2018.
(b) Net interest spread is the arithmetic difference between the yield on interest earning assets and the rate paid on interest bearing liabilities.
(c) Net yield, also referred to as NIM, is computed by dividing NII (FTE) by total interest earning assets.
(d) Securities recorded at amortized cost. Unrealized holding gains and losses are included in non-interest earning assets.

The Corporation’s interest income increased primarily due to increased interest income on loans, resulting in a higher NIM of 3.55% for the third quarter of 2019, compared to 3.52% for the third quarter of 2018 and 3.56% for the year-to-date period in 2019, compared to 3.42% for the same period in 2018. The yield earned on assets increased by 29 basis points during the nine months ended September 30, 2019, while the rate paid on liabilities increased by 23 basis points when comparing both years. This resulted in a six basis point increase in interest spread, and the effect of non-interest bearing deposits increased by eight basis points during the nine months ended September 30, 2019, compared to the prior year, resulting in the increase in NIM of fourteen basis points. Management anticipates challenges improving NIM during the remainder of 2019 as the Federal Reserve has decreased rates three times in the third and fourth quarters of 2019 putting pressure on the Corporation’s asset yields. Loan yields increased significantly during 2018 and throughout the first six months of 2019 with the higher Prime rate and higher yields on fixed-rate loans. However, with the recent declines in interest rates generally and the Prime rate specifically, loan yields are once again being challenged. Growth in the loan portfolio coupled with better yields prior to the third quarter of 2019 on variable rate loans caused loan interest income to increase through September 30, 2019. The Corporation’s loan yield increased 28 basis points in the first nine months of 2019 compared to the first nine months of 2018. Loan interest income increased $4,576,000, or 22.4%, for the nine months ended September 30, 2019, compared to the same period in 2018.

Loan pricing was challenging in early 2018 as a result of competition resulting in fixed-rate loans being priced at very low levels and variable-rate loans priced at the Prime rate or below. Pricing improved during the last half of 2018 and into the first half of 2019 with much more significant loan growth. The Prime rate was 5.00% as of September 30, 2019, and was very similar to the typical business or commercial five-year fixed rates being extended. The commercial or business fixed rates do increase with longer fixed terms or lower credit quality. In terms of the variable rate pricing, nearly all variable rate loans offered are Prime-based. Management is able to price loan customers with higher levels of credit risk at Prime plus pricing, such as Prime plus 0.75%, which amounted to 5.75% at September 30, 2019. However, there are relatively few of these higher rate loans in the commercial and agricultural portfolios due to the strong credit quality of the Corporation’s borrowers and market competition. Competition in the immediate market area has been pricing select shorter-term fixed-rate commercial and agricultural lending rates close to 4.00% for the strongest loan credits.

Tax equivalent yields on the Corporation’s securities increased by eight basis points for the nine months ended September 30, 2019, compared to the same period in 2018. The Corporation’s securities portfolio consists of nearly all fixed income debt instruments. However, the variable rate percentage of the portfolio was 16.4% as of September 30, 2019. The Corporation’s taxable securities experienced an 18 basis-point increase in yield for the nine months ended September 30, 2019, compared to the same period in 2018. Security reinvestment in the first nine months of 2019 has been occurring at higher rates even with increased amortization on mortgage-backed and collateralized mortgage obligation securities. The Corporation’s U.S. agency mortgage-backed securities and collateralized mortgage obligations experience faster principal prepayments as market rates decrease, causing the amortization of premium to increase, effectively decreasing the yield.

The yield on tax-exempt securities decreased by two basis point for the nine months ended September 30, 2019. For the Corporation, these bonds consist entirely of tax-free municipal bonds. The tax equivalent yield on this portion of the portfolio declined in 2018 due to the tax law changes. The yields on municipal bonds are not as attractive as they once were. Management was generally able to sell some of these bonds without taking net losses on this sector by taking advantage of improved bond pricing. Management desired to reduce the municipal bond sector due to three primary reasons. The first reason was to lower portfolio duration as a result of the continued Federal Reserve rate increases that were occurring in 2018. The municipal bonds typically have the longest duration out of all the Corporation’s securities. Secondly, the tax equivalent yield of all of these tax-free instruments was effectively reduced by approximately 16% as a result of the decrease in the Federal corporate tax rate from 34% to 21% at the end of 2017. Lastly, the Corporation’s loan growth increased sharply in the second half of 2018 and into 2019, making it appropriate to partially fund this asset growth from the largest segment of the securities portfolio.

The Corporation’s average deposits increased $66.1 million, or 7.7%, with all types of interest-bearing deposits increasing $40.7 million, or 7.4%, while non-interest bearing demand deposits increased $25.5 million, or 8.2%. In years prior to 2019 and 2018, with short-term rates low and with small rate differences for longer-term deposits, the consumer generally elected to stay short and maintain funds in accessible deposit instruments. Even with higher market rates available, it appears the customer still prefers keeping balances in both non-interest and interest bearing checking products and savings accounts. In addition to the consumer staying liquid with their available funds, there has been a general trend of funds flowing from time deposit accounts into non-interest checking, NOW and savings accounts. The average balance of the Corporation’s interest bearing liabilities increased during the nine months ended September 30, 2019. The average balance of time deposits declined during this same period compared to 2018, but the other areas of NOW, MMDA, and savings grew sufficiently enough to compensate for the decline in time deposits, causing total interest bearing funds to increase. However, with slightly higher rates on NOW, MMDA, and time deposits, the Corporation incurred more interest expense. Time deposit balances have been growing more recently due to the odd-month CD promotions currently available but management expects these time deposit balances to level out throughout the remainder of 2019 as a result of the discontinuance of the CD promotions in the fourth quarter of 2019. It is anticipated that the growth achieved throughout 2019 will continue to result in higher interest expense, but also will provide needed liquidity to fund loan growth.

Interest expense on deposits increased by $1,123,000, or 74.7%, for the nine months ended September 30, 2019, compared to the same period in 2018. Demand and savings deposits reprice in their entirety whenever the offering rates are changed, therefore management is cautious in terms of increasing portfolio interest rates. Interest rates on interest checking and money market accounts were increased slightly in the fourth quarter of 2018. No core deposit rates were changed in the first nine months of 2019. For the nine months ended September 30, 2019, the average balances of interest bearing demand deposits increased by $41.9 million, or 19.7%, over the same period in 2018, while the average balance of savings accounts increased by $6.9 million, or 3.5%.

Time deposits reprice over time according to their maturity schedule. This enables management to both reduce and increase rates slowly over time. During the nine months ended September 30, 2019, time deposit balances decreased compared to balances at September 30, 2018. The decrease can be attributed to the low rates paid on time deposits, which has caused the differential between time deposit rates and rates on non-maturity deposits to be minimal, as well as more competitive time deposit rates being offered by other financial institutions in the local market area. As a result, customers have elected to keep more of their funds in non-maturity deposits and less funds in time deposits. Because time deposits are the most expensive deposit product for the Corporation and the largest dollar expense from a funding standpoint, the reduction in time deposits, along with the increases in interest-bearing checking, savings, and non-interest bearing checking, has allowed the Corporation to achieve a more balanced deposit funding position and maintain a lower cost of funds. However, beginning in the fourth quarter of 2018 and continuing into the first nine months of 2019, time deposit balances began to increase once again with the offering of two odd-month term time deposit specials. Management expects this trend to slow down throughout the remainder of 2019 as these specials were discontinued in October 2019. The Corporation's interest expense on time deposits increased by $219,000, or 20.6%, for the first nine months of 2019, compared to the same period in 2018, despite the decrease in average balance. This growth in interest expense was due to the higher promotional rates that were offered beginning in the fourth quarter of 2018. Average balances of time deposits decreased by $8.1 million, or 5.6%, for the nine months ended September 30, 2019, compared to the same period in 2018. The average annualized interest rate paid on time deposits increased by 27 basis points for the nine-month period when comparing both years.

The Corporation historically uses both short-term and long-term borrowings to supplement liquidity generated by deposit growth. Average short-term advances of $2,340,000 were utilized in the nine months ended September 30, 2019, while average short-term advances of $6,749,000 were utilized in the nine months ended September 30, 2018. Management has used long-term borrowings as part of an asset liability strategy to lengthen liabilities rather than as a source of liquidity. Average total borrowings increased by $1,551,000, or 2.1%, for the nine months ended September 30, 2019, compared to the same period in 2018. Interest expense on borrowed funds was $173,000, or 17.6% higher, for the nine-month period when comparing 2019 to 2018.

For the nine months ended September 30, 2019, the net interest spread increased by six basis points to 3.29%, compared to 3.23% for the nine months ended September 30, 2018. The effect of non-interest bearing funds increased by eight basis points for the nine-month period compared to the same period in the prior year. The effect of non-interest bearing funds refers to the benefit gained from deposits on which the Corporation does not pay interest. As rates go higher, the benefit of non-interest bearing deposits increases because there is more difference between non-interest bearing funds and interest bearing liabilities. For example, if an interest checking account with $10,000 earns 1%, the benefit for $10,000 of non-interest bearing deposits is equivalent to $100; but if the interest-checking rate is increased to 1.50%, then the benefit of the non-interest bearing funds is $150. This assumes dollar-for-dollar replacement, which is not realistic, but demonstrates the way the higher cost of funds affects the benefit to non-interest bearing deposits.

The Asset Liability Committee (ALCO) carefully monitors the NIM because it indicates trends in net interest income, the Corporation’s largest source of revenue. For more information on the plans and strategies in place to protect the NIM and moderate the impact of rising rates, refer to Item 7A: Quantitative and Qualitative Disclosures about Market Risk.

Provision for Loan Losses

The allowance for loan losses (ALLL) provides for losses inherent in the loan portfolio as determined by a quarterly analysis and calculation of various factors related to the loan portfolio. The amount of the provision reflects the adjustment management determines necessary to ensure the ALLL is adequate to cover any losses inherent in the loan portfolio. The Corporation recorded a provision expense of $630,000 for the three months ended September 30, 2019, and $840,000 for the nine months ended September 30, 2019, compared to $190,000 and $470,000 for the three and nine months ended September 30, 2018, respectively. The analysis of the ALLL takes into consideration, among other things, the following factors:

- levels and trends in delinquencies, nonaccruals, charge-offs and recoveries,
- trends within the loan portfolio,
- changes in lending policies and procedures,
- experience of lending personnel and management oversight,
- national and local economic trends,
- concentrations of credit,
- external factors such as legal and regulatory requirements,
- changes in the quality of loan review and board oversight, and
- changes in the value of underlying collateral.

During the nine months ended September 30, 2019, the Corporation recorded provision expense of $840,000 primarily due to growth in the loan portfolio and an increase in nonaccrual and classified loans. Management closely tracks delinquent, non-performing, and classified loans as a percentage of capital and of the loan portfolio.

As of September 30, 2019, total delinquencies represented 0.56% of total loans, compared to 0.38% as of September 30, 2018. These ratios are extremely low compared to local and national peer groups. The vast majority of the Corporation’s loan customers have remained very steadfast in making their loan payments and avoiding delinquency, even during challenging economic conditions. The delinquency ratios speak to the long-term health, conservative nature, and, importantly, the character of the Corporation’s customers and lending practices. Classified loans are primarily determined by loan-to-value and debt-to-income ratios. The level of classified loans has increased from September 30, 2018 to September 30, 2019, from 13.9% of regulatory capital to 15.7% of regulatory capital. The delinquency and classified loan information is utilized in the quarterly ALLL calculation, which directly affects the provision expense. A sharp increase or decrease in delinquencies and/or classified loans during the quarter would be cause for management to increase or decrease the provision expense. The level of actual charge-offs relative to the amount of recoveries can also have a significant impact on the provision. Management had charge-offs that exceeded recoveries by $32,000 in the first nine months of 2019.

Generally, management will evaluate and adjust, if necessary, the provision expense each quarter based upon completion of the quarterly ALLL calculation. Future provision amounts will generally depend on the amount of loan growth achieved versus levels of delinquent, non-performing, and classified loans, as well as charge-offs and recoveries.

In addition to the above, provision expense is impacted by three major components that are all included in the quarterly calculation of the ALLL. First, specific allocations are made for any loans where management has determined an exposure that needs to be provided for. These specific allocations are reviewed each quarter to determine if adjustments need to be made. It is common for specific allocations to be reduced as additional principal payments are made, so while some specific allocations are being added, others are being reduced. Second, management provides for estimated losses on pools of similar loans based on historical loss experience. Finally, management utilizes qualitative factors every quarter to adjust historical loss experience to take into consideration the current trends in loan volume, delinquencies, charge-offs, changes in lending practices, and the quality of the Corporation’s underwriting, credit analysis, lending staff, and Board oversight. National and local economic trends and conditions are also helpful to determine the amount of loan loss allowance the Corporation should be carrying on the various types of loans. Management evaluates and adjusts, if necessary, the qualitative factors on a quarterly basis.

In the first nine months of 2019, qualitative factors were adjusted based on current information regarding delinquency, economic conditions, and other factors. Changes in qualitative factors were unchanged for two loan pools and declined for the other seven loan pools. Adjustments to the qualitative factors were minor in nature with most changes being only five or ten basis points of adjustment, the lowest amount of adjustment that management will make.

Management also monitors the allowance as a percentage of total loans. The percentage of the allowance to total loans has increased since September 30, 2018, and remains higher than the Bank's national peer group from the Uniform Bank Performance Reports. As of September 30, 2019, the allowance as a percentage of total loans was 1.28%, up from 1.26% at September 30, 2018, and up from 1.25% as of December 31, 2018. Management continues to evaluate the ALLL in relation to the size of the loan portfolio and changes to the segments within the loan portfolio and their associated credit risk. Management believes the ALLL is adequate to provide for future loan losses based on the current portfolio and the current economic environment. More detail is provided under Allowance for Loan Losses in the Financial Condition section that follows.

Other Income

Other income for the third quarter of 2019 was $2,943,000, an increase of $156,000, or 5.6%, compared to the $2,787,000 earned during the third quarter of 2018. For the year-to-date period ended September 30, 2019, other income totaled $8,249,000, a decrease of $546,000, or 6.2%, compared to the same period in 2018. The following tables detail the categories that comprise other income.

OTHER INCOME
(DOLLARS IN THOUSANDS)

	Three Months Ended September 30,		Increase (Decrease)	
	2019	2018		
	$	$	$	%
Trust and investment services	**538**	449	89	19.8
Service charges on deposit accounts	**349**	341	8	2.3
Other service charges and fees	**352**	512	(160)	(31.3)
Commissions	**734**	658	76	11.6
Gains on securities transactions, net	**42**	4	38	950.0
Gains on equity securities, net	**7**	3	4	133.3
Gains on sale of mortgages	**606**	515	91	17.7
Earnings on bank owned life insurance	**186**	186	—	0.0
Other miscellaneous income	**129**	119	10	8.4
Total other income	**2,943**	2,787	156	5.6

OTHER INCOME
(DOLLARS IN THOUSANDS)

	Nine Months Ended September 30,		Increase (Decrease)	
	2019	2018		
	$	$	$	%
Trust and investment services	**1,580**	1,477	103	7.0
Service charges on deposit accounts	**1,026**	1,006	20	2.0
Other service charges and fees	**998**	1,345	(347)	(25.8)
Commissions	**2,145**	1,899	246	13.0
Gains/(losses) on securities transactions, net	**229**	(24)	253	(1054.2)
Gains on equity securities, net	**51**	50	1	2.0
Gains on sale of mortgages	**1,370**	1,102	268	24.3
Earnings on bank owned life insurance	**543**	1,477	(934)	(63.2)
Other miscellaneous income	**307**	463	(156)	(33.7)
Total other income	**8,249**	8,795	(546)	(6.2)

Trust and investment services income increased $89,000, or 19.8%, and $103,000, or 7.0%, for the three and nine months ended September 30, 2019, compared to the same periods last year. This revenue consists of income from traditional trust services and income from alternative investment services provided through a third party. In the third quarter of 2019, traditional trust income increased by $16,000, or 5.6%, while income from alternative investments increased by $73,000, or 44.8%, compared to the third quarter of 2018. For the nine months ended September 30, 2019, traditional trust services income increased by $27,000, or 2.9%, while income from alternative investment services increased by $76,000, or 13.7%, compared to the same period in 2018. The trust and investment services area continues to be an area of strategic focus for the Corporation. Management believes there continues to be great need for retirement, estate, small business succession planning, and personal investment services in the Corporation's service area. Management also sees these services as being a necessary part of a comprehensive line of financial solutions across the organization.

Other service charges and fees decreased by $160,000, or 31.3%, and $347,000, or 25.8%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018. The decrease is primarily due to a decrease in loan administration fees that were lower by $177,000, or 69.5%, and $404,000, or 65.9%, for the three and nine months ended September 30, 2019, respectively, compared to the same periods in 2018. Additionally, mortgage origination fees were lower by $111,000 and $303,000, or 100.0%, for both the quarter and year-to-date periods in 2019 compared to the same periods in the prior year. Partially offsetting these decreases, fees on an off-balance sheet cash management product were $112,000 in the third quarter of 2019, and $300,000 for the year-to-date period in 2019, and are now being recorded in other service charges whereas in the prior year, the fees were included in interest income. Various other fee income categories increased or decreased to lesser degrees making up the remainder of the variance compared to the prior year.

Commissions increased by $76,000, or 11.6%, and $246,000, or 13.0%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018. This was primarily caused by debit card interchange income, which increased by $88,000, or 15.4%, and $247,000, or 15.0%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018. The interchange income is a direct result of the volume of debit card transactions processed and this income increases as customer accounts increase or as customers utilize their debit cards to a higher degree.

For the three and nine months ended September 30, 2019, $42,000 and $229,000 of gains on securities transactions were recorded, respectively, compared to gains of $4,000 and losses of $24,000, respectively, for the same periods in 2018. Gains or losses on securities transactions fluctuate based on market opportunities to take gains and reposition the securities portfolio to improve long-term earnings, or as part of management's asset liability goals to improve liquidity or reduce interest rate risk or fair value risk. The gains or losses recorded by the Corporation depend heavily on market pricing and the volume of security sales. Generally, the lower U.S. Treasury yields go, the more management will be motivated to pursue taking gains from the sale of securities. However, these market opportunities are evaluated subject to the Corporation's other asset liability measurements and goals. The yield curve in the first nine months of 2019 provided better opportunities to take gains out of the portfolio than during the first nine months of 2018.

Gains on the sale of mortgages were $606,000 for the three-month period ended September 30, 2019, compared to $515,000 for the same period in 2018, a $91,000, or 17.7% increase. For the nine-month period ended September 30, 2019, mortgage gains amounted to $1,370,000, compared to $1,102,000 for the same period in 2018, a $268,000, or 24.3% increase. Mortgage activity was higher in the first nine months of 2019 compared to the prior year, primarily as the result of lower long-term interest rates. Management anticipates that gains throughout the remainder of 2019 may continue at a higher level compared to the prior year due to the favorable interest rate environment and reasonable margins received on the mortgages that are being sold.

For the three months ended September 30, 2019, earnings on bank-owned life insurance (BOLI) were identical to earnings for the three months ended September 30, 2018. For the year-to-date period, earnings on BOLI decreased by $934,000, or 63.2%, compared to the same period in 2018. The large year-to-date decrease in BOLI income was caused by $913,000 of insurance proceeds received in the first quarter of 2018 due to the death of a participant. The amount of BOLI income is generally dependent upon the actual return of the policies, the insurance cost components, and any benefits paid upon death that exceed the policy's cash surrender value. Increases in cash surrender value are a function of the return of the policy net of all expenses.

The miscellaneous income category increased by $10,000, or 8.4%, for the three months ended September 30, 2019, and decreased by $156,000, or 33.7%, for the nine months ended September 30, 2019, compared to the same periods in 2018. The primary reason for the year-to-date decrease in miscellaneous income was a decrease in net mortgage servicing income which declined by $172,000 for in 2019 compared to 2018, due to the interest rate environment that resulted in faster amortization of existing mortgage servicing assets.

Operating Expenses

Operating expenses for the third quarter of 2019 were $8,128,000, an increase of $57,000, or 0.7%, compared to the $8,071,000 for the third quarter of 2018. For the year-to-date period ended September 30, 2019, operating expenses totaled $24,627,000, an increase of $505,000, or 2.1%, compared to the same period in 2018. The following tables provide details of the Corporation’s operating expenses for the three and nine-month periods ended September 30, 2019, compared to the same periods in 2018.

OPERATING EXPENSES
(DOLLARS IN THOUSANDS)

	Three Months Ended September 30,		Increase (Decrease)	
	2019	2018		
	$	$	$	%
Salaries and employee benefits	**5,227**	5,197	30	0.6
Occupancy expenses	**605**	624	(19)	(3.0)
Equipment expenses	**297**	296	1	0.3
Advertising & marketing expenses	**205**	147	58	39.5
Computer software & data processing expenses	**620**	590	30	5.1
Bank shares tax	**233**	226	7	3.1
Professional services	**448**	438	10	2.3
Other operating expenses	**493**	553	(60)	(10.8)
Total Operating Expenses	**8,128**	8,071	57	0.7

OPERATING EXPENSES
(DOLLARS IN THOUSANDS)

	Nine Months Ended September 30,		Increase (Decrease)	
	2019	2018		
	$	$	$	%
Salaries and employee benefits	**15,520**	15,378	142	0.9
Occupancy expenses	**1,825**	1,889	(64)	(3.4)
Equipment expenses	**871**	875	(4)	(0.5)
Advertising & marketing expenses	**621**	583	38	6.5
Computer software & data processing expenses	**1,886**	1,708	178	10.4
Bank shares tax	**698**	669	29	4.3
Professional services	**1,479**	1,376	103	7.5
Other operating expenses	**1,727**	1,644	83	5.0
Total Operating Expenses	**24,627**	24,122	505	2.1

Salaries and employee benefits are the largest category of operating expenses. In general, they comprise approximately 63% of the Corporation’s total operating expenses. For the three months ended September 30, 2019, salaries and benefits increased $30,000, or 0.6%, from the same period in 2018. For the nine months ended September 30, 2019, salaries and benefits increased $142,000, or 0.9%, compared to the nine months ended September 30, 2018. Salaries decreased by $71,000, or 1.8%, and employee benefits increased by $102,000, or 8.1%, for the three months ended September 30, 2019, compared to the same period in 2018. For the nine months ended September 30, 2019, salary expense decreased by $243,000, or 2.1%, while employee benefits increased by $385,000, or 10.1%, compared to the nine months ended September 30, 2018. Salary costs were lower due to higher deferred costs on loan originations which are recorded as a contra salary expense. Employee benefits expense was at a higher level for the quarter and year-to-date periods in 2019 due to higher health insurance costs which increased by $69,000, or 11.5%, and $239,000, or 13.3%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018.

Occupancy expenses consist of the following:

- Depreciation of bank buildings
- Real estate taxes and property insurance
- Building lease expense
- Utilities
- Building repair and maintenance

Occupancy expenses decreased $19,000, or 3.0%, and $64,000, or 3.4%, for the three and nine months ended September 30, 2019, compared to the same periods in the prior year. Utilities costs decreased by $12,000, or 7.4%, and $59,000, or 10.3%, when comparing the three and nine months ended September 30, 2019, to the same periods in the prior year. These savings were primarily driven by lower telephone and electric costs. Various other occupancy expense categories increased or decreased by smaller amounts making up the remainder of the quarter and year-to-date variance.

Advertising and marketing expenses increased by $58,000, or 39.5%, and $38,000, or 6.5%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018. These expenses can be further broken down into two categories, marketing expenses and public relations. The marketing expenses increased by $27,000, or 24.7%, for the quarter-to-date period, and increased by $39,000, or 10.4%, for the year-to-date period ended September 30, 2019, compared to the same periods in the prior year. Public relations expenses increased by $31,000, or 85.5%, and decreased by $1,000, or 0.6%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018. Marketing expenses support the overall business strategies of the Corporation; therefore, the timing of these expenses is highly dependent upon the execution of those strategies.

Computer software and data processing expenses increased by $30,000, or 5.1%, for the third quarter of 2019 compared to 2018, and $178,000, or 10.4%, for the nine months ended September 30, 2019, compared to the same period in 2018. Software-related expenses were up by $18,000, or 5.2%, for the three months ended September 30, 2019, and up by $36,000, or 3.6%, for the nine months ended September 30, 2019, compared to the same periods in the prior year. The increases were primarily because of increased amortization on existing software as well as purchases of new software platforms to support the strategic initiatives of the Corporation. Software expenses are likely to continue to increase in 2019, but the actual increase will be dependent on how quickly new software platforms are identified, analyzed, approved and placed into service. Data processing fees were up $48,000, or 19.6%, and $142,000, or 20.3%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018. These fees are likely to increase throughout the remainder of 2019 as data processing fees increase with the increase in customer transactions.

Bank shares tax expense was $233,000 for the third quarter of 2019, an increase of $7,000, or 3.1%, from the third quarter of 2018. For the year-to-date period, shares tax increased by $29,000, or 4.3%, compared to the prior year. Two main factors determine the amount of bank shares tax: the ending value of shareholders' equity and the ending value of tax-exempt U.S. obligations. The shares tax calculation uses a period-end balance of shareholders' equity and a tax rate of 0.95%. The increase in 2019 can be primarily attributed to the Corporation's growing value of shareholders' equity.

Professional services expense increased $10,000, or 2.3%, and $103,000, or 7.5%, for the three and nine-month periods ended September 30, 2019, compared to the same periods in 2018. These services include accounting and auditing fees, legal fees, and fees for other third-party services. Other outside service fees increased by $32,000, or 17.2%, and $110,000, or 20.7%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018. Trust department processing fees were lower by $37,000, or 113.5%, and $22,000, or 16.8%, for the three and nine months ended September 30, 2019, compared to the same periods in 2018. Several other professional services expenses increased or decreased slightly making up the remainder of the variance.

Income Taxes

Prior to 2018, the majority of the Corporation's income was taxed at a corporate rate of 34% for Federal income tax purposes. In December of 2017, the Tax Cuts and Jobs Act lowered the corporate tax rate from 34% to 21% effective for 2018 and years going forward. For the nine months ended September 30, 2019, the Corporation recorded Federal income tax expense of $1,596,000, compared to $960,000 for the nine months ended September 30, 2018. The effective tax rate for the Corporation was 15.6% for the nine months ended September 30, 2019, compared to 11.3% for the same period in 2018. The Corporation's effective tax rate has historically been maintained at low levels primarily due to a relatively high level of tax-free municipal bonds held in the securities portfolio. The fluctuation of the effective tax rate will occur as a result of total tax-free revenue as a percentage of total revenue. The lower effective tax rate for the year-to-date period in 2018 was primarily caused by the lower Federal corporate tax rate as well as a higher percentage of tax-free income that was elevated by $913,000 of BOLI death benefit recognized in the first quarter of 2018.

Certain items of income are not subject to Federal income tax, such as tax-exempt interest income on loans and securities, and BOLI income; therefore, the effective income tax rate for the Corporation is lower than the stated tax rate. The effective tax rate is calculated by dividing the Corporation's provision for Federal income taxes on the Consolidated Statements of Income by the income before income taxes for the applicable period.

The Corporation is also subject to Pennsylvania Corporate Net Income Tax; however, the Corporation's Holding Company has very limited taxable corporate net income activities. The Corporation's wholly owned subsidiary, Ephrata National Bank, is subject to Pennsylvania Bank Shares Tax. Like Federal Corporate income tax, the Pennsylvania Bank Shares Tax is a significant expense for the Corporation, amounting to $698,000 in the first nine months of 2019 compared to $669,000 in 2018. The Bank Shares Tax expense appears on the Corporation's Consolidated Statements of Income, under operating expenses.

Financial Condition

Investment Securities

The Corporation classifies all of its debt securities as available for sale and reports the portfolio at fair value. As of September 30, 2019, the Corporation had $299.0 million of securities available for sale, which accounted for 26.1% of assets, compared to 26.8% as of December 31, 2018, and 27.8% as of September 30, 2018. Based on ending balances, the securities portfolio increased 1.2% from September 30, 2018, and 1.7% from December 31, 2018.

The securities portfolio was showing a net unrealized gain of $2,111,000 as of September 30, 2019, compared to an unrealized loss of $7,254,000 as of December 31, 2018, and an unrealized loss of $10,361,000 as of September 30, 2018. The valuation of the Corporation's securities portfolio, predominately debt securities, is impacted by both the U.S. Treasury rates and the perceived forward direction of interest rates. The 10-year U.S. Treasury yield was 3.05% as of September 30, 2018, 2.69% as of December 31, 2018, and 1.68% as of September 30, 2019. The lower Treasury rates have caused an increase in market valuation, which has resulted in the unrealized gains recorded at September 30, 2019, compared to losses recorded at December 31, 2018, and September 30, 2018.

The table below summarizes the Corporation's amortized cost, unrealized gain or loss position, and fair value for each sector of the securities portfolio for the periods ended September 30, 2019, December 31, 2018, and September 30, 2018.

AMORTIZED COST AND FAIR VALUE OF SECURITIES HELD
(DOLLARS IN THOUSANDS)

	Amortized Cost $	Net Unrealized Gains (Losses) $	Fair Value $
September 30, 2019			
U.S. government agencies	**35,398**	**(82)**	**35,316**
U.S. agency mortgage-backed securities	**46,354**	**(443)**	**45,911**
U.S. agency collateralized mortgage obligations	**54,510**	**150**	**54,660**
Asset-backed securities	**19,787**	**(219)**	**19,568**
Corporate bonds	**54,672**	**—**	**54,672**
Obligations of states and political subdivisions	**86,129**	**2,727**	**88,856**
Total debt securities, available for sale	**296,850**	**2,133**	**298,983**
Equity securities	**6,130**	**(22)**	**6,108**
Total securities	**302,980**	**2,111**	**305,091**
December 31, 2018			
U.S. government agencies	31,025	(905)	30,120
U.S. agency mortgage-backed securities	46,363	(1,724)	44,639
U.S. agency collateralized mortgage obligations	55,182	(1,092)	54,090
Asset-backed securities	11,440	(41)	11,399
Corporate bonds	61,085	(1,893)	59,192
Obligations of states and political subdivisions	96,157	(1,532)	94,625
Total debt securities	301,252	(7,187)	294,065
Equity securities	6,001	(67)	5,934
Total securities	307,253	(7,254)	299,999

	Amortized Cost $	Net Unrealized Gains (Losses) $	Fair Value $
September 30, 2018			
U.S. government agencies	35,083	(1,593)	33,490
U.S. agency mortgage-backed securities	48,542	(2,292)	46,250
U.S. agency collateralized mortgage obligations	56,545	(2,001)	54,544
Asset-backed securities	7,772	(25)	7,747
Corporate bonds	59,748	(1,503)	58,245
Obligations of states and political subdivisions	98,025	(2,966)	95,059
Total debt securities	305,715	(10,380)	295,335
Equity securities	5,770	19	5,789
Total securities available for sale	311,485	(10,361)	301,124

Interest rate changes and the perceived forward direction of interest rates generally have a close relationship to the valuation of the Corporation's fixed income securities portfolio. There are also a number of other market factors that impact bond prices. During 2018, the Federal Reserve increased short-term rates four times, but mid and long-term U.S. Treasury rates did not increase at the same speed, so there was a general flattening of the yield curve throughout 2018. With lower long-term rates in the first nine months of 2019, the yield curve is even flatter resulting in the higher valuation of the securities portfolio. The 10-year U.S. Treasury reached a low of 2.44% in early 2018 then ran up to a 2018 high of 3.24% in November and slowly retreated until hitting 2.69% at the end of the year. In the first nine months of 2019, the 10-year U.S. Treasury rate slowly decreased to a September low of 1.47% before increasing slightly to 1.68% as of September 30, 2019. Management believes that U.S. Treasury rates will remain stagnant throughout the remainder of 2019 or could decrease with anticipated Federal Reserve rate decreases. Beyond interest rate movements, there are also a number of other factors that influence bond pricing including regulatory changes, financial performance of issuers, changes to credit rating of insurers of bonds, changes in market perception of certain classes of securities, and many more. Management monitors the changes in interest rates and other market influences to assist in management of the securities portfolio.

Any material increase in market interest rates would have a negative impact on the market value of the Corporation's fixed income debt securities. As of September 30, 2019, approximately 83.6% of the Corporation's debt securities were fixed rate securities with the other 16.4% variable rate. The variable rate instruments generally experience very little impact to valuation based on a change in rates, whereas the impact of a change in market interest rates will vary on the fixed rate securities according to type of bond, length and structure of each instrument. The municipal bond sector is the largest of the portfolio and, as a result, management will closely monitor the 10-year U.S. Treasury yield due to its impact on these securities. The other sectors of the portfolio have shorter lives and duration and would be more influenced by the 2-year and 5-year U.S. Treasury rates. It is anticipated that the current unrealized gains could improve even further if market rates remain stagnant or decrease during the remainder of the year.

The Corporation's effective duration decreased in the third quarter of 2019, from 3.0 as of December 31, 2018, to 2.2 as of September 30, 2019. Effective duration is a measurement of the length of the securities portfolio with a higher level indicating more length and more exposure to an increase in interest rates. The securities portfolio base case effective duration was 3.4 as of September 30, 2018, and decreased to 3.0 as of December 31, 2018, with a further decline to 2.2 as of September 30, 2019. Duration is expected to remain stable or decline slightly throughout the remainder of 2019. The Corporation was able to reduce effective duration by purchasing more variable rate securities throughout 2018. Additionally, with declining rates, pass-through structures of MBS and CMO instruments typically shorten in duration as principal payments increase.

Management's actions to maintain reasonable effective duration of the securities portfolio are part of a broader asset liability plan to continually work to mitigate future interest rate risk and fair value risk to the Corporation. Part of that strategy is to retain higher levels of cash and cash equivalents to increase liquidity and provide an immediate hedge against higher interest rates and fair value risk. However, despite taking actions to mitigate the Corporation's future risk, these risks are inherent to the banking model. Unrealized gains and losses on securities will vary significantly according to market forces. Management's focus will continue to be on the long-term performance of these securities. While management has and will continue to take gains from the portfolio when opportunities exist, the broader securities strategy remains to buy and hold debt securities until maturity. Because market interest rates were declining in the first nine months of 2019, there was some opportunity to realize gains from the sales of securities. As a result, gains from the sales of securities were up for the nine months ended September 30, 2019, compared to the prior year's period.

The Corporation typically invests excess liquidity into securities, primarily fixed-income bonds. The securities portfolio provides interest and dividend income to supplement the interest income on loans. Additionally, the securities portfolio assists in the management of both liquidity risk and interest rate risk. In order to provide maximum flexibility for management of liquidity and interest rate risk, the securities portfolio is classified as available for sale and reported at fair value. Management adjusts the value of all the Corporation's securities on a monthly basis to fair market value as determined in accordance with U.S. generally accepted accounting principles. Management has the ability and intent to hold all debt securities until maturity, and does not generally record impairment on bonds that are currently valued below book value. In addition to the fixed and variable rate bonds, the Corporation's equity holdings consist of a small CRA-qualified mutual fund with a book and fair market value of $5.5 million. The CRA fund is a Small Business Association (SBA) variable rate fund with a stable dollar price. The Corporation also has a small portfolio of bank stocks with a book value of $601,000 and fair market value of $579,000 as of September 30, 2019. The equity holdings make up 2.0% of the Corporation's securities available for sale.

All securities, bonds, and equity holdings are evaluated for impairment on a quarterly basis. Should any impairment occur, management would write down the security to a fair market value in accordance with U.S. generally accepted accounting principles, with the amount of the write down recorded as a loss on securities.

Each quarter, management sets portfolio allocation guidelines and adjusts the security portfolio strategy generally based on the following factors:

- ALCO positions as to liquidity, credit risk, interest rate risk, and fair value risk
- Growth of the loan portfolio
- Slope of the U.S. Treasury curve
- Relative performance of the various instruments, including spread to U.S. Treasuries
- Duration and average length of the portfolio
- Volatility of the portfolio
- Direction of interest rates
- Economic factors impacting debt securities

The investment policy of the Corporation imposes guidelines to ensure diversification within the portfolio. The diversity specifications provide opportunities to shorten or lengthen duration, maximize yield, and mitigate credit risk. The composition of the securities portfolio based on fair market value is shown in the following table.

SECURITIES PORTFOLIO
(DOLLARS IN THOUSANDS)

	Period Ending					
	September 30, 2019		December 31, 2018		September 30, 2018	
	$	%	$	%	$	%
U.S. government agencies	**35,316**	**11.6**	30,120	10.0	33,490	11.1
U.S. agency mortgage-backed securities	**45,911**	**15.1**	44,639	14.9	46,250	15.4
U.S. agency collateralized mortgage obligations	**54,660**	**17.9**	54,090	18.0	54,544	18.1
Asset-backed securities	**19,568**	**6.4**	11,399	3.8	7,747	2.6
Corporate debt securities	**54,672**	**17.9**	59,192	19.7	58,245	19.3
Obligations of states and political subdivisions	**88,856**	**29.1**	94,625	31.6	95,059	31.6
Total debt securities, available for sale	**298,983**	**98.0**	294,065	98.0	295,335	98.1
Marketable equity securities (a)	**6,108**	**2.0**	5,934	2.0	5,789	1.9
Total securities	**305,091**	**100.0**	299,999	100.0	301,124	100.0

(a) As of January 1, 2018, the Corporation adopted ASU 2016-01, resulting in the reclassification of equity securities from available-for sale.

The largest movements within the securities portfolio were shaped by market factors, such as:

- slope of the U.S. Treasury curve and projected forward rates
- interest spread versus U.S. Treasury rates on the various securities
- pricing of the instruments, including supply and demand for the product
- structure of the instruments, including duration and average life
- portfolio weightings versus policy guidelines
- prepayment speeds on mortgage-backed securities and collateralized mortgage obligations
- credit risk of each instrument and risk-based capital considerations
- Federal income tax considerations with regard to obligations of tax-free states and political subdivisions.

The Corporation's U.S. government agency sector increased by $1.8 million, or 5.5%, since September 30, 2018, with the weighting increased from 11.1% of the portfolio to 11.6%. In the past, management's goal was to maintain agency securities at approximately 15% of the securities portfolio. In the current rate environment, management is comfortable maintaining agencies slightly below this level. This sector is also important in maintaining adequate risk weightings of the portfolio, to ensure sufficient U.S. government securities for pledging purposes, and importantly to ladder out a schedule of agency and corporate maturities over the next 5 years to avoid any concentration of maturities. Next to U.S. Treasuries, U.S. agencies are viewed as the safest instruments and are considered by management as a foundational portion of the portfolio.

The Corporation's U.S. agency MBS and CMO sectors have remained relatively unchanged in total since September 30, 2018. These two security types both consist of mortgage instruments that pay monthly interest and principal, however the behavior of the two types vary according to the structure of the mortgage pool or CMO instrument. Management desires to maintain a substantial amount of MBS and CMOs in order to assist in adding to and maintaining a stable five-year ladder of cash flows, which is important in providing stable liquidity and interest rate risk positions. Unlike the typical U.S. agency paper, corporate bonds, and obligations of states and political subdivisions, which only pay principal at final maturity, the U.S. agency MBS and CMO securities pay contractual monthly principal and interest, but are also subject to additional prepayment of principal. The combined effect of all of these instruments paying monthly principal and interest provides the Corporation with a reasonably stable base cash flow of approximately $2.0 - $2.5 million. Cash flows coming off of MBS and CMOs do slow down and speed up as interest rates increase or decrease, which has an impact on the portfolio's length and yield. As interest rates decline, prepayment of principal on securities increases, the duration of the security shortens, and the yield declines as more amortization is required on premium bonds. When interest rates increase, the opposite of this occurs. Despite the fluctuations that occur in terms of monthly cash flow as a result of changing prepayment speeds, the monthly cash flow generated by U.S. agency MBS and CMO securities is reasonably stable and as a group is material, and helps to soften or smooth out the Corporation's total monthly cash flow from all securities.

Management invested in asset-backed securities in 2018 in the form of floating rate student loan pools in an effort to provide an instrument that will perform well in a rates-up environment and offset the interest rate risk of the longer fixed-rate municipal bonds. These securities provide a variable rate return materially above the overnight Federal funds rate in a safe investment with a risk rating very similar to that of U.S. Agency bonds. The asset-backed securities generally provide monthly principal and interest payments to complement the Corporation's ongoing cash flow. Asset-backed securities were $19.6 million as of September 30, 2019, compared to $11.4 million as of December 31, 2018, and $7.7 million as of September 30, 2018.

As of September 30, 2019, the fair value of the Corporation's corporate bonds decreased by $3.6 million, or 6.1%, from balances at September 30, 2018. Like any security, corporate bonds have both positive and negative qualities and management must evaluate these securities on a risk versus reward basis. Corporate bonds add diversity to the portfolio and provide strong yields for short maturities; however, by their very nature, corporate bonds carry a high level of credit risk should the entity experience financial difficulties. Management stands to possibly lose the entire principal amount if the entity that issued the corporate paper fails. As a result of the higher level of credit risk taken by purchasing a corporate bond, management has in place procedures to closely analyze the financial health of the company as well as policy guidelines. The guidelines include both maximum investment by issuer and minimal credit ratings that must be met in order for management to purchase a corporate bond. Financial analysis is conducted prior to every corporate bond purchase with ongoing monitoring performed on all securities held.

Obligations of states and political subdivisions, or municipal bonds, are tax-free securities that generally provide the highest yield in the securities portfolio. They also carry the longest duration on average of any instrument in the securities portfolio. In the prolonged period of historically low interest rates, the municipal bond sector has outperformed all other sectors of the portfolio. Municipal tax-equivalent yields generally start well above other taxable bonds. These instruments also experience significant fair market value gains and losses when interest rates decrease and increase. However, due to the decrease in the Federal tax rate as enacted by the Tax Cuts and Jobs Act, municipal yields do not outperform the other segments of the securities portfolio to the same degree as years prior to 2018. While the tax-equivalent yields are still good, the benefit of the tax-free income was impacted resulting in the sales of a number of municipal bonds in the fourth quarter of 2017. Additional municipal securities were sold throughout 2018 to help provide needed liquidity and to reposition the portfolio for better rates-up performance. Due to these sales, the fair market value of municipal holdings has decreased by $6.2 million, or 6.5%, from September 30, 2018 to September 30, 2019. Municipal bonds represented 29.1% of the securities portfolio as of September 30, 2019, compared to 31.6% as of September 30, 2018. The Corporation's investment policy limits municipal holdings to 125% of Tier 2 capital. As of September 30, 2019, municipal holdings amounted to 72% of Tier 2 capital.

By policy, management is to identify and recommend whether to hold or sell securities with credit ratings that have fallen below minimum policy credit ratings required at the time of purchase, or below investment grade. Management monitors the security ratings on a monthly basis and reviews quarterly with the Board of Directors. Management, with Board approval, determines whether it is in the Corporation's best interest to continue to hold any security that has fallen below policy guidelines or below investment grade based on the expectation of recovery of market value or improved performance. At this time management has elected, and the Board has approved, holding all securities that have fallen below initial policy guidelines. As of September 30, 2019, no securities have fallen below investment grade.

As of September 30, 2019, fifteen of the thirty corporate securities held by the Corporation showed an unrealized holding loss. These securities with unrealized holding losses were valued at 99.4% of book value. The Corporation's investment policy requires that corporate bonds have a minimum credit rating of A3 by Moody's or A- by S&P or Fitch at the time of purchase, or an average or composite rating of A-. As of September 30, 2019, all but two of the corporate bonds had at least one A3 or A- rating by one of the two predominate credit rating services, Moody's and S&P. These two corporate bonds were from the same issuer and had a total book value of $3.0 million, and did not have an A3 or A- rating as of September 30, 2019. These bonds were rated Moody's Baa1 and S&P BBB+, which are two levels above the minimum required to be considered investment grade. Management conducts ongoing monitoring of these bonds and has chosen to continue to hold these bonds with Board approval. In addition, there are thirteen corporate bond instruments that have split ratings with the highest rating within the Corporation's initial purchase policy guidelines and the lower rating outside of management guidelines, but all are still investment grade. The thirteen bonds have a book value of $21.6 million with a $36,000 unrealized gain as of September 30, 2019. Management conducts ongoing monitoring of these bonds with the Board approving holding these securities on a quarterly basis. Currently, there are no indications that any of these bonds would discontinue contractual payments.

The Corporation's investment policy requires that municipal bonds not carrying insurance have a minimum credit rating of A3 by Moody's or A- by S&P or Fitch at the time of purchase. As of September 30, 2019, no municipal bonds carried a credit rating under these levels.

Management utilizes several municipal surveillance reports and engages an independent non-brokerage service third party to perform enhanced municipal credit evaluation. Management will typically sell municipal securities if negative trends in financial performance are found and/or ratings have declined to levels deemed unacceptable. As a result of the above monitoring and actions taken to proactively sell weaker municipal credits, the Corporation's entire municipal bond portfolio consists of investment grade credits.

The entire securities portfolio is reviewed monthly for credit risk and evaluated quarterly for possible impairment. The Corporation's municipal and corporate bonds present the largest credit risk and highest likelihood for any possible impairment. Due to the ability for corporate credit situations to change rapidly and ongoing nationwide concerns of pension obligations impacting municipalities, management continues to closely monitor all corporate and municipal securities.

Loans

Net loans outstanding increased by 10.5%, to $728.6 million at September 30, 2019, from $659.3 million at September 30, 2018. Net loans increased by 6.3%, an annualized rate of 8.4%, from $685.4 million at December 31, 2018. The following table shows the composition of the loan portfolio as of September 30, 2019, December 31, 2018, and September 30, 2018.

LOANS BY MAJOR CATEGORY
(DOLLARS IN THOUSANDS)

	September 30, 2019		December 31, 2018		September 30, 2018	
	$	%	$	%	$	%
Commercial real estate						
Commercial mortgages	**113,744**	**15.4**	101,419	14.6	100,871	15.1
Agriculture mortgages	**173,697**	**23.6**	165,926	24.0	157,057	23.6
Construction	**17,661**	**2.4**	18,092	2.6	19,245	2.9
Total commercial real estate	**305,102**	**41.4**	285,437	41.2	277,173	41.6
Consumer real estate (a)						
1-4 family residential mortgages	**250,898**	**34.1**	219,037	31.6	207,992	31.2
Home equity loans	**11,366**	**1.5**	10,271	1.5	10,328	1.6
Home equity lines of credit	**69,113**	**9.4**	64,413	9.3	64,151	9.6
Total consumer real estate	**331,377**	**45.0**	293,721	42.4	282,471	42.4
Commercial and industrial						
Commercial and industrial	**56,690**	**7.7**	61,043	8.8	54,836	8.2
Tax-free loans	**16,575**	**2.3**	22,567	3.3	23,008	3.5
Agriculture loans	**20,918**	**2.8**	20,512	3.0	19,274	2.9
Total commercial and industrial	**94,183**	**12.8**	104,122	15.1	97,118	14.6
Consumer	**5,651**	**0.8**	9,197	1.3	9,471	1.4
Total loans	**736,313**	**100.0**	692,477	100.0	666,233	100.0
Less:						
Deferred loan fees (costs), net	**(1,791)**		(1,596)		(1,536)	
Allowance for loan losses	**9,474**		8,666		8,428	
Total net loans	**728,630**		685,407		659,341	

(a) Residential real estate loans do not include mortgage loans serviced for others which totaled $138,468,000 as of September 30, 2019, $126,916,000 as of December 31, 2018, and $117,655,000 as of September 30 2018.

There was significant growth in the loan portfolio since September 30, 2018, and December 31, 2018. Most major loan categories showed an increase in balances from September 30, 2018 and December 31, 2018. Loan growth was significant in 2018 and continued with strong growth in the first nine months of 2019.

The consumer residential real estate category represents the largest group of loans for the Corporation. The consumer residential real estate category of total loans increased from $282.5 million on September 30, 2018, to $331.4 million on September 30, 2019, a 17.3% increase. This category includes closed-end fixed rate or adjustable-rate residential real estate loans secured by 1-4 family residential properties, including first and junior liens, and floating rate home equity loans. The 1-4 family residential mortgages account for the vast majority of residential real estate loans with fixed and floating home equity loans making up the remainder. Historically, the entire consumer residential real estate component of the loan portfolio has averaged close to 40% of total loans. As of September 30, 2018, this percentage was 42.4%, and as of September 30, 2019, it increased to 45.0%. Management expects the consumer residential real estate category to increase at a similar pace throughout the remainder of 2019 due to a continued effort to increase mortgage volume and lower interest rates, which should continue to motivate home buyers and those refinancing. The economic conditions for consumers have also improved slightly going into 2019. Consumer disposable income is higher and home valuations have increased, which has increased the equity available in their homes. These favorable conditions to originate mortgages are subject to market conditions that can change rather quickly. Mortgage volume would slow should interest rates reverse course and home valuations decline later in 2019.

The first lien 1-4 family mortgages increased by $42.9 million, or 20.6%, from September 30, 2018, to September 30, 2019. These first lien 1-4 family loans made up 74% of the residential real estate total as of September 30, 2018, and 76% as of September 30, 2019. The vast majority of the first lien 1-4 family closed end loans consist of single family personal first lien residential mortgages and home equity loans, with the remainder consisting of 1-4 family residential non-owner-occupied mortgages. In the first nine months of 2019, purchase money origination constituted 76% of the Corporation's mortgage originations with construction-only and construction-permanent loans making up 32% of that. Total production increased by 18% over the previous quarter and year-to-date originations were up by 13% compared to the same period in 2018. The growth in the Corporation's held-for-investment portfolio continued to be concentrated in its ARM products. As of September 30, 2019, ARM balances were $119.0 million, 24.3% higher compared to December 31, 2018. During the first nine months of 2019, 28% of all ARMs booked were 10/1 ARMs, 48% were 7/1 ARMs, and 24% were 5/1 ARMs. The ARM product is beneficial to the Corporation as it limits the interest rate risk to a much shorter time period. As of the end of the quarter, 61% of the residential loan portfolio of the Corporation was adjustable rate mortgages. Market conditions were favorable in the third quarter and combined with an increase in overall production, the gains on the sale of mortgages increased by 18% quarter-over-quarter and by 24% year-to-date compared to the first nine months of 2018.

As of September 30, 2019, the remainder of the residential real estate loans consisted of $11.4 million of fixed rate junior lien home equity loans, and $69.1 million of variable rate home equity lines of credit (HELOCs). This compares to $10.3 million of fixed rate junior lien home equity loans, and $64.2 million of HELOCs as of September 30, 2018. Therefore, combined, these two types of home equity loans increased from $74.5 million to $80.5 million, an increase of 8.1%. The Prime rate had remained at a very low level of 3.25% for seven years beginning in December of 2008 and increased by 25 basis points to 3.50% in December of 2015 and another 25 basis points to 3.75% in December of 2016 before increasing three more times in 2017 and 4 times in 2018 ending the year at a rate of 5.50%. The majority of borrowers chose variable-rate HELOC products throughout 2018 instead of fixed-rate home equity loans. In addition, multiple HELOC specials with a low introductory rate were offered in 2018, which encouraged more HELOC activity resulting in the increase in this category of loans since the prior year. While 2018 did not see a significant shift away from the variable-rate HELOC product, more consumers did move to a fixed rate product in the first half of 2019 as rates had increased several times throughout the past number of years. However, with the Federal Reserve rate decreases in the third and fourth quarters of 2019, customers may move back to more variable rate product. Management expects HELOC activity to increase during the remainder of 2019 as customers may elect to borrow more funds on their lines with lower interest rates.

Commercial real estate makes up of 41.4% of total loans as of September 30, 2019, compared to 41.6% of total loans as of September 30, 2018. Within the commercial real estate segment there has been an increase in agricultural mortgages and commercial mortgages over the past year, with construction based mortgages declining slightly. Agricultural mortgages increased $16.6 million, or 10.6%, from $157.1 million as of September 30, 2018, to $173.7 million as of September 30, 2019. The increase in agricultural mortgages was caused by an increase in the pipeline of agricultural projects throughout 2018. These loans are now closing as some farmers are moving ahead with projects that may have been on hold for a period of time. Dairy lending remains constrained with milk prices at three-year lows and it does not appear pricing will improve materially in the immediate future. There have been overcapacity issues with some consolidation of the area's larger milk producers. Several dairy farmers have left the industry or are in the process of doing so. Egg prices improved in 2018, with average prices materially above the 2017 average. Approximately 45% of the Corporation's agricultural purpose loans support dairy operations while another 25% are either broiler or egg producers. Management believes the level of agricultural mortgages will steadily increase aided by the Corporation's renewed focus on the agricultural community and a full staff ready to meet agriculture lending needs but challenged by the declining economic conditions for farmers in the local market area.

Commercial real estate loans increased to $305.1 million at September 30, 2019, from $277.2 million at September 30, 2018, a 10.1% increase. The increase in commercial real estate occurred in the agriculture and commercial mortgages. Agriculture mortgages increased by $16.6 million, or 10.6%, and commercial mortgages increased by $12.9 million, or 12.8%, from September 30, 2018, to September 30, 2019. The agricultural mortgages, along with agricultural loans not secured by real estate, accounted for 26.4% of the entire loan portfolio as of September 30, 2019, compared to 26.5% as of September 30, 2018. Management believes as economic conditions improve further in 2019, other elements of the local diversified economy outside of the agriculture industry will expand and cause commercial mortgages to continue to grow as well.

Commercial mortgages increased $12.8 million, or 12.7%, from balances at September 30, 2018. Commercial mortgages as a percentage of the total loan portfolio increased to 15.4% as of September 30, 2019, compared to 15.1% at September 30, 2018. New loan production in this segment is currently outpacing normal principal payments, pay downs, and payoffs. The commercial real estate market environment is showing slow growth in the Corporation's market area but more competition is vying for this business. Management expects commercial real estate loans to remain stable as a percentage of the Corporation's loans for the remainder of 2019.

The Corporation's commercial construction loan balances declined by $1.5 million, or 7.8%, from September 30, 2018 to September 30, 2019. Management was experiencing some demand for smaller residential builds like construction on existing lots but no new large scale projects. Commercial construction loans were 2.9% of the total loan portfolio as of September 30, 2018, compared to 2.4% as of September 30, 2019.

The other area of commercial lending is non-real estate secured commercial lending, referred to as commercial and industrial lending. Commercial and industrial loans not secured by real estate accounted for 12.8% of total loans as of September 30, 2019, compared to 14.6% as of September 30, 2018. In scope, the commercial and industrial loan sector, at 12.8% of total loans, is significantly smaller than the commercial real estate sector at 41.4% of total loans. This is consistent with management's credit preference for obtaining real estate collateral when making commercial loans. The balance of total commercial and industrial loans decreased from $97.1 million at September 30, 2018, to $94.2 million at September 30, 2019, a 3.0% decrease. This category of loans generally includes unsecured lines of credit, truck, equipment, and receivable and inventory loans, in addition to tax-free loans to municipalities. Based on current levels of demand for these types of loans and the higher level of commercial and industrial expertise that the Corporation now has, management anticipates that these loans could experience growth in the remainder of 2019.

The Corporation provides credit to many small and medium-sized businesses. Much of this credit is in the form of Prime-based lines of credit to local businesses where the line may not be secured by real estate, but is based on the health of the borrower with other security interests on accounts receivable, inventory, equipment, or through personal guarantees. Commercial and industrial loans increased to $56.7 million at September 30, 2019, a $1.9 million, or 3.5% increase, from the $54.8 million at September 30, 2018. The commercial and industrial agricultural loans grew by $1.6 million, or 8.5%, and the tax-free loans declined by $6.4 million, or 28.0%, from balances at September 30, 2018, primarily due to the payoff of a loan relationship to one local municipality.

The consumer loan portfolio decreased to $5.7 million at September 30, 2019, from $9.5 million at September 30, 2018. Consumer loans made up 0.8% of total loans on September 30, 2019, and 1.4% on September 30, 2018. The decrease in consumer loans since September 30, 2018, was primarily due to a $5.0 million consumer purpose loan made to a high net worth customer in the second quarter of 2018 that was paid off in September of 2019. The long-term trend over the past decade has seen homeowners turning to the equity in their homes to finance cars and education rather than traditional consumer loans that are generally unsecured. Slightly higher demand for unsecured credit is being outpaced by principal payments on existing loans resulting in the decrease in balances. Management anticipates that the Corporation's level of consumer loans will likely remain stable as a percentage of the portfolio, as the need for additional unsecured credit is generally offset by those borrowers wishing to reduce debt levels and move away from the higher cost of unsecured financing relative to other forms of real estate secured financing.

Non-Performing Assets

Non-performing assets include:

- Nonaccrual loans
- Loans past due 90 days or more and still accruing
- Troubled debt restructurings
- Other real estate owned

NON-PERFORMING ASSETS
(DOLLARS IN THOUSANDS)

	September 30, 2019 $	December 31, 2018 $	September 30, 2018 $
Nonaccrual loans	**2,466**	1,833	1,018
Loans past due 90 days or more and still accruing	**322**	397	102
Troubled debt restructurings	**1,157**	448	454
Total non-performing loans	**3,945**	2,678	1,574
Other real estate owned	**—**	—	—
Total non-performing assets	**3,945**	2,678	1,574
Non-performing assets to net loans	**0.54%**	0.39%	0.24%

The total balance of non-performing assets increased by $2.4 million, or 150.6%, from September 30, 2018 to September 30, 2019, and increased by $1.3 million, or 47.3%, from December 31, 2018 to September 30, 2019. The increase from the prior year was primarily due to a combination of higher levels of nonaccrual loans and troubled debt restructurings (TDRs). Loans past due 90 days or more and still accruing were up $220,000 from the prior year period, but down slightly since December 31, 2018. The increase in nonaccrual loans was a result of the addition of two business relationships totaling approximately $800,000 and an agricultural relationship totaling $846,000. These additions were partially offset by the payoff of two agricultural-related loans in the amount of $816,000 in the third quarter of 2019 that were on nonaccrual status, as well as the charge-off of two business loans totaling $164,000 that were previously nonaccrual loans. One TDR loan in the amount of $718,000 was added in 2019 when payment terms were changed on a real estate secured agricultural-purpose loan. An older TDR loan that accounted for the total TDR balances as of September 30, 2018 and December 31, 2018, had a $439,000 balance as of September 30, 2019.

Management continues to monitor delinquency trends and the level of non-performing loans closely. At this time, management believes that the potential for material losses related to non-performing loans is increasing with the level of delinquencies slightly higher than those experienced in 2018.

There was no other real estate owned (OREO) as of September 30, 2019, December 31, 2018, or September 30, 2018.

Allowance for Loan Losses

The allowance for loan losses is established to cover any losses inherent in the loan portfolio. Management reviews the adequacy of the allowance each quarter based upon a detailed analysis and calculation of the allowance for loan losses. This calculation is based upon a systematic methodology for determining the allowance for loan losses in accordance with generally accepted accounting principles. The calculation includes estimates and is based upon losses inherent in the loan portfolio. The allowance calculation includes specific provisions for under-performing loans and general allocations to cover anticipated losses on all loan types based on historical losses. The calculation is also influenced by nine qualitative factors that are adjusted on a quarterly basis as needed. Based on the quarterly loan loss calculation, management will adjust the allowance for loan losses through the provision as necessary. Changes to the allowance for loan losses during the year are primarily affected by five main factors:

- Historical loan losses
- Qualitative factor adjustments including levels of delinquent and non-performing loans
- Growth trends of the loan portfolio
- Recovery of loans previously charged off
- Provision for loan losses

Strong credit and collateral policies have been instrumental in producing a favorable history of loan losses for the Corporation. The Allowance for Loan Losses table below shows the activity in the allowance for loan losses for the nine-month periods ended September 30, 2019 and September 30, 2018. At the bottom of the table, two benchmark percentages are shown. The first is net charge-offs as a percentage of average loans outstanding for the year. The second is the total allowance for loan losses as a percentage of total loans.

ALLOWANCE FOR LOAN LOSSES
(DOLLARS IN THOUSANDS)

	Nine Months Ended September 30,	
	2019	2018
	$	$
Balance at January 1,	**8,666**	8,240
Loans charged off:		
Real estate	**122**	244
Commercial and industrial	**63**	110
Consumer	**26**	26
Total charged off	**211**	380
Recoveries of loans previously charged off:		
Real estate	**(129)**	(30)
Commercial and industrial	**(47)**	(61)
Consumer	**(3)**	(7)
Total recovered	**(179)**	(98)
Net loans charged-off	**32**	282
Provision charged to operating expense	**840**	470
Balance at September 30,	**9,474**	8,428
Net charge-offs as a % of average total loans outstanding	**0.00%**	0.05%
Allowance at end of period as a % of total loans	**1.28%**	1.26%

Charge-offs for the nine months ended September 30, 2019, were $211,000, compared to $380,000 for the same period in 2018. Management typically charges off unsecured debt over 90 days delinquent with little likelihood of recovery. In the first nine months of 2019, the Corporation charged off a business relationship totaling $164,000 and several smaller amounts related to consumer loans. Recoveries were higher in the first nine months of 2019 as the Corporation recovered $128,000 related to one commercial loan relationship and smaller amounts related to other loans. In the first nine months of 2018, a large commercial loan relationship was charged off as well as several small consumer loans.

The allowance as a percentage of total loans represents the portion of the total loan portfolio for which an allowance has been provided. Management regularly reviews the overall risk profile of the loan portfolio and the impact that current economic trends have on the Corporation's loans. The financial industry typically evaluates the quality of loans on a scale with "unclassified" representing healthy loans, "special mention" being the first indication of credit concern, and several successive classified ratings indicating further credit declines of "substandard," "doubtful," and, ultimately, "loss."

The Corporation's level of classified loans was $19.4 million on September 30, 2019, compared to $15.9 million on September 30, 2018. Total classified loans have increased during the first nine months of 2019 primarily related to the downgrade of an agricultural customer with $1.4 million in outstanding balances as well as several other agricultural-related downgrades. Having more loans in a classified status could result in a larger allowance as higher amounts of projected historical losses and qualitative factors are attached to these loans. In addition to this impact, management performs a specific allocation test on these classified loans. There was $596,000 of specifically allocated allowance against the classified loans as of September 30, 2019, $132,000 of specific allocation as of December 31, 2018, and $116,000 of specific allocation as of September 30, 2018. Typically, as the classified loan balances fluctuate, the associated specific allowance applied to them fluctuates, resulting in a lower or higher required allowance.

The net charge-offs as a percentage of average total loans outstanding indicates the percentage of the Corporation's total loan portfolio that has been charged off during the period, after reducing charge-offs by recoveries. The Corporation continues to experience low net charge-off percentages due to strong credit practices. Management continually monitors delinquencies, classified loans, and non-performing loans closely in regard to how they may impact charge-offs in the future. The actual charge-offs have been running at moderate levels, and management expects this to continue through the remainder of 2019. Management practices are in place to reduce the number and severity of losses. In regard to severely delinquent loans, management attempts to improve the Corporation's collateral or credit position and, in the case of a loan workout, intervene to minimize additional charge-offs.

The allowance as a percentage of total loans was 1.28% as of September 30, 2019, 1.25% as of December 31, 2018, and 1.26% as of September 30, 2018. Management anticipates that the allowance percentage will remain fairly stable during the remainder of 2019, as the allowance balance is increased with additional provision expense to account for loan growth throughout the year. It is typical for the allowance for loan losses to contain a small amount of excess reserves. Management desires that the amount of excess reserve in the allowance for loan losses be maintained between 5% and 10%. The excess reserve stood at 2.5% as of September 30, 2019.

Premises and Equipment

Premises and equipment, net of accumulated depreciation, decreased by $0.5 million, or 1.9%, to $25.2 million as of September 30, 2019, from $25.7 million as of September 30, 2018. As of September 30, 2019, $202,000 was classified as construction in process compared to $85,000 as of September 30, 2018. Fixed assets declined as a result of depreciation outpacing new purchases in 2019.

Regulatory Stock

The Corporation owns multiple forms of regulatory stock that is required in order to be a member of the Federal Reserve Bank (FRB) and members of banks such as the Federal Home Loan Bank (FHLB) and Atlantic Community Bankers Bank (ACBB). The Corporation's $7.2 million of regulatory stock holdings as of September 30, 2019, consisted of $7.0 million of FHLB of Pittsburgh stock, $151,000 of FRB stock, and $37,000 of Atlantic Community Bancshares, Inc. stock, the Bank Holding Company of ACBB. All of these stocks are valued at a stable dollar price, which is the price used to purchase or liquidate shares; therefore, the investment is carried at book value and there is no fair market value adjustment.

The Corporation's investment in FHLB stock is required for membership in the organization. The amount of stock required is dependent upon the relative size of outstanding FHLB borrowings and mortgage activity. Excess stock is typically repurchased from the Corporation at par if the borrowings decline to a predetermined level. The Corporation's FHLB stock position was $7.0 million on September 30, 2019, $6.2 million on December 31, 2018, and $6.2 million on September 30, 2018, with no excess capital stock position. Any future stock repurchases would be the result of lower borrowing balances. Stock repurchases by the FHLB occur every quarter.

The 2018 and 2019 first quarter dividend declarations made on FHLB stock by FHLB of Pittsburgh were at a 6.75% annualized yield on activity stock and 3.50% annualized yield on membership stock. This dividend was increased to 7.75% on activity stock and 4.50% on membership stock in the second quarter of 2019. Most of the Corporation's dividend is based on the activity stock, which is based on the amount of borrowings and mortgage activity with FHLB.

Deposits

The Corporation's total ending deposits at September 30, 2019, increased by $27.3 million, or 3.0%, and by $56.1 million, or 6.3%, from December 31, 2018, and September 30, 2018, respectively. Customer deposits are the Corporation's primary source of funding for loans and securities. In the past few years, the economic concerns and volatility of the equity markets continued to lead customers to banks for safe places to invest money, despite historically low interest rates. The mix of the Corporation's deposit categories has changed moderately since September 30, 2018, with the changes being a $1.1 million, or 0.3% increase in non-interest bearing demand deposit accounts, a $4.4 million, or 5.1% increase in NOW balances, a $45.8 million, or 44.4% increase in money market balances, a $6.6 million, or 3.4% increase in savings account balances, a $2.0 million, or 1.5% increase in time deposit balances, and a $3.7 million, or 100.0% decrease in brokered CD balances.

The growth across most categories of core deposit accounts is a direct result of the opening of new branch offices as well as the expansion of business at existing branch offices. The Corporation has gained many new customers as a result of being a long-standing safe community bank known for offering understandable financial products and services with lower fees. While the prolonged historically low interest rates helped the Corporation in growing core deposits in 2016 and prior years, this has slowed down in recent years due to the Federal Reserve rate increases that have given customers more bank-related options in the market. While customers still view demand deposit, money market and savings accounts as the safest, most convenient place to maintain funds for maximum flexibility, there are more opportunities to invest in other funds outside of banks that can now compete with higher interest rates. Management believes deposit balances will grow through the remainder of 2019 at an annualized pace similar to the first nine months of 2019, as interest rates potentially decline further due to Federal Reserve rate actions.

While non-interest bearing demand deposits increased marginally from September 30, 2018, there was a decrease of $21.2 million, or 5.7%, from December 31, 2018. Similarly, money market accounts increased by $40.2 million, or 37.1%, for the same time period. This shift between non-interest bearing accounts and money market accounts was caused by the reclassification of a pool of deposits held on balance sheet related to a cash management sweep account. These deposits, totaling $30.0 million at December 31, 2018, were reclassified as money market deposits in 2019 to better reflect the nature of the product. This recategorization caused a decline of $30 million in non-interest bearing demand accounts with an offsetting increase in money market deposit accounts.

The Deposits by Major Classification table, shown below, provides the balances of each category for September 30, 2019, December 31, 2018, and September 30, 2018.

DEPOSITS BY MAJOR CLASSIFICATION
(DOLLARS IN THOUSANDS)

	September 30, 2019 $	December 31, 2018 $	September 30, 2018 $
Non-interest bearing demand	**347,929**	369,081	346,827
Interest bearing demand	**19,275**	20,104	19,379
NOW accounts	**90,444**	89,072	86,031
Money market deposit accounts	**148,863**	108,594	103,080
Savings accounts	**203,706**	199,665	197,075
Time deposits	**136,774**	130,719	134,785
Brokered time deposits	**—**	2,499	3,749
Total deposits	**946,991**	919,734	890,926

The growth and mix of deposits is often driven by several factors including:

- Convenience and service provided
- Current rates paid on deposits relative to competitor rates
- Level of and perceived direction of interest rates
- Financial condition and perceived safety of the institution
- Possible risks associated with other investment opportunities
- Level of fees on deposit products

The Corporation has been a stable presence in the local market area that has experienced several large bank mergers over the past several years. Three new convenient locations were added since 2016, significantly expanding the Corporation's footprint, with a presence in three counties with a total of thirteen branch locations. The Corporation has a history of offering competitive interest rates and fair and understandable service fees because of a strong commitment to the customers and the communities that it serves. Management has always priced products and services in a manner that makes them affordable for all customers. This in turn creates a high degree of customer loyalty and a stable deposit base. Additionally, as financial institutions have come under increased scrutiny from both regulators and customers, the Corporation has maintained an outstanding reputation. Management believes the Corporation's deposit base has benefited as a result of a growing desire by customers to seek a longstanding, reliable financial institution as a partner to meet their financial needs.

Time deposits are typically a more rate-sensitive product, making them a source of funding that is prone to balance variations depending on the interest rate environment and how the Corporation's time deposit rates compare with the local market rates. Time deposits fluctuate as consumers search for the best rates in the market, with less allegiance to any particular financial institution. As of September 30, 2019, time deposit balances, excluding brokered deposits, had increased $2.0 million, or 1.5%, from September 30, 2018, and $6.1 million, or 4.6%, from December 31, 2018. The Corporation has experienced a slow and steady shift in deposit trends over the past five years as customers have moved money from time deposits into core checking and savings accounts. With minimal differences between shorter term CD rates and interest bearing non-maturity deposits, customers are more inclined to accumulate their funds in a liquid account that can be accessed at any time. This had resulted in declining time deposit balances and more significant growth in the core deposit areas. However, in the fourth quarter of 2018, the Corporation began offering two odd-term CD products with more attractive rates that encouraged customers to invest. These promotional CD products have been effective in growing the time deposit balances since the prior year. The promotional CD rates ended in the third quarter of 2019, so management expects a slower CD growth rate throughout the remainder of 2019.

Time deposits have FDIC insurance coverage insuring no loss of principal up to $250,000 per account, based on certain account structures. As a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, the $250,000 FDIC insurance coverage on all deposit accounts was made permanent. This has caused an increase in the percentage of time deposits over $100,000 held by the Corporation.

Borrowings

Total borrowings were $80.0 million, $73.3 million, and $69.4 million as of September 30, 2019, December 31, 2018, and September 30, 2018, respectively. Of these amounts, $7.9 million and $1.1 million reflect short-term funds as of December 31, 2018 and September 30, 2018, respectively, with no short-term funds outstanding as of September 30, 2019. Short-term funds are used for immediate liquidity needs and are not typically part of an ongoing liquidity or interest rate risk strategy; therefore, they fluctuate more rapidly. When short-term funds are used, they are purchased through correspondent and member bank relationships as overnight borrowings or through the FHLB for terms less than one year.

Total long-term borrowings, borrowings initiated for terms longer than one year, were $80.0 million as of September 30, 2019, $65.4 million as of December 31, 2018, and $68.4 million as of September 30, 2018. The long-term borrowings for the Corporation were made up entirely of FHLB long-term advances at September 30, 2019, December 31, 2018, and September 30, 2018. FHLB advances are used as a secondary source of funding and to mitigate interest rate risk. These long-term funding instruments are typically a more effective funding instrument in terms of selecting the exact amount, rate, and term of funding rather than trying to source the same through deposits. In this manner, management can efficiently meet known liquidity and interest rate risk needs. Over the course of the past few years, the Corporation has minimally changed the ladder of long-term FHLB borrowings, by replacing maturing advances with new long-term advances typically at rate savings. After nine Federal Reserve rate increases and a higher but flatter U.S. Treasury curve, new borrowings in the first half of 2019 were being initiated at higher interest rates. However, Market interest rates declined significantly during the third quarter of 2019 with two Federal Reserve rate declines. As a result, management anticipates obtaining new FHLB long-term borrowings at lower interest rates than those advances that are maturing. Management will continue to analyze and compare the costs and benefits of borrowing versus obtaining funding from deposits.

In order to limit the Corporation's exposure and reliance to a single funding source, the Corporation's Asset Liability Policy sets a goal of maintaining the amount of borrowings from the FHLB to 15% of asset size. As of September 30, 2019, the Corporation was significantly under this policy guideline at 7.0% of asset size with $80.0 million of total FHLB borrowings. The Corporation also has a policy that limits total borrowings from all sources to 150% of the Corporation's capital. As of September 30, 2019, the Corporation was significantly under this policy guideline at 69.2% of capital with $80.0 million total borrowings from all sources. The Corporation has maintained FHLB borrowings and total borrowings well within these policy guidelines throughout all of 2018 and through the first nine months of 2019.

The Corporation continues to be well under the FHLB maximum borrowing capacity (MBC), which is currently $439.6 million. The Corporation's two internal policy limits mentioned above are far more restrictive than the FHLB MBC, which is calculated and set quarterly by FHLB.

Stockholders' Equity

Federal regulatory authorities require banks to meet minimum capital levels. The Corporation, as well as the Bank, as the solely owned subsidiary of the Corporation, maintains capital ratios well above those minimum levels. The risk-weighted capital ratios are calculated by dividing capital by total risk-weighted assets. Regulatory guidelines determine the risk-weighted assets by assigning assets to specific risk-weighted categories. The calculation of tier I capital to risk-weighted average assets does not include an add-back to capital for the amount of the allowance for loan losses, thereby making this ratio lower than the total capital to risk-weighted assets ratio.

The following tables reflect the capital ratios for the Corporation and Bank compared to the regulatory capital requirements.

REGULATORY CAPITAL RATIOS:

		Regulatory Requirements	
As of September 30, 2019	Capital Ratios	Adequately Capitalized	Well Capitalized
Total Capital to Risk-Weighted Assets			
Consolidated	**14.7%**	**8.0%**	**10.0%**
Bank	**14.6%**	**8.0%**	**10.0%**
Tier 1 Capital to Risk-Weighted Assets			
Consolidated	**13.5%**	**6.0%**	**8.0%**
Bank	**13.4%**	**6.0%**	**8.0%**
Common Equity Tier 1 Capital to Risk-Weighted Assets			
Consolidated	**13.5%**	**4.5%**	**6.5%**
Bank	**13.4%**	**4.5%**	**6.5%**
Tier 1 Capital to Average Assets			
Consolidated	**10.0%**	**4.0%**	**5.0%**
Bank	**10.0%**	**4.0%**	**5.0%**
As of December 31, 2018			
Total Capital to Risk-Weighted Assets			
Consolidated	14.3%	8.0%	10.0%
Bank	14.1%	8.0%	10.0%
Tier I Capital to Risk-Weighted Assets			
Consolidated	13.2%	6.0%	8.0%
Bank	13.0%	6.0%	8.0%
Common Equity Tier I Capital to Risk-Weighted Assets			
Consolidated	13.2%	4.5%	6.5%
Bank	13.0%	4.5%	6.5%
Tier I Capital to Average Assets			
Consolidated	10.0%	4.0%	5.0%
Bank	9.8%	4.0%	5.0%
As of September 30, 2018			
Total Capital to Risk-Weighted Assets			
Consolidated	14.6%	8.0%	10.0%
Bank	14.3%	8.0%	10.0%
Tier 1 Capital to Risk-Weighted Assets			
Consolidated	13.5%	6.0%	8.0%
Bank	13.2%	6.0%	8.0%
Common Equity Tier 1 Capital to Risk-Weighted Assets			
Consolidated	13.5%	4.5%	6.5%
Bank	13.2%	4.5%	6.5%
Tier 1 Capital to Average Assets			
Consolidated	10.1%	4.0%	5.0%
Bank	10.0%	4.0%	5.0%

Dividends play a vital role in the management of capital levels of the Corporation. Management seeks a balance between maintaining a sufficient cushion of excess capital above regulatory limits versus the payment of dividends to the shareholders as a direct return of their investment. Due to a constant stream of stable earnings, the payment of a dividend is needed to maintain capital at acceptable levels in order to provide an adequate return of equity to the shareholders.

The Corporation's dividends per share for the nine months ended September 30, 2019, were $0.46, a 7.0% increase over the $0.43 paid out in the first nine months of 2018. Dividends are paid from current earnings and available retained earnings. The Corporation's current capital plan calls for management to maintain tier I capital to average assets between 9.5% and 12.0%. The Corporation's current tier I capital ratio is 10.0%. As a secondary measurement, the capital plan also targets a long-term dividend payout ratio in the range of 30% to 45%. This ratio will vary according to income, but over the long term, the Corporation's goal is to maintain and target a payout ratio within this range. For the nine months ended September 30, 2019, the payout ratio was 30.5%. Management's goal is to maintain all regulatory capital ratios at current levels. Future dividend payout ratios are dependent on the future level of earnings and other factors that impact the level of capital.

The amount of unrealized gain or loss on the securities portfolio is reflected, net of tax, as an adjustment to capital, as required by U.S. generally accepted accounting principles. This is recorded as accumulated other comprehensive income or loss in the capital section of the consolidated balance sheet. An unrealized gain increases capital, while an unrealized loss reduces capital. This requirement takes the position that, if the Corporation liquidated the securities portfolio at the end of each period, the current unrealized gain or loss on the securities portfolio would directly impact the Corporation's capital. As of September 30, 2019, the Corporation showed an unrealized gain, net of tax, of $1,685,000, compared to an unrealized loss of $5,678,000 at December 31, 2018, and an unrealized loss of $8,200,000 as of September 30, 2018. These unrealized gains and losses, net of tax are excluded from capital when calculating the tier I capital to average assets numbers above. The amount of unrealized gain or loss on the securities portfolio, shown net of tax, as an adjustment to capital, does not include any actual impairment taken on securities, which is shown as a reduction to income on the Corporation's Consolidated Statements of Income. No impairment was recorded in the nine months ended September 30, 2019, or in the same prior year period. The changes in unrealized gains and losses are due to normal changes in market valuations of the Corporation's securities as a result of interest rate movements.

Regulatory Capital Changes

In July 2013, the federal banking agencies issued final rules to implement the Basel III regulatory capital reforms and changes required by the Dodd-Frank Act. The phase-in period for community banking organizations began January 1, 2015, while larger institutions (generally those with assets of $250 billion or more) began compliance on January 1, 2014. The final rules call for the following capital requirements:

- A minimum ratio of common equity tier I capital to risk-weighted assets of 4.5%.
- A minimum ratio of tier I capital to risk-weighted assets of 6%.
- A minimum ratio of total capital to risk-weighted assets of 8%.
- A minimum leverage ratio of 4%.

In addition, the final rules established a common equity tier I capital conservation buffer of 2.5% of risk-weighted assets applicable to all banking organizations. If a banking organization fails to hold capital above the minimum capital ratios and the capital conservation buffer, it will be subject to certain restrictions on capital distributions and discretionary bonus payments. The phase-in period for the capital conservation and countercyclical capital buffers for all banking organizations began on January 1, 2016.

Under the initially proposed rules, accumulated other comprehensive income (AOCI) would have been included in a banking organization's common equity tier I capital. The final rule allows community banks to make a one-time election not to include these additional components of AOCI in regulatory capital and instead use the existing treatment under the general risk-based capital rules that excludes most AOCI components from regulatory capital. The opt-out election was made by the Corporation with the filing of the first quarter Call Report as of March 31, 2015.

The final rules permanently grandfather non-qualifying capital instruments (such as trust preferred securities and cumulative perpetual preferred stock) issued before May 19, 2010 for inclusion in the tier I capital of banking organizations with total consolidated assets less than $15 billion as of December 31, 2009, and banking organizations that were mutual holding companies as of May 19, 2010. The Corporation does not have trust preferred securities or cumulative perpetual preferred stock with no plans to add these to the capital structure.

The proposed rules would have also modified the risk-weight framework applicable to residential mortgage exposures to require banking organizations to divide residential mortgage exposures into two categories in order to determine the applicable risk weight. In response to commenter concerns about the burden of calculating the risk weights and the potential negative effect on credit availability, the final rules do not adopt the proposed risk weights but retain the current risk weights for mortgage exposures under the general risk-based capital rules.

Consistent with the Dodd-Frank Act, the new rules replace the ratings-based approach to securitization exposures, which was based on external credit ratings, with the simplified supervisory formula approach in order to determine the appropriate risk weights for these exposures. Alternatively, banking organizations may use the existing gross-up approach to assign securitization exposures to a risk weight category or choose to assign such exposures a 1,250 percent risk weight. The Corporation does not securitize assets and has no plans to do so.

Under the rules, mortgage servicing assets (MSAs) and certain deferred tax assets (DTAs) are subject to stricter limitations than those applicable under the previous general risk-based capital rule. The rules also increased the risk weights for past-due loans, certain commercial real estate loans, and some equity exposures, and made selected other changes in risk weights and credit conversion factors.

Management has evaluated the impact of the above rules on levels of the Corporation’s capital. The final rulings were more favorable in terms of the items that would have a more significant impact to the Corporation and community banks in general. Specifically, the AOCI final ruling, which would have had the greatest negative impact to capital, provided the Corporation with an opt-out provision. The final ruling on the risk weightings of mortgages was favorable and did not have a material negative impact. The rulings as to trust preferred securities, preferred stock, and securitization of assets are not applicable to the Corporation, and presently the revised treatment of MSAs is not material to capital. The remaining changes to risk weightings on several items mentioned above such as past-due loans and certain commercial real estate loans do not have a material impact to capital presently, but could change as these levels change.

Off-Balance Sheet Arrangements

In the normal course of business, the Corporation typically has off-balance sheet arrangements related to loan funding commitments. These arrangements may impact the Corporation’s financial condition and liquidity if they were to be exercised within a short period of time. As discussed in the following liquidity section, the Corporation has in place sufficient liquidity alternatives to meet these obligations. The following table presents information on the commitments by the Corporation as of September 30, 2019.

OFF-BALANCE SHEET ARRANGEMENTS
(DOLLARS IN THOUSANDS)

	September 30, 2019 $
Commitments to extend credit:	
Revolving home equity	**98,766**
Construction loans	**31,563**
Real estate loans	**64,533**
Business loans	**122,801**
Consumer loans	**1,216**
Other	**4,785**
Standby letters of credit	**9,612**
Total	**333,276**

Significant Legislation

Dodd-Frank Wall Street Reform and Consumer Protection Act

In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) was signed into law. Dodd-Frank is intended to affect a fundamental restructuring of federal banking regulation. Among other things, Dodd-Frank creates a new Financial Stability Oversight Council to identify systemic risks in the financial system and gives federal regulators new authority to take control of and liquidate financial firms. Dodd-Frank additionally creates a new independent federal regulator to administer federal consumer protection laws. Dodd-Frank is expected to have a significant impact on the Corporation's business operations as its provisions take effect. It is difficult to predict at this time what specific cumulative impact Dodd-Frank and the yet-to-be-written implementing rules and regulations will have on community banks. However, it is expected that, at a minimum, they will increase the Corporation's operating and compliance costs and could increase interest expense. Among the provisions that have already or are likely to affect the Corporation are the following:

Holding Company Capital Requirements
Dodd-Frank requires the Federal Reserve to apply consolidated capital requirements to bank holding companies that are no less stringent than those currently applied to depository institutions. Under these standards, trust preferred securities will be excluded from tier I capital unless such securities were issued prior to May 19, 2010, by a bank holding company with less than $15 billion in assets. Dodd-Frank additionally requires that bank regulators issue countercyclical capital requirements so that the required amount of capital increases in times of economic expansion and decreases in times of economic contraction, are consistent with safety and soundness.

Deposit Insurance
Dodd-Frank permanently increased the maximum deposit insurance amount for banks, savings institutions, and credit unions to $250,000 per depositor. Additionally, on February 7, 2011, the Board of Directors of the FDIC approved a final rule based on the Dodd-Frank Act that revises the assessment base from one based on domestic deposits to one based on assets. This change, which was effective in April 2011, saved the Corporation a significant amount of FDIC insurance premiums from the significantly higher FDIC insurance premiums placed into effect after the financial crisis.

Corporate Governance
Dodd-Frank requires publicly traded companies to give stockholders a non-binding vote on executive compensation at least every three years, a non-binding vote regarding the frequency of the vote on executive compensation at least every six years, and a non-binding vote on "golden parachute" payments in connection with approvals of mergers and acquisitions unless previously voted on by shareholders. The SEC has finalized the rules implementing these requirements which took effect on January 21, 2011. The Corporation was exempt from these requirements until January 21, 2013, due to its status as a smaller reporting company. Additionally, Dodd-Frank directs the federal banking regulators to promulgate rules prohibiting excessive compensation paid to executives of depository institutions and their holding companies with assets in excess of $1.0 billion, regardless of whether the company is publicly traded. Dodd-Frank also gives the SEC authority to prohibit broker discretionary voting on elections of directors and executive compensation matters.

Limits on Interchange Fees
Dodd-Frank amended the Electronic Fund Transfer Act to, among other things, give the Federal Reserve the authority to establish rules regarding interchange fees charged for electronic debit transactions by payment card issuers having assets over $10 billion and to enforce a new statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer.

Consumer Financial Protection Bureau
Dodd-Frank created the Consumer Financial Protection Bureau (CFPB), which is granted broad rulemaking, supervisory and enforcement powers under various federal consumer financial protection laws, including the Equal Credit Opportunity Act, Truth in Lending Act, Real Estate Settlement Procedures Act, Fair Credit Reporting Act, Fair Debt Collection Act, the Consumer Financial Privacy Provisions of the Gramm-Leach-Bliley Act, and certain other statutes. The CFPB has examination and primary enforcement authority with respect to depository institutions with $10 billion or more in assets. Smaller institutions will be subject to rules promulgated by the CFPB but will continue to be examined and supervised by federal banking regulators for consumer compliance purposes. The CFPB will have authority to prevent unfair, deceptive, or abusive practices in connection with the offering of consumer financial products. Dodd-Frank authorizes the CFPB to establish certain minimum standards for the origination of residential mortgages including a determination of the borrower's ability to repay. In addition, Dodd-Frank will allow borrowers to raise certain defenses to foreclosure if they receive any loan other than a "qualified mortgage" as defined by the CFPB. Dodd-Frank permits states to adopt consumer protection laws and standards that are more stringent than those adopted at the federal level and, in certain circumstances, permits state attorneys general to enforce compliance with both the state and federal laws and regulations.

Prohibition Against Charter Conversions of Troubled Institutions

Dodd-Frank prohibits a depository institution from converting from a state to federal charter or vice versa while it is the subject of a cease and desist order or other formal enforcement action or a memorandum of understanding with respect to a significant supervisory matter unless the appropriate federal banking agency gives notice of the conversion to the federal or state authority that issued the enforcement action and that agency does not object within 30 days. The notice must include a plan to address the significant supervisory matter. The converting institution must also file a copy of the conversion application with its current federal regulator which must notify the resulting federal regulator of any ongoing supervisory or investigative proceedings that are likely to result in an enforcement action and provide access to all supervisory and investigative information relating thereto.

Interstate Branching

Dodd-Frank authorizes national and state banks to establish branches in other states to the same extent as a bank chartered by that state would be permitted. Previously, banks could only establish branches in other states if the host state expressly permitted out-of-state banks to establish branches in that state. Accordingly, banks will be able to enter new markets more freely.

Limits on Interstate Acquisitions and Mergers

Dodd-Frank precludes a bank holding company from engaging in an interstate acquisition – the acquisition of a bank outside its home state – unless the bank holding company is both well capitalized and well managed. Furthermore, a bank may not engage in an interstate merger with another bank headquartered in another state unless the surviving institution will be well capitalized and well managed. The previous standard in both cases was adequately capitalized and adequately managed.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

As a financial institution, the Corporation is subject to three primary risks:

- Credit risk
- Liquidity risk
- Interest rate risk

The Board of Directors has established an Asset Liability Management Committee (ALCO) to measure, monitor, and manage these primary market risks. The Asset Liability Policy has instituted guidelines for all of these primary risks, as well as other financial performance measurements with target ranges. The Asset Liability goals and guidelines are consistent with the Strategic Plan goals related to financial performance.

Credit Risk
For discussion on credit risk refer to the sections in Item 2. Management's Discussion and Analysis, on securities, non-performing assets, and allowance for loan losses.

Liquidity Risk
Liquidity refers to having an adequate supply of cash available to meet business needs. Financial institutions must ensure that there is adequate liquidity to meet a variety of funding needs, at a minimal cost. Minimal cost is an important component of liquidity. If a financial institution is required to take significant action to obtain funding, and is forced to utilize an expensive source, it has not properly planned for its liquidity needs. Funding new loans and covering deposit withdrawals are the primary liquidity needs of the Corporation. The Corporation uses a variety of funding sources to meet liquidity needs, such as:

- Deposits
- Loan repayments
- Maturities and sales of securities
- Borrowings from correspondent and member banks
- Current earnings

As noted in the discussion on deposits, customers have historically provided the Corporation with a reliable and steadily increasing source of funds liquidity. The Corporation also has in place relationships with other banking institutions for the purpose of buying and selling Federal funds. The lines of credit with these institutions provide immediate sources of additional liquidity. The Corporation currently has unsecured lines of credit totaling $32 million. This does not include amounts available from member banks such as the Federal Reserve Discount Window or the FHLB of Pittsburgh.

Management uses a cumulative maturity gap analysis to measure the amount of assets maturing within various periods versus liabilities maturing in those same periods. A gap ratio of 100% represents an equal amount of assets and liabilities maturing in the same stated period. Management monitors six-month, one-year, three-year, and five-year cumulative gaps to assist in determining liquidity risk. As of September 30, 2019, the six-month, and one-year, gap ratios were within corporate guidelines, but the three-year and five-year gap ratios were higher than corporate policy guidelines, due to a larger amount of loans and securities now maturing in less than five years. The six-month gap ratio was 97.7%, compared to an upper policy guideline of 155%; the one-year gap ratio was 101.0%, compared to an upper policy guideline of 140%; the three-year gap ratio was 131.1%, compared to an upper guideline of 125%; and the five-year gap ratio was 135.3%, compared to an upper policy guideline of 115%. The results show asset sensitivity. In a rising interest rate cycle with the likelihood of higher rates, higher gap ratios would be more beneficial to the Corporation. However, in a declining rate environment, being asset sensitive is unfavorable. Even though the Corporation shows asset sensitivity above policy guidelines for the longer-term gap measurements, it is likely we would be back in a rising rate environment for those longer three and five-year periods and having asset sensitivity would be beneficial in that case. Management will continue to monitor and manage the length of the balance sheet in order to sustain reasonable asset yields in a declining rate environment while still positioning for a likely rising rate environment out in the future.

Gap ratios have been increasing for the Corporation throughout 2018 and into 2019, but decreased at the end of the third quarter of 2019, showing slightly less asset sensitivity. The Corporation's assets are moderately long, but the length of the securities portfolio and the loan portfolio is more than offset by the length of the Corporation's core deposit liabilities in conjunction with holding relatively high levels of cash and cash equivalents. Beyond the non-maturity deposits, management is able to utilize the length of wholesale funding instruments to offset the declining length of the CD portfolio. Management believes that the Federal Reserve rate decreases coupled with two CD promotional rates offered since the fourth quarter of 2018, have resulted in growth to our CD portfolio during the first nine months of 2019. Management is anticipating a slow-down in the growth rate of the CD portfolio, as the odd-month CD specials ended in October, 2019.

The size and length of the Corporation's core deposit liabilities provide the most extension in terms of lengthening the liabilities on the balance sheet. The length of the core deposits is significantly longer than the Corporation's longest term deposits and wholesale borrowings. The mix of the Corporation's liabilities alone would be sufficient to offset the Corporation's longer assets and to maintain gap ratios within management's guidelines.

Management desires to control the cost of funds and improve the loan-to-deposit ratio and does have a large securities portfolio to draw liquidity from in the event deposit growth slows down. Throughout the first three quarters of 2019, management sold some securities in an effort to fund the loan growth that was occurring. With gap ratios that are already sufficiently high, management can put more of the available cash to work earning higher returns. Additionally, cash balances are high enough now that additional loan growth can be funded directly from overnight cash.

Higher gap ratios are beneficial in providing financial flexibility for the Corporation. Higher gap ratios often are an indication that there are more short-term assets on the balance sheet, providing more available liquidity. The quickest way to elevate gap ratios is to retain higher levels of cash on the balance sheet. Management may desire to have higher gap ratios when factoring in future loan growth or other funding changes to the balance sheet. Since late 2018, management has been actively working to increase the Corporation's loan-to-deposit ratio. As the loan-to-deposit ratio increases and more loans go on to the Corporation's balance sheet, the asset mix will generally lengthen and the gap ratios will decline. As of September 30, 2019, the loan-to-deposit ratio was 77.9%, compared to 75.5%, at December 31, 2018. Management does anticipate that more progress will be made on the loan-to-deposit ratio throughout the remainder of 2019, and would also anticipate that gap ratios will continue to decline slowly.

Management's desired gap levels will also change due to the direction of interest rates. In December of 2018, the Federal Reserve last increased overnight interest rates. Since then, U.S. Treasury interest rates across the yield curve have declined significantly with the yield curve flattening and even becoming inverted on the short end. On July 31, 2019, the Federal Reserve cut the overnight interest rate for the first time in ten years, with an additional decrease of 25 basis points on September 18, 2019, and another 25 basis point decline on October 30, 2019. Cash and other short term assets were directly impacted by this change in overnight rates. If the Corporation's liquid assets cannot be deployed into higher yielding longer term assets, then management will reduce the amount of cash and short-term assets to reduce the exposure to future decreases in the overnight rate. Prior to the third and fourth quarter Federal Reserve rate actions, the overnight rate was higher than long-term rates such as the 10-year U.S. Treasury. This is often an indication of a weaker economy, with a possible need for further rate cuts. Management believes the overnight Federal Funds rate will not decline further in 2019, but could possibly increase or decrease in 2020.

The risk of liabilities repricing at higher interest rates is decreasing in the present environment as the Corporation does not foresee the need to raise deposit interest rates with the recent Federal Reserve rate decreases. A number of the Corporation's maturing time deposits have already repriced to higher rates by taking advantage of the promotional CD rates. However, a large portion of the Corporation's deposits are core deposits with little repricing expected to occur in the near future. The Corporation's maturing time deposits and borrowings are generally repricing to slightly higher interest rates but this should level out if overnight rates remain low in 2020. The Corporation's average cost of funds was 52 basis points as of September 30, 2019, which is low from an historic perspective and slightly lower than the previous quarter but higher than the previous year. This cost of funds will likely level out for the remainder of 2019. The average cost of funds includes the benefit of non-interest bearing demand deposit accounts. The Corporation's cost of funds was 36 basis points as of December 31, 2018 and 37 basis points as of September 30, 2018.

Deposits had not been very rate sensitive for a number of years as a result of the limited desirable rates available to the deposit customers. However, as market interest rates continued to rise in 2018, customer behavior patterns changed and deposits became more rate sensitive, with a portion leaving the Corporation. The Corporation had experienced a steady growth in both non-interest bearing and interest bearing funds during this last prolonged and historically low interest rate cycle, but in 2018 and through the third quarter of 2019, deposit growth has been slower than in prior years.

The performance of the equity markets also has a bearing on how much of the current deposits will remain at the Corporation. It is management's observation that since the financial crisis, an element of the Corporation's deposit customers has been reluctant to redeploy funds presently at banks back into the equity market. Investors have grown weary of the volatility of the equity markets. Negative events, primarily overseas, have caused multiple cycles of sharp equity declines followed by recoveries. The equity markets performed very well in 2017 and were stabilized after large expected correction. This caused a resurgence of customers pulling funds from deposit accounts to reinvest in the equity markets in 2018. But later in 2018, there had been renewed volatility in the equity market with significant declines in December of 2018 that erased the equity gains realized in earlier 2018. These events are still fresh in the investors' minds. It remains to be seen whether this recent volatility will slow the reaction of deposit customers to higher market interest rates. So far in 2019, the equity markets have had very strong gains, which to date have not adversely impacted the Corporation's deposit levels.

The Corporation's net interest margin is down slightly from levels in the previous quarter. Management's future asset liability decisions will be dependent upon improvements in asset yield as well as the expected timing of further short-term rate increases or decreases. Management expects that the gap ratios will remain within or above the established guidelines throughout the remainder of 2019.

It is important to stress that the gap ratios are a static measurement of the Corporation's asset liability position. It is only one of many asset liability analysis tools management utilizes to measure, monitor, and manage both liquidity and interest rate risk. The deficiencies with the gap analysis are that it makes no provision for changes to the balance sheet out into the future and would not factor in changes that management would very likely make to mitigate future interest rate risk.

In addition to the cumulative maturity gap analysis discussed above, management utilizes a number of liquidity measurements that management believes has advantages over and gives better clarity to the Corporation's present and projected liquidity than the static gap analysis offers.

The Corporation analyzes the following additional liquidity measurements in an effort to monitor and mitigate liquidity risk:

- *Core Deposit Ratio* – Core deposits as a percentage of assets
- *Funding Concentration Analysis* – Alternative funding sources outside of core deposits as a percentage of assets
- *Short-term Funds Availability* – Readily available short-term funds as a percentage of assets
- *Securities Portfolio Liquidity* – Cash flows maturing in one year or less as a percentage of assets and securities
- *Readily Available Unencumbered Securities and Cash* – Unencumbered securities as a percentage of the securities portfolio and as a percentage of total assets
- *Borrowing Limits* – Internal borrowing limits in terms of both FHLB and total borrowings
- *Three, Six, and Twelve-month Projected Sources and Uses of Funds* – Projection of future liquidity positions

These measurements are designed to prevent undue reliance on outside sources of funding and to ensure a steady stream of liquidity is available should events occur that would cause a sudden decrease in deposits or large increase in loans or both, which would in turn draw significantly from the Corporation's available liquidity sources. As of September 30, 2019, the Corporation was within guidelines for all of the above measurements.

Throughout 2018 it was important for the Corporation to be prepared for a continued rates-up environment with more liquidity available so funds could be reinvested in higher yielding assets. Now moving into the latter part of 2019, with three Fed rate declines, it appears there could be a lengthy pause on increasing short-term rates depending on whether the economy will continue growing or slow down. Management had been carrying an average of approximately $30 million to $40 million of cash and cash equivalents on a daily basis throughout most of 2019. Management anticipates carrying similar levels of cash going forward but this will depend on loan growth. With the recent decreases in overnight rates and a shorter securities portfolio, it is more likely management would utilize more of this cash to fund loan growth and run on the lower side of the above range.

The Corporation's liquidity measurements are tracked and reported quarterly by management to both observe trends and ensure the measurements stay within desired ranges. Management is confident that a sufficient amount of internal and external liquidity exists to provide for significant unanticipated liquidity needs.

Interest Rate Risk
Interest rate risk is measured using two analytical tools:

- Changes in net interest income
- Changes in net portfolio value

Financial modeling is used to forecast net interest income and earnings, as well as net portfolio value, also referred to as fair value. The modeling is generally conducted under seven different interest rate scenarios. The scenarios consist of a projection of net interest income if rates remain flat, increase 100, 200, or 300 basis points, or decrease 50, 100, or 150 basis points. Currently, the flat-rate scenario seems more likely for the remainder of 2019 and into 2020, with the Federal funds rate at 2.00% as of September 30, 2019, and 1.75% as of October 30, 2019. The rates-down scenarios are much less likely now with three Federal Reserve rate cuts already established. For that reason, management believes it appropriate to model rates down 50, 100, and 150 basis points to most adequately cover all the reasonably possible declining rate scenarios that the Corporation could face, while continuing to model rates up scenarios of 100, 200, and 300 basis points. While management has more recently turned its focus to rates-down scenarios, with each Federal Reserve rate reduction, the ability to further reduce interest rates diminishes and the exposure to higher interest rates increases. The overnight Federal funds rate and the current U.S. Treasury rates are presently at low historical levels. Because of this historical perspective, if management would take a neutral position in terms of the direction of forward interest rates, there is clearly more long term risk of rates going up than down. So while in the near term it is likely we may see no Federal Reserve rate increases or decreases, management remains guarded about the impact of higher interest rates and continues to prepare for rate increases on a larger scale than decreases.

The results obtained through the use of forecasting models are based on a variety of factors. Both the net interest income and fair value forecasts make use of the maturity and repricing schedules to determine the changes to the balance sheet over the course of time. Additionally, there are many assumptions that factor into the results. These assumptions include, but are not limited to, the following:

- Projected forward interest rates
- Slope of the U.S. Treasury curve
- Spreads available on securities over the U.S. Treasury curve
- Prepayment speeds on loans held and mortgage-backed securities
- Anticipated calls on securities with call options
- Deposit and loan balance fluctuations
- Competitive pressures affecting loan and deposit rates
- Economic conditions
- Consumer reaction to interest rate changes

For the interest rate sensitivity analysis and net portfolio value analysis discussed below, results are based on a static balance sheet reflecting no projected growth from balances as of September 30, 2019. While it is unlikely that the balance sheet will not grow at all, management considers a static analysis to be the most conservative and most accurate means to evaluate fair value and future interest rate risk. The static balance sheet approach is used to reduce the number of variables in calculating the model's accuracy in predicting future net interest income. It is appropriate to pull out various balance sheet growth scenarios which could be utilized to compensate for a declining margin. By testing the model using a base model assuming no growth, this variable is eliminated and management can focus on predicted net interest income based on the current existing balance sheet. Management does run additional scenarios with expected growth rates through the asset liability model to most accurately predict future financial performance. This is done separately and apart from the static balance sheet approach discussed above to test fair value and future interest rate risk.

As a result of the many assumptions, this information should not be relied upon to predict future results. Additionally, both of the analyses discussed below do not consider any action that management could take to minimize or offset the negative effect of changes in interest rates. These tools are used to assist management in identifying possible areas of risk in order to address them before a greater risk is posed. Personnel perform an in-depth annual validation and a quarterly review of the settings and assumptions used in the model to ensure reliability of the forecast results. In addition to the annual validation review, management also engages a third party every three years to obtain a complete external review of the model. That review was completed in the third quarter of 2017. The purpose was to conduct a comprehensive evaluation of the model input, assumptions, and output and this study concluded that the model is managed appropriately and generating acceptable results. Back testing of the model to actual results is performed quarterly to ensure the validity of the assumptions in the model. The internal and external validations as well as the back testing indicate that the model assumptions are reliable.

Changes in Net Interest Income

The change in net interest income measures the amount of net interest income fluctuation that would be experienced over one year, assuming interest rates change immediately and remain the same for one year. This is considered to be a short-term view of interest rate risk. The analysis of changes in net interest income due to changes in interest rates is commonly referred to as interest rate sensitivity. The Corporation's interest rate sensitivity analysis indicates that if interest rates were to go up immediately, the Corporation would realize more net interest income. This is due to the ability of the Corporation to immediately achieve higher interest earnings on interest-earning assets while having the ability to limit the amount of increase in interest-bearing liabilities based on the timing of deposit rate changes. This results in an increase in net interest income in the rising rate scenarios, but a decline in net interest income in the declining rate scenarios.

The third quarter 2019 analysis projects net interest income expected in the seven rate scenarios over a one-year time horizon. As of September 30, 2019, the Corporation was within guidelines for the maximum amount of net interest income change in all rate scenarios. All up-rate scenarios show a positive impact to net interest income. The increase in net interest income in the up-rate scenarios is largely due to the increase in variable rate loans and the recent purchases of variable rate securities and the cash balances held on the Corporation's balance sheet. On the liability side, when interest rates do increase, it is typical for management to react more slowly in increasing deposit rates. Loans that are Prime-based will increase by the full amount of the market rate movement while deposit rates will only increase at a fraction of the market rate increase. Additionally, deposit rates may level off more when market rates increase by 200 or 300 basis points where variable loan rates will still increase by the same amount as the Prime rate. With three interest rates decrease since June 30, 2019, the Corporation would have exposure to all maturing fixed-rate loans and securities, which would reprice lower while most of the Corporation's interest-bearing deposits could not be repriced any lower. This would result in a decline in net interest income in any down-rate scenario. Even in the unlikely down-rate scenarios, the Corporation is within guidelines for the exposure to net interest income changes.

For the rates-up 100 basis point scenario, net interest income increases by 2.2% compared to the rates unchanged scenario. In the remaining rates-up scenarios, the net interest income increases slightly more substantially reflecting the sizable amount of the Corporation's interest-earning assets that reprice immediately by the full amount of the Fed increase versus the limited amount of deposit increases that management would approve on the Corporation's interest-bearing deposits. The higher interest rates go, the greater the likelihood that the proportionality of the Corporation's deposit rate changes decreases as a percentage of the Federal Reserve's action. For the rates-up 200 and 300 basis point scenarios, net interest income increases by 6.0% and 10.7%, respectively, compared to the rates unchanged scenario. Management's maximum permitted net interest income declines by policy are -5%, -10%, and -15%, for the rates-up 100, 200, and 300 basis point scenarios, respectively.

The positive impact of higher rates is primarily due to the favorable impact of all of the Corporation's variable rate loans repricing by the full amount of the Federal rate change, assisted by the Corporation's relatively high interest earning cash balances and that component of the loans and securities portfolios that reprice in less than one year. This more than offsets the increase in interest expense caused by repricing deposits, where they are only repricing by a fraction of the rate change. The Corporation's borrowings do price up faster than deposits, generally equivalent to the U.S. Treasury market. However, borrowings only make up approximately 7.8% of the total funding provided by deposits and borrowings. The more aggressive rates-up scenarios also benefit from known historical experience of deposit rate increases lagging and a slowing in the pace of the actual rate increase as interest rates continue to rise. This allows management the ability to benefit from higher rates by controlling the amount of the increase on large amounts of liabilities that could reprice.

As of September 30, 2019, results in the down 50 basis point scenario show a net interest income decrease of 1.5% compared to the rates unchanged scenario and compared to a policy guideline of -2.5%. In the more aggressive rates-down scenarios of -100 and -150 basis points, net interest income decreases by 5.0% and 6.2%, respectively, compared to policy guidelines of -5.0% and -7.5%. Management does not expect the Corporation's exposure to interest rate changes to increase or change significantly during the remainder of 2019.

The assumptions and analysis of interest rate risk are based on historical experience during varied economic cycles. Management believes these assumptions to be appropriate; however, actual results could vary significantly. Management uses this analysis to identify trends in interest rate sensitivity and determine if action is necessary to mitigate asset liability risk.

Changes in Net Portfolio Value

The change in net portfolio value is considered a tool to measure long-term interest rate risk. The analysis measures the exposure of the balance sheet to valuation changes due to changes in interest rates. The calculation of net portfolio value discounts future cash flows to the present value based on current market rates. The change in net portfolio value estimates the gain or loss in value that would occur on market sensitive instruments given an interest rate increase or decrease in the same seven scenarios mentioned above. As of September 30, 2019, the Corporation was within guidelines for all rate scenarios. The trend over the past year has been lessening risk in the rising rate scenarios with increasing cash balances and core deposit balances with the current quarter showing an even larger benefit in all rising rate scenarios than the quarter ended June 30, 2019. The strong gap ratios played a large role in improving the Corporation’s net portfolio value profile. The non-interest bearing demand deposit accounts and low-interest bearing checking, NOW, and money market accounts provide more benefit to the Corporation when interest rates are higher and the difference between the overnight funding costs compared to the average interest bearing core deposit rates are greater. As interest rates increase, the discount rate used to value the Corporation’s interest bearing accounts increases, causing a lower net present value for these interest-bearing deposits. This improves the modeling of the Corporation’s fair value risk to higher interest rates as the liability amounts decrease causing a higher net portfolio value of the Corporation’s balance sheet. However, as interest rates decrease, the discount rate used to value the Corporation’s interest bearing accounts decreases, causing a higher net present value for these interest-bearing deposits.

The results as of September 30, 2019, indicate that the Corporation’s net portfolio value would experience valuation gains of 21.3%, 33.1%, and 38.5% in the rates-up 100, 200, and 300 basis point scenarios. Management’s maximum permitted declines in net portfolio value by policy are -5% for rates-up 100 basis points, graduating up to -15% for rates-up 300 basis points. A valuation loss would indicate that the value of the Corporation’s assets is declining at a faster pace than the decrease in the value of the Corporation’s liabilities. The analysis does show a valuation loss in the down 50, 100, and 150 basis point scenarios of -7.5%, -12.0%, and -12.9%, respectively, compared to policy guidelines of -7.5%, -15.0%, and -22.5%. The Corporation’s expected valuation loss was within guideline for all scenarios. With rates decreasing by 25 basis points each in July and September, and with an additional fourth quarter Fed rate action, the exposure to valuation changes could change going forward if the behavior of the Corporation’s deposits changes due to lower interest rates. Based on five past decay rate studies on the Corporation’s core deposits, management does not expect a material decline in core deposit accounts, including the non-interest bearing accounts, as short term interest rates decrease. Up to this point, the Corporation’s core deposits have been stable through a number of rate cycles.

The weakness with the net portfolio value analysis is that it assumes liquidation of the Corporation rather than as a going concern. For that reason, it is considered a secondary measurement of interest rate risk to “Changes in Net Interest Income” discussed above. However, the net portfolio value analysis is a more important tool to measure the impact of interest rate changes to capital. In the current regulatory climate, the focus is on ensuring adequate asset liability modeling is being done to project the impact of very large interest rate increases on capital. The asset liability modeling currently in place measures the impact of such a rate change on the valuation of the Corporation’s loans, securities, deposits, and borrowings, and the resulting impact to capital. Management continues to analyze additional scenario testing to model “worst case” scenarios to adequately plan for the possible severe impact of such events.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures.

Management carried out an evaluation, under the supervision and with the participation of the Chief Executive Officer and Treasurer (Principal Financial Officer), of the effectiveness of the design and the operation of the Corporation's disclosure controls and procedures (as such term as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of September 30, 2019, pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Chief Executive Officer along with the Treasurer (Principal Financial Officer) concluded that the Corporation's disclosure controls and procedures as of September 30, 2019, are effective to ensure that information required to be disclosed in the reports that the company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission.

(b) Changes in Internal Controls.

There have been no changes in the Corporation's internal controls over financial reporting that occurred during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

PART II – OTHER INFORMATION
September 30, 2019

Item 1. Legal Proceedings

Management is not aware of any litigation that would have a material adverse effect on the consolidated financial position or results of operations of the Corporation or its subsidiaries taken as a whole. There are no proceedings pending other than ordinary routine litigation incident to the business of the Corporation. In addition, no material proceedings are pending, are known to be threatened, or contemplated against the Corporation by governmental authorities.

Item 1A. Risk Factors

The Corporation continually monitors the risks related to the Corporation's business, other events, the Corporation's Common Stock, and the Corporation's industry. Management has not identified any new risk factors since the December 31, 2018 Form 10-K filing.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Purchases

The following table details the Corporation's purchase of its own common stock during the three months ended September 30, 2019.

Issuer Purchase of Equity Securites

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans *	Maximum Number of Shares that May Yet be Purchased Under the Plan *
July 2019	**5,000**	**19.41**	**5,000**	**184,434**
August 2019	**6,000**	**19.53**	**6,000**	**178,434**
September 2019	**11,400**	**19.94**	**11,400**	**167,034**
Total	**22,400**			

* On February 20, 2019, the Board of Directors of the Corporation approved a plan to repurchase, in the open market and privately renegotiated transactions, up to 100,000 shares of its outstanding common stock. This plan replaces the 2015 plan. The first purchase of common stock under this plan occurred on May 13, 2019. By September 30, 2019, a total of 32,966 shares were repurchased at a total cost of $661,000, for an average cost per share of $20.05. The total number of shares authorized to be repurchased under the plan was increased to 200,000 pursuant to the 2-for-1 stock split, which became effective on June 28, 2019.

Item 3. Defaults Upon Senior Securities – Nothing to Report

Item 4. Mine Safety Disclosures – Not Applicable

Item 5. Other Information – Nothing to Report

Item 6. Exhibits:

Exhibit No.	Description
3(i)	Articles of Incorporation of the Registrant, as amended (Incorporated by reference to Exhibit 3.1 of the Corporation's Form 8-K filed with the SEC on June 7, 2019)
3 (ii)	By-Laws of the Registrant, as amended. (Incorporated herein by reference to Exhibit 3.2 of the Corporation's Form 8-K filed with the SEC on January 15, 2010.)
10.1	Form of Deferred Income Agreement. (Incorporated herein by reference to Exhibit 10.1 of the Corporation's Quarterly Report on Form 10-Q filed with the SEC on August 13, 2008.)
10.2	2011 Employee Stock Purchase Plan (Incorporated herein by reference to Exhibit 10.2 of the Corporation's Annual Report on Form 10-K for the year ended December 31, 2011, filed with the SEC on March 29, 2012.)
10.3	2010 Non-Employee Directors' Stock Plan. (Incorporated herein by reference to Exhibit 10 of the Corporation's Form S-8 filed with the SEC on June 4, 2010.)
31.1	Section 302 Chief Executive Officer Certification (Required by Rule 13a-14(a)).
31.2	Section 302 Principal Financial Officer Certification (Required by Rule 13a-14(a)).
32.1	Section 1350 Chief Executive Officer Certification (Required by Rule 13a-14(b)).
32.2	Section 1350 Principal Financial Officer Certification (Required by Rule 13a-14(b)).

SIGNATURES

Pursuant to the requirements of Section 13 or 15 (d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ENB Financial Corp
(Registrant)

Dated: November 14, 2019	By:	/s/ Aaron L. Groff, Jr. **Aaron L. Groff, Jr.** **Chairman of the Board,** **Chief Executive Officer and President**
Dated: November 14, 2019	By:	/s/ Scott E. Lied **Scott E. Lied, CPA** **Treasurer** **Principal Financial Officer**

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Section 2: EX-31.1 (EX-31.1)

ENB FINANCIAL CORP

Exhibit 31.1

CERTIFICATION

I, **Aaron L. Groff, Jr.**, certify that:

1. I have reviewed this quarterly report on Form 10-Q of **ENB Financial Corp**;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies, and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2019

By: /s/ Aaron L. Groff, Jr.
Aaron L. Groff, Jr.
Chairman of the Board,
Chief Executive Officer and President

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Section 3: EX-31.2 (EX-31.2)

ENB FINANCIAL CORP

Exhibit 31.2

CERTIFICATION

I, **Scott E. Lied**, certify that:

1. I have reviewed this quarterly report on Form 10-Q of **ENB Financial Corp**;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies, and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date:	November 14, 2019	By:	/s/ Scott E. Lied **Scott E. Lied, CPA** **Treasurer** **Principal Financial Officer**

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Section 4: EX-32.1 (EX-32.1)

ENB FINANCIAL CORP

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADDED BY
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of ENB Financial Corp (the "Corporation") for the period ended September 30, 2019, as filed with the Securities and Exchange Commission (the "Report"), I, Aaron L. Groff, Jr., Chairman of the Board, Chief Executive Officer and President, of the Corporation, certify, pursuant to 18 U.S.C. Section 1350, as added by Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. To my knowledge, the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Corporation as of and for the period covered by the Report.

Date:	November 14, 2019	By:	/s/ Aaron L. Groff, Jr. **Aaron L. Groff, Jr.** **Chairman of the Board,** **Chief Executive Officer and President**

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Section 5: EX-32.2 (EX-32.2)

ENB FINANCIAL CORP

Exhibit 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADDED BY
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of ENB Financial Corp (the "Corporation") for the period ended September 30, 2019, as filed with the Securities and Exchange Commission (the "Report"), I, Scott E. Lied, Treasurer of the Corporation, certify, pursuant to 18 U.S.C. Section 1350, as added by Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. To my knowledge, the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Corporation as of and for the period covered by the Report.

Date: November 14, 2019	By:	/s/ Scott E. Lied **Scott E. Lied, CPA** **Treasurer** **Principal Financial Officer**

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