2017

ANNUAL REPORT

First Bancshares, Inc.
Bellevue, Ohio

First National Bank

"Your Bank of a Lifetime"

First Bancshares, Inc.

Bellevue, Ohio

First Bancshares, Inc. is a one-bank holding company. Its principal subsidiary, First National Bank, is a full-service bank with offices in Bellevue, Catawba, Clyde, Fremont, Port Clinton, Put-in-Bay and Sandusky, Ohio.

The Annual Meeting
of Shareholders of
First Bancshares, Inc.
will be held
Wednesday, April 25, 2018
2:00 P.M.
at
First National Bank
120 North Street
Bellevue, Ohio

First Bancshares, Inc. ~ ~ A Great Investment

Dividend Reinvestment Program

This program was adopted in 2012 to allow First Bancshares, Inc. investors the opportunity to direct their dividend payments each quarter to purchase additional shares.

The program is available to all shareholders with open enrollment at any time.

First Bancshares, Inc.
Dividend History

Holding Company Stock Issued - 5/31/1983

	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
4th Quarter	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.40	$0.40	$0.40	$0.40	$0.40	$0.50
Stock Split: 2-for-1, effective 5/31/83												
1st Quarter	0.00	0.625	0.70	0.75	0.75	0.75	0.40	0.40	0.40	0.40	0.40	0.50
2nd Quarter	0.525	0.00	0.00	0.00	0.00	0.40	0.45	0.45	0.45	0.50	0.60	0.60
3rd Quarter	0.525	0.625	0.75	0.80	0.85	0.45	0.45	0.45	0.55	0.65	0.75	0.60
Subtotal	**$1.05**	**$1.25**	**$1.45**	**$1.55**	**$1.60**	**$1.60**	**$1.70**	**$1.70**	**$1.80**	**$1.95**	**$2.15**	**$2.20**
Extra Dividend	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Total Cash Dividend	**$1.05**	**$1.25**	**$1.45**	**$1.55**	**$1.60**	**$1.60**	**$1.70**	**$1.70**	**$1.80**	**$1.95**	**$2.15**	**$2.20**

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
4th Quarter	$0.55	$0.60	$0.65	$0.70	$0.75	$0.55	$0.55	$0.60	$0.60	$0.60	$0.70	$0.70
					Stock Split: 2-for-1, effective 2/1/99							
1st Quarter	0.55	0.60	0.65	0.70	0.40	0.55	0.60	0.60	0.60	0.60	0.70	0.70
2nd Quarter	0.55	0.60	0.65	0.70	0.40	0.55	0.60	0.60	0.60	0.60	0.70	0.50
3rd Quarter	0.55	0.60	0.65	0.70	0.40	0.55	0.60	0.60	0.60	0.60	0.70	0.50
Subtotal	**$2.20**	**$2.40**	**$2.60**	**$2.80**	**$1.95**	**$2.20**	**$2.35**	**$2.40**	**$2.40**	**$2.40**	**$2.80**	**$2.40**
Extra Dividend	0.10	0.25	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.30	0.20	0.00
Total Cash Dividend	**$2.30**	**$2.65**	**$2.80**	**$3.00**	**$2.15**	**$2.40**	**$2.55**	**$2.60**	**$2.60**	**$2.70**	**$3.00**	**$2.40**
(Split-Adjusted)					**$3.55**							

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
4th Quarter	$0.50	$0.50	$0.50	$0.30	$0.30	$0.30	$0.40	$0.45	$0.17	$0.18	$0.20
								Stock Split: 3-for-1, effective 12/29/14			
1st Quarter	0.50	0.50	0.50	0.30	0.15	0.35	0.40	0.45	0.17	0.18	0.20
2nd Quarter	0.50	0.50	0.30	0.30	0.15	0.35	0.40	0.45	0.17	0.18	0.22
3rd Quarter	0.50	0.50	0.30	0.30	0.20	0.35	0.45	0.50	0.17	0.18	0.22
Subtotal	**$2.00**	**$2.00**	**$1.60**	**$1.20**	**$0.80**	**$1.35**	**$1.65**	**$1.85**	**$0.68**	**$0.72**	**$0.84**
Extra Dividend	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Total Cash Dividend	**$2.00**	**$2.00**	**$1.60**	**$1.20**	**$0.80**	**$1.35**	**$1.65**	**$1.85**	**$0.68**	**$0.72**	**$0.84**

Message to Shareholders

February 19, 2018

Dear Shareholder;

As this is being written, we are toward the end of a cold and snowy winter. The temperatures in January and February were quite frigid in northern Ohio and the ground has generally been covered in snow most of the winter. We look forward to spring and hope by the time you receive the annual report our snow is long gone. While the weather for the first part of 2018 has been a little harsh, we are happy to report that 2017 was a good year financially for the company. Net income after tax was down from the prior year but pretax income was up over $243,000. The tax code change that occurred just prior to the end of the year resulted in us having to take an adjustment to our tax deferred assets and liabilities. While it's a little difficult to explain in the content of this narrative, in essence, the lower tax rates affected the value of these items on our balance sheet and the net effect is reported through our income tax payable. That total was roughly $393,000. The positive factor is that the lower tax rate in effect for this and future years will allow us to recover that adjustment in 2018 with future years benefitting fully from the new tax rates. We covered many highlights in the January dividend letter and the annual report contains all of the financial data and host of other required schedules outlining much more detail.

The economy tends to be top of mind as interest rates start to increase at a steady clip and the Federal Reserve is broadcasting the expectation of three to four rate hikes in 2018. With an unemployment rate that is close to full employment and potential pressure on wages, the Federal Reserve is keeping close watch to make sure the economy does not heat up too fast. We are seeing signs of a strengthening economy and business expansion taking place in our market area. We expect this to help boost loan demand and fuel some additional growth for First National Bank.

Our new office in Fremont opened on June 1st and has been well received in the community. Our business development officers have been active in that market and we are seeing the effects of those efforts come to fruition. Our overall marketing efforts are being ramped up with new initiatives to tell our story of delivering high quality customer service in a highly competitive environment. We continue to invest in our staff with ongoing training, competitive wages and a strong benefit package that is a leader in our market. The bank is in very good position to take advantage of a solid economy, lower tax rates and expanding business base. We believe this should translate into another strong year of financial performance which will help to drive the return on your investment in our company.

The annual meeting information is at the beginning of the annual report and we welcome all of our shareholders to attend. We are grateful for your support of the company and will continue to work hard to maintain that trust.

Sincerely,

Steven L. Mays, DVM
Chairman of the Board

Dean J. Miller
President and CEO

DIXON, DAVIS, BAGENT & COMPANY
CERTIFIED PUBLIC ACCOUNTANTS
1205 WEAVER DRIVE • GRANVILLE, OHIO 43023 • 740-321-1000 • FAX 740-321-1100

INDEPENDENT AUDITOR'S REPORT

The Audit Committee of the Board of Directors
First Bancshares, Inc.
Bellevue, Ohio

We have audited the accompanying consolidated financial statements of First Bancshares, Inc., which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of income, changes in equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

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

Dixon, Davis, Bagent & Co.

Dixon, Davis, Bagent & Company
Granville, Ohio
February 19, 2018

Consolidated Balance Sheet

	December 31, 2017	December 31, 2016
Assets		
Cash and due from banks (Note 2)	$ 5,714,540	$ 5,685,709
Federal funds sold	-	-
Interest-bearing deposits in banks	-	-
Total cash and cash equivalents	5,714,540	5,685,709
Investment securities – Available for sale (Note 3)	20,536,598	25,418,397
Investment securities – Held to maturity (Note 3)	1,654,795	2,652,532
Other securities (Note 3)	1,223,617	862,792
Loans – Net of allowance for loan losses of $1,972,106 and $1,984,349 in 2017 and 2016, respectively (Note 4)	169,437,721	157,596,167
Foreclosed assets	99,997	92,997
Premises and equipment (Note 5)	4,515,665	4,087,337
Accrued interest receivable	778,392	733,219
Cash surrender value of life insurance	4,431,917	3,363,828
Other assets (Note 12)	1,254,174	1,516,090
Total assets	$ 209,647,416	$ 202,009,068
Liabilities and Stockholders' Equity		
Liabilities		
Deposits (Note 6)		
Noninterest-bearing	$ 33,351,542	$ 36,151,748
Interest-bearing	146,466,156	131,819,568
Total deposits	179,817,698	167,971,316
Federal Home Loan Bank advances (Note 7)	4,244,915	9,300,908
Bank line of credit (Note 8)	3,699,073	3,699,073
Federal funds purchased	2,288,000	2,462,604
Accrued interest payable	33,856	22,676
Accrued and other liabilities	1,772,562	1,864,863
Total liabilities	191,856,104	185,321,440
Stockholders' Equity		
Preferred stock – no par value; authorized 750,000 shares; 0 shares issued and outstanding	-	-
Common stock - $5.00 par value; authorized 750,000 shares; issued and outstanding 660,600 shares	1,101,000	1,101,000
Treasury stock – At cost; 91,259 and 91,119 shares at December 31, 2017 and 2016, respectively	(1,395,520)	(1,392,474)
Additional paid-in capital	1,107,431	1,104,093
Retained earnings	16,946,460	15,814,502
Accumulated other comprehensive income	31,941	60,507
Total stockholders' equity	17,791,312	16,687,628
Total liabilities and stockholders' equity	$ 209,647,416	$ 202,009,068

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

First Bancshares, Inc.
Bellevue, Ohio

Consolidated Statement of Operations

	Year Ended December 31, 2017	Year Ended December 31, 2016
Interest Income		
Loans – including fees	$ 8,496,412	$ 7,861,233
Debt securities:		
Taxable	342,211	414,893
Tax-exempt	228,281	278,722
Other	158,648	136,650
Total interest income	9,225,552	8,691,498
Interest Expense		
Deposits	744,804	497,662
Borrowings	248,353	168,285
Total interest expense	993,157	665,947
Net Interest Income	8,232,395	8,025,551
Provision for Loan Losses (Note 4)	53,500	(338,474)
Net Interest Income After Provision for Loan Losses	8,178,895	8,364,025
Noninterest Income		
Service charges – Deposits	455,935	367,808
Net gain on sale of loans	136,671	122,447
Writedown of other real estate owned	-	(142,046)
Rental fees and commissions	20,800	22,400
Gain on sale of investment securities	9,990	(8,461)
Visa interchange fees	192,258	164,119
Other	476,530	340,137
Other real estate operation income	-	26,607
Total noninterest income	1,292,184	893,011
Noninterest Expenses		
Salaries and employee benefits (Note 11)	3,930,555	3,718,404
Occupancy and equipment	654,142	610,656
Data processing	605,149	559,971
Other real estate owned operating expense	-	87,047
State tax	136,596	138,168
Professional fees	144,254	234,016
FDIC insurance	56,687	103,531
Advertising	38,844	37,205
Director fees	103,800	103,400
Other	970,994	1,081,726
Total noninterest expenses	6,641,021	6,674,124
Income – Before income taxes	2,830,058	2,582,912
Income Tax Expense (Note 12)	1,214,560	731,204
Net Income	$ 1,615,498	$ 1,851,708

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

Consolidated Statement of Comprehensive Income

	2017	2016
Net income	$ 1,615,498	$ 1,851,708
Other comprehensive income (loss), net of tax:		
Unrealized net holding gain (loss) on securities available-for-sale, net of income taxes of $(52,098) and $(147,987) for the years ended December 31, 2017 and 2016, respectively	(64,412)	(295,730)
Reclassification adjustment for gains realized, net of income taxes of $12,188 and $2,877 for the years ended December 31, 2017 and 2016, respectively	35,846	8,461
Other comprehensive income (loss)	(28,566)	(287,269)
Comprehensive income (loss)	$ 1,586,932	$ 1,564,439

Consolidated Statement of Changes in Stockholders' Equity

	Preferred Stock	Common Stock	Treasury Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balance – December 31, 2015	$ -	$ 1,101,000	$(1,390,694)	$ 1,090,893	$ 14,372,835	$ 347,776	$ 15,521,810
Comprehensive income:							
Net income	-	-	-	-	1,851,708	-	1,851,708
Change in net unrealized gain on securities – Net of tax of $(147,987)	-	-	-	-	-	(287,269)	(287,269)
Total comprehensive Income	-	-	-	-	-	-	1,564,439
Purchase of treasury stock	-	-	(1,780)	13,200	-	-	11,420
Dividends declared $0.72 per share	-	-	-	-	(410,041)	-	(410,041)
Balance – December 31, 2016	-	$ 1,101,000	$(1,392,474)	$ 1,104,093	$ 15,814,502	$ 60,507	$ 16,687,628
Comprehensive income:							
Net income	-	-	-	-	1,615,498	-	1,615,498
Change in net unrealized gain on securities – Net of tax of $(52,098)	-	-	-	-	-	(28,566)	(28,566)
Total comprehensive Income	-	-	-	-	-	-	1,586,932
Purchase of treasury stock	-	-	(3,046)	3.338	-	-	292
Dividends declared $0.84 per share	-	-	-	-	(483,540)	-	(483,540)
Balance – December 31, 2017	$ -	$ 1,101,000	$(1,395,520)	$ 1,107,431	$ 16,946,460	$ 31,941	$ 17,791,312

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

First Bancshares, Inc.
Bellevue, Ohio

Consolidated Statement of Cash Flows

	Year Ended December 31, 2017	2016
Cash Flows from Operating Activities		
Net Income	$ 1,615,498	$ 1,851,708
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation expense	290,111	273,354
Provision for loan losses	53,500	(338,474)
Accretion and amortization of securities	292,274	359,493
Gain on sale of investments	(35,846)	(8,461)
Deferred income taxes	(46,117)	514,599
Increase in cash surrender value of life insurance	(1,068,088)	125,096
Stock based compensation	3,338	13,200
Impairment of other real estate owned	-	142,046
Net change in:		
Accrued interest receivable and other assets	248,037	130,421
Accrued interest payable and other liabilities	(35,000)	253,092
Net cash provided by operating activities	1,317,707	3,316,074
Cash Flows from Investing Activities		
Activity in available-for-sale securities:		
Proceeds from sale	3,780,888	1,644,133
Maturities, prepayments, and calls	2,896,502	4,248,998
Purchases	(2,111,875)	(8,852,871)
Activity in held-to-maturities securities:		
Purchases	-	(504,452)
Payments on held-to-maturity securities	997,736	-
Purchase of Federal Reserve Bank stock	(30,400)	(57,600)
Purchase of FHLB and UBB stock	(330,425)	-
Net change in loans	(11,895,054)	(18,545,193)
Proceeds from sale of foreclosed assets	-	1,006,653
Additions to foreclosed real estate	(7,000)	(92,997)
Additions to premises and equipment	(718,440)	(553,556)
Net cash used in investing activities	(7,418,068)	(21,706,885)
Cash Flows from Financing Activities		
Net change in deposits	11,846,384	9,507,635
Payments on Federal Home Loan Bank advances	(5,055,993)	(2,063,723)
Payments on note payable	-	-
Increase in note payable	-	650,000
Change in short-term borrowed funds	(174,604)	9,493,604
Purchase of treasury stock	(3,046)	(1,780)
Dividends paid	(483,549)	(410,041)
Net cash provided by (used in) financing activities	6,129,192	17,175,695
Net Increase (Decrease) in Cash and Cash Equivalents	28,831	(1,215,117)
Cash and Cash Equivalents – Beginning of year	5,685,709	6,900,826
Cash and Cash Equivalents – End of year	$ 5,714,540	$ 5,685,709
Supplemental Cash Flow Information		
Cash paid for:		
Interest	$ 981,977	$ 663,784
Income taxes	730,000	304,286
Loans transferred to other real estate	59,000	92,997

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

Note 1 – Nature of Business and Significant Accounting Policies

Basis of Presentation and Consolidation – The consolidated financial statements include the accounts of First Bancshares, Inc. (the "Corporation") and its wholly owned subsidiaries, First National Bank (the "Bank") and First Bellevue Properties, Inc. All significant intercompany balances and transactions have been eliminated in consolidation.

Nature of Operations – The Bank provides a full range of financial services to individuals and corporate customers in the Ohio counties of Huron, Sandusky, Erie, Ottawa, and Seneca. First Bellevue Properties, Inc. is used for property management.

Use of Estimates – In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of investment securities, and deferred tax assets.

Cash and Cash Equivalents – For the purpose of the consolidated statement of cash flows, cash and cash equivalents include cash and balances due from banks, federal funds sold, and interest-bearing deposits in banks which mature within 90 days.

Securities – Debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and recorded at amortized cost. Securities not classified as held to maturity, including equity securities with readily determinable fair values, are classified as "available for sale" and are recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Loans and Allowance for Loan Losses – Loans are carried at the amount of unpaid principal, adjusted for deferred loan fees and origination costs. Interest on loans is accrued based on the principal amounts outstanding. Nonrefundable loan fees and related direct costs are deferred and the net amount is amortized to income as a yield adjustment over the life of the loan using the interest method. When principal or interest is delinquent for ninety days or more, the bank evaluates the loan for nonaccrual status.

After a loan is placed on nonaccrual status, all interest previously accrued but not collected is reversed against current period interest income. Subsequent collections of interest payments on nonaccrual loans are recognized as interest income unless ultimate collectability of the loan is in doubt. Cash collections on loans where ultimate collectability remains in doubt are applied as reductions of the loan principal balance and no interest income is recognized until the principal balance has been collected.

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. The allowance is based on two basic principles of accounting (i) FASB ASC 450, *Contingencies,* which requires that losses be accrued when they are probable of occurring and estimable and (ii) FASB ASC 310, *Receivables,* which requires that losses on impaired loans be accrued based on the differences between the loan balance and either the value of collateral, if such loans are considered to be collateral dependent and in the process of collection, or the present value of future cash flows, or the loan's value as observable in the secondary market. A loan is considered impaired when, based on current information and events, the bank has concerns about the ability to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfall generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and

Note 1 – Nature of Business and Significant Accounting Policies (Continued)

borrower, including the length of the day, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

The bank's allowance for loan losses has three basic components: the specific allowance, the formula allowance and the pooled allowance. Each of these components is determined based upon estimates that can and do change when the actual events occur. As a result of the uncertainties inherent in the estimation process, management's estimate of loan losses and the related allowance could change in the near term.

The specific allowance component is used to individually establish an allowance for loans identified for impairment testing. When impairment is identified, a specific reserve may be established based on the bank's calculation of the estimated loss embedded in the individual loan. Impairment testing includes consideration of the borrower's overall financial condition, resources and payment record, support available from financial guarantors and the fair market value of collateral. These factors are combined to estimate the probability and severity of inherent losses. Large groups of smaller balance, homogeneous loans are collectively evaluated for impairment. Accordingly, the bank does not separately evaluate individual consumer and residential loans for impairment.

The formula allowance component is used for estimating the loss on internally risk rated loans exclusive of those identified as impaired. The loans meeting the bank's internal criteria for classification, such as special mention, substandard, doubtful and loss, as well as specifically identified impaired loans, are segregated from performing loans within the portfolio. These internally classified loans are then grouped by loan type (commercial, commercial real estate, commercial construction, residential real estate, residential construction or installment). Each loan type is assigned an allowance factor based on management's estimate of the associated risk, complexity and size of the individual loans within the particular loan category. Classified loans are assigned a higher allowance factor than non-classified loans due to management's concerns regarding collectability or management's knowledge of particular elements surrounding the borrower. Allowance factors increase with the worsening of the internal risk rating.

The pooled formula component is used to estimate the losses inherent in the pools of non-classified loans.

These loans are then also segregated by loan type and allowance factors are assigned by management based on delinquencies, loss history, trends in volume and terms of loans, effects of changes in lending policy, the experience and depth of management, national and local economic trends, concentrations of credit, results of the loan review system and the effect of external factors (i.e. competition and regulatory requirements).

Allowance factors and overall size of the allowance may change from period to period based on management's assessment of the above-described factors and the relative weights given to each factor in addition, various regulatory agencies periodically review the allowance for loan losses. These agencies may require the bank to make additions to the allowance for loan losses based on their judgments of collectability based on information available to them at the time of their examination.

Loans are placed into a nonaccruing status and classified as nonperforming when the principal or interest has been in default for a period of 90 days or more unless the obligation is well secured and in the process of collection. A debt is "well secured" if it is secured by (i) pledges of real or personal property, including securities, that have a realizable value sufficient to discharge the debt, (including accrued interest), in full, or (ii) the guarantee of a financially responsible party. A debt is "in process of collection" if collection on the debt is proceeding in due course either through legal action, including judgment enforcement procedure, or, in appropriate circumstances, through collection efforts not involving legal action which are reasonably expected to result in repayment of the debt or in its restoration to a current status.

Loans classified as substandard or worse are considered for impairment testing. A substandard loan shows signs of continuing negative financial trends and unprofitability and therefore, is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. The borrower on such loans typically exhibits one or more of the following characteristics: financial ratios and profitability margins are well below industry average; a negative cash flow position exists; debt service capacity is insufficient to the service debt and an improvement in the cash flow position is unlikely within the next twelve months; secondary and tertiary means of debt repayment are weak. Loans classified as substandard are characterized by the probability that the bank will not collect amounts due according to the contractual terms or sustain some loss if the deficiencies are not corrected.

Loss potential, while existing with respect to the aggregate amount of substandard (or worse) loans, does not have to exist in any individual assets classified as substandard. Such credits are also evaluated for nonaccrual status.

Note 1 – Nature of Business and Significant Accounting Policies (Continued)

Impaired loans include loans that have been classified as substandard or worse. However, certain loans have been paying as agreed and have remained current, with some financial issues related to cash flow that have caused some concern as to the ability of the borrower to perform in accordance with the current loan terms but not to such an extent as to require the loan be put in a nonaccruing status. Cash receipts on impaired loans are recorded as interest income as received, unless the loan is in a nonaccrual status.

The bank's charge-off policy states after all collection efforts have been exhausted and the loan is deemed to be a loss, it will be charged to the bank's established allowance for loan losses. Consumer loans subject to the Uniform Retail Credit Classification are charged-off as follows: (a) closed end loans are charged-off no later than 120 days after becoming delinquent, (b) consumer loans to borrowers who subsequently declare bankruptcy, where the bank is an unsecured creditor, are charged-off within 60 days of receipt of the notification from the bankruptcy court, (c) fraudulent loans are charged-off within 90 days of discovery and (d) death of a borrower will cause a charge-off to be incurred at such time an actual loss is determined. All other types of loans are generally evaluated for loss potential at the 90th day past due threshold, and any loss is recognized no later than the 120th day past due threshold; each loss is evaluated on its specific facts regarding the appropriate timing to recognize the loss.

Troubled Debt Restructuring (TDRs) – Management classified loans as TDRs when a borrower is experiencing financial difficulties and the Corporation has granted a concession. In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Corporation internal underwriting policy. Management's policy is to modify loans by extending the term or by granting a temporary or permanent contractual interest rate below the market rate, not by forgiving debt. TDRs are separately identified for impairment disclosures and are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral.

Off-balance-sheet Instruments – In the ordinary course of business, the Corporation has entered into commitments under commercial letters of credit and standby letters of credit. Such financial instruments are recorded when they are funded.

Servicing – Servicing assets are recognized as separate assets when rights are acquired through sale of financial assets. Capitalized servicing rights are reported in other assets and are amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights by predominant characteristics, such as interest rates and terms. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. Impairment is recognized through a valuation allowance for an individual stratum, to the extent that fair value is less than the capitalized amount for the stratum.

Loans serviced for others are not included in the accompanying consolidated balance sheet. The unpaid principal balances of mortgage loans serviced for others were $68.7 million and $66.0 million at December 31, 2017 and 2016, respectively. The related mortgage servicing rights, included in other assets, were $615,065 and $514,494 at December 31, 2017 and 2016, respectively. At December 31, 2017 and 2016, the book value of the servicing rights approximated fair value and no valuation allowances were required.

Foreclosed Assets – Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value at the date of the foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets.

Premises and Equipment – Land is carried at cost. Buildings and equipment are carried at cost, less accumulated depreciation computed on the straight-line method over the estimated useful lives of the assets.

Bank-owned Life Insurance – The Bank has purchased life insurance policies on certain key officers. Bank-owned life insurance is recorded at its cash surrender value, or the amount that can be realized.

Postretirement Benefits – The Corporation has endorsement split-dollar life insurance policies and agreements with individuals to provide a benefit extending to postretirement periods. The liability in connection with these agreements was recorded effective January 1, 2008 as a decrease in retained earnings of $161,060 when the accounting treatment

Note 1 – Nature of Business and Significant Accounting Policies (Continued)

for such agreements changed. At December 31, 2017 and 2016, the Corporation had a liability of $200,639 and $195,040, respectively, in connection with these benefits.

Stock Based Compensation – Compensation cost is recognized for stock options and stock awards issued to employees based on the fair value of these awards at the date of the grant. Fair value of the stock options is determined by the mean between the lowest bid and highest bid asked prices on the grant date. Compensation cost is recognized over the required service period, generally defined as the vesting period. At December 31, 2017, common stock committed to be issued was 315 shares.

Treasury Stock – Treasury stock is stated at cost. Cost is determined by the average cost method.

Income Taxes - Income taxes are provided for the tax effects reported in the financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the basis of available-for-sale securities, allowance for loan losses, accumulated depreciation, and accrued employee benefits. The deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred tax assets and liabilities are reflected at income tax rates applicable to the period in which the deferred tax assets and liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. The Bancorp files consolidated income tax returns with its subsidiary on a calendar year basis.

Fair Value Measurements - The Bancorp follows the guidance of FASB ASC 825, *Financial Instruments*, and FASB ASC 820, *Fair Value Measurement*. This guidance permits entities to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This guidance clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. Under this guidance, fair value measurements are not adjusted for transaction costs. This guidance establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

Comprehensive Income – Accounting principles generally require that recognized revenue, expenses, gains, and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the consolidated balance sheet; such items, along with net income, are components of comprehensive income.

The components of other comprehensive income and related tax effects are as follows:

	2017	2016
Net income	$1,615,498	$1,851,708
Other comprehensive income		
Unrealized holding gains (losses) on available-for-sale Securities	(116,510)	(443,717)
Reclassification adjustment for gains on sale recognized in income	35,846	8,461
Net unrealized gains (losses)	(80,664)	(435,256)
Tax effect	52,098	147,987
Other comprehensive income	$1,586,932	$1,564,439

Reclassification – Certain amounts appearing in the prior year's financial statements have been classified to conform to the current year's financial statements.

Note 1 – Nature of Business and Significant Accounting Policies (Continued)

Subsequent Events – The consolidated financial statements and related disclosures include evaluation of events up through and including February 19, 2018, which is the date the consolidated financial statements were available to be issued.

Note 2 – Restriction on Cash and Amounts Due from Banks

The Bank is required to maintain average balances on hand or with the Federal Reserve Bank. At December 31, 2017 and 2016, these reserve balances amounted to $471,000 and $596,000, respectively.

Note 3 – Securities

The amortized cost and fair value of securities, with gross unrealized gains and losses, are as follows:

	2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Available-for-sale securities:				
U.S. government and federal agency	$ 2,693,867	$ 22,622	$ (28,204)	$ 2,688,285
Mortgage backed	9,881,950	2,433	(191,737)	9,692,646
State and municipal	7,472,349	22,490	(71,787)	7,423,052
Preferred stock	448,000	284,614	-	732,614
Total available-for-sale securities	$20,496,166	$ 332,159	$(291,728)	$20,536,597
Held-to-maturity securities:				
Tax-exempt bonds	$ 1,654,795	$ 126,996	$ (3,417)	$ 1,778,374
Total held-to-maturity securities	$ 1,654,795	$ 126,996	$ (3,417)	$ 1,778,374

	2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Available-for-sale securities:				
U.S. government and federal agency	$ 3,628,442	$ 15,732	$ (57,312)	$ 3,586,862
Mortgage backed	12,213,137	34,192	(191,752)	12,055,577
State and municipal	9,037,141	42,015	(146,912)	8,932,244
Preferred stock	448,000	395,714	-	843,714
Total available-for-sale securities	$25,326,720	$ 487,653	$(395,976)	$25,418,397
Held-to-maturity securities:				
Tax-exempt bonds	$ 2,652,532	$ 5,993	$(176,191)	$ 2,482,334
Total held-to-maturity securities	$ 2,652,532	$ 5,993	$(176,191)	$ 2,482,334

At December 31, 2017 and 2016, securities with a carrying value of $15,962,344 and $30,018,637, respectively, were pledged to secure borrowings, public deposits, and for other purposes required or permitted by law.

Note 3 – Securities (Continued)

The amortized cost and fair value of debt securities by contractual maturity at December 31, 2017 are as follows:

	Securities Held to Maturity		Securities Available for Sale	
	Amortized Cost	Market Value	Amortized Cost	Market Value
Due in one year or less	$ 25,104	$ 25,698	$ -	$ -
Due in one through five years	116,273	125,693	1,730,765	1,719,455
Due in five years through ten years	147,335	166,471	7,277,212	7,274,212
Due after ten years	1,366,083	1,460,512	1,158,238	1,158,239
	1,654,795	1,778,374	10,166,215	10,151,906
Mortgage-backed securities	-	-	9,881,951	9,652,077
Preferred stock	-	-	448,000	732,614
Total	$ 1,654,795	$ 1,778,374	$20,496,166	$20,536,597

Information pertaining to securities with gross unrealized losses at December 31, 2017 and 2016, aggregated by investment category and length of time that individual securities have been in a continuous loss position, is as follows:

	2017			
	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
U.S. government and federal agency	$ -	$ -	$ (28,204)	$ 1,344,609
State and municipal	-	-	(71,787)	3,285,860
Mortgage backed	(34,665)	2,634,105	(157,072)	6,701,726
Total available-for-sale securities	$ (34,665)	$ 2,634,105	$ (257,063)	$ 11,332,195

	2016			
	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
U.S. government and federal agency	$ (57,312)	$ 1,798,114	$ -	$ -
State and municipal	(16,514)	1,209,895	(130,398)	3,881,730
Mortgage backed	(163,029)	7,478,859	(28,723)	2,287,303
Total available-for-sale securities	$ (236,855)	$10,486,868	$ (159,121)	$ 6,169,033

Unrealized losses on securities have not been recognized into income because the issuers' bonds are of high credit quality, the Bank has the intent and ability to hold the securities for the foreseeable future, and the decline in fair value is primarily due to increased market interest rates. The fair value is expected to recover as the bonds approach the maturity date.

Other securities consist of restricted Federal Home Loan Bank stock, Federal Reserve Bank stock and United Bankers' Bank stock. These stocks are carried at cost, which approximates market value.

Note 4 – Loans

A summary of the balances of loans is as follows:

	2017	2016
Mortgage loans on real estate:		
Residential 1-4 family	$ 34,982,520	$ 32,130,703
Commercial	91,968,755	87,409,633
Total mortgage loans on real estate	126,951,275	119,540,336
Commercial and agricultural loans	41,960,175	37,364,692
Consumer loans	2,498,377	2,675,488
Total loans	171,409,827	159,580,516
Less allowances for loan losses	1,972,106	1,984,349
Net loans	$169,437,721	$157,596,167

An analysis of the allowance for loan losses is as follows:

	2017	2016
Balance at beginning of year	$ 1,984,349	$ 1,879,237
Provision for loan losses	53,500	(321,917)
Loans charged off	(66,353)	(67,120)
Recoveries of loans previously charged off	610	494,149
Balance at end of year	$ 1,972,106	$ 1,984,349

The following is a summary of information pertaining to impaired loans:

	2017	2016
Impaired loans without a valuation allowance	$ 1,532,116	$ 445,303
Impaired loans with a valuation allowance	644,924	53,677
Total impaired	$ 2,177,040	$ 498,980
Valuation allowance related to impaired loans	$ 71,749	$ 10,946
Total nonaccrual loans	986,099	361,124
Average investment in impaired loans during the year	1,338,010	1,037,819

No interest income has been recognized on impaired loans during the years ended December 31, 2017 and 2016. No additional funds are committed to be advanced in connection with impaired loans.

In the ordinary course of business, the Bank has granted loans to principal officers, directors, and their affiliates amounting to $749,622 and $1,015,792 as of December 31, 2017 and 2016, respectively.

Note 4 – Loans (Continued)

December 31, 2017

	Residential Mortgages	Consumer Loans	Commercial Loans	Agricultural Loans	Commercial Real Estate Mortgages	Agricultural Real Estate Mortgages	Total
Allowance for Loan Loss:							
Beginning Balance	$ 402,476	$ 17,443	$ 438,852	$ 37,410	$ 1,013,245	$ 74,923	$ 1,984,349
Provision	(49,737)	6,349	(4,187)	21,695	100,561	(21,182)	53,499
Charge-offs	(3,586)	(6,303)	-	-	(56,463)	-	(66,352)
Recoveries	-	-	610	-	-	-	610
Total	$ 349,153	$ 17,489	$ 435,275	$ 59,105	$ 1,057,343	$ 53,741	$ 1,972,106
Specific Reserves-Impaired Loans	$ 9,791	$ -	$ -	$ -	$ 61,958	$ -	$ 71,749
General Reserves	339,362	17,489	435,275	59,105	995,385	53,741	1,900,357
Total	$ 349,153	$ 17,489	$ 435,275	$ 59,105	$ 1,057,343	$ 53,741	$ 1,972,106
Loans individually evaluated for impairment	$ 161,383	$ -	$ -	$ -	$ 2,015,657	$ -	$ 2,177,040
Loans collectively evaluated for impairment	34,821,137	2,498,377	38,431,506	3,528,669	86,744,686	3,208,412	169,232,787
Total	$34,982,520	$ 2,498,377	$38,431,506	$ 3,528,669	$88,760,343	$ 3,208,412	$171,409,827

	Impaired Loans With Allowance			Impaired Loans With No Allowance	
	Principal Balance	Recorded Investment	Allocated Allowance for Loan Loss	Principal Balance	Recorded Investment
Impaired Loans and Related Allowance:					
Residential Mortgages	$ 52,201	$ 46,694	$ 9,791	$ 129,082	$ 114,690
Consumer Loans	-	-	-	-	-
Commercial Loans	-	-	-	-	-
Agricultural Loans	-	-	-	-	-
Commercial Real Estate Mortgages	598,230	598,230	61,958	206,587	148,869
Agricultural Real Estate Mortgages	-	-	-	-	-
Total	$ 650,431	$ 644,924	$ 71,749	$ 335,669	$ 263,559

Note 4 – Loans (Continued)

December 31, 2016

	Residential Mortgages	Consumer Loans	Commercial Loans	Agricultural Loans	Commercial Real Estate Mortgages	Agricultural Real Estate Mortgages	Total
Allowance for Loan Loss:							
Beginning Balance	$ 346,914	$ 19,689	$ 327,462	$ 43,273	$ 1,082,769	$ 59,130	$ 1,879,237
Provision	98,321	(7,857)	131,952	(5,863)	(554,263)	15,793	(321,917)
Charge-offs	(42,759)	(900)	(21,981)	-	(1,480)	-	(67,120)
Recoveries	-	6,511	1,419	-	486,219	-	494,149
Total	$ 402,476	$ 17,443	$ 438,852	$ 37,410	$ 1,013,245	$ 74,923	$ 1,984,349
Specific Reserves-Impaired Loans	$ 10,946	$ -	$ -	$ -	$ -	$ -	$ 10,946
General Reserves	391,530	17,443	438,852	37,410	1,013,245	74,923	1,973,403
Total	$ 402,476	$ 17,443	$ 438,852	$ 37,410	$ 1,013,245	$ 74,923	$ 1,984,349
Loans individually evaluated for impairment	$ 202,941	$ -	$ -	$ -	$ 1,552,287	$ -	$ 1,755,228
Loans collectively evaluated for impairment	31,927,762	2,675,488	34,491,366	2,873,356	80,649,454	5,207,862	157,825,288
Total	$32,130,703	$ 2,675,488	$34,491,366	$ 2,873,356	$82,201,741	$ 5,207,862	$159,580,516

	Impaired Loans With Allowance			Impaired Loans With No Allowance	
	Principal Balance	Recorded Investment	Allocated Allowance for Loan Loss	Principal Balance	Recorded Investment
Impaired Loans and Related Allowance:					
Residential Mortgages	$ 53,677	$ 50,546	$ 10,946	$ 162,395	$ 152,395
Consumer Loans	-	-	-	-	-
Commercial Loans	-	-	-	-	-
Agricultural Loans	-	-	-	-	-
Commercial Real Estate Mortgages	-	-	-	282,908	240,588
Agricultural Real Estate Mortgages	-	-	-	-	-
Total	$ 53,677	$ 50,546	$ 10,946	$ 445,303	$ 392,983

Note 4 – Loans (Continued)

December 31, 2017

Credit Quality Indicators by Type of Loan:	Residential Mortgages	Consumer Loans	Commercial Loans	Agricultural Loans	Commercial Real Estate Mortgages	Agricultural Real Estate Mortgages	Total	Grade
Grade								
Pass	$34,731,210	$ 2,498,377	$35,481,560	$ 3,528,669	$83,491,696	$ 3,176,610	$162,908,122	1-4
Special Mention	-	-	2,008,602	-	2,581,247	31,802	4,621,651	5
Substandard	251,310	-	941,344	-	2,687,400	-	3,880,054	6
Doubtful	-	-	-	-	-	-	-	7
Loss	-	-	-	-	-	-	-	8
Total	$34,982,520	$ 2,498,377	$38,431,506	$ 3,528,669	$88,760,343	$ 3,208,412	$171,409,827	

Aging analysis of Past Due Loans and Nonaccrual Loans:	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days or Nonaccrual	Total Past Due Loans	Total Current Loans	Total Loans	Recorded Investment Past Due >90 Days and Still Accruing
Residential Mortgages	$ 224,757	$ -	$ 186,892	$ 411,649	$34,570,871	$ 34,982,520	$ -
Consumer Loans	1,673	-	913	2,586	2,495,791	2,498,377	-
Commercial Loans	519,132	-	-	519,132	37,912,374	38,431,506	-
Agricultural Loans	-	-	-	-	3,528,669	3,528,669	-
Commercial Real Estate Mortgages	179,743	-	620,463	800,206	87,960,137	88,760,343	-
Agricultural Real Estate Mortgages	-	15,913	-	15,913	3,192,499	3,208,412	-
Total	$ 925,305	$ 15,913	$ 808,268	$ 1,749,486	$169,660,341	$171,409,827	$ -

Note 4 – Loans (Continued)

December 31, 2016

Credit Quality Indicators by Type of Loan:	Residential Mortgages	Consumer Loans	Commercial Loans	Agricultural Loans	Commercial Real Estate Mortgages	Agricultural Real Estate Mortgages	Total	Grade
Grade								
Pass	$31,868,251	$ 2,675,488	$34,401,648	$ 2,873,356	$78,182,753	$ 4,876,479	$154,877,975	1-4
Special Mention	-	-	89,688	-	3,710,138	331,383	4,131,209	5
Substandard	262,452	-	-	-	308,880	-	571,332	6
Doubtful	-	-	-	-	-	-	-	7
Loss	-	-	-	-	-	-	-	8
Total	$32,130,703	$ 2,675,488	$34,491,336	$ 2,873,356	$82,201,771	$ 5,207,862	$159,580,516	

Aging analysis of Past Due Loans and Nonaccrual Loans:	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days or Nonaccrual	Total Past Due Loans	Total Current Loans	Total Loans	Recorded Investment Past Due >90 Days and Still Accruing
Residential Mortgages	$ 93,508	$ -	$ 120,536	$ 214,044	$31,916,659	$ 32,130,703	$ -
Consumer Loans	3,386	1,432	-	4,818	2,670,670	2,675,488	-
Commercial Loans	-	-	-	-	34,491,336	34,491,336	-
Agricultural Loans	-	-	-	-	2,873,356	2,873,356	-
Commercial Real Estate Mortgages	1,068	-	240,588	241,656	81,960,115	82,201,771	-
Agricultural Real Estate Mortgages	-	-	-	-	5,207,862	5,207,862	-
Total	$ 97,962	$ 1,432	$ 361,124	$ 460,518	$159,119,998	$159,580,516	$ -

Note 4 – Loans (Continued)

The following tables present loans by class modified as troubled debt restructurings that occurred during the years ending December 31, 2017 and 2016:

2017	Number of Loans	Premodification Outstanding Recorded Investment	Post-Modification Balance at December 31, 2017
Troubled Debt Restructurings:			
Commercial:			
Construction		$ -	$ -
Commercial residential	1	1,343,504	1,343,504
Non-farm non-residential	1	26,094	26,094
Other	-	-	-
Agriculture:			
Agriculture 1-4 family	-	-	-
Other agriculture real estate	-	-	-
Other agriculture	-	-	-
Real Estate Mortgage:			
Construction	-	-	-
1-4 owner occupied	-	-	-
Installment:			
Auto	-	-	-
Other	-	-	-
Total	2	$ 1,369,598	$ 1,369,598

2016	Number of Loans	Premodification Outstanding Recorded Investment	Post-Modification Balance at December 31, 2016
Troubled Debt Restructurings:			
Commercial:			
Construction	-	$ -	$ -
Commercial residential	1	1,396,332	1,396,332
Non-farm non-residential	1	28,039	28,039
Other	-	-	-
Agriculture:			
Agriculture 1-4 family	-	-	-
Other agriculture real estate	-	-	-
Other agriculture	-	-	-
Real Estate Mortgage:			
Construction	-	-	-
1-4 owner occupied	-	-	-
Installment:			
Auto	-	-	-
Other	-	-	-
Total	2	$ 1,424,371	$ 1,424,371

Troubled debt restructurings for which there was a payment default within twelve months following the modification during the year ending December 31, 2017 consists of loans totaling $0 at December 31, 2017.

The troubled debt restructurings described above had no specific reserves at December 31, 2016.

Note 5 – Bank Premises and Equipment

A summary of the cost and accumulated depreciation of premises and equipment is as follows:

	2017	2016
Land	$ 1,712,661	$ 1,460,639
Buildings and building improvements	4,978,990	4,768,854
Furniture, fixtures, and equipment	2,058,839	1,838,919
Vehicles	47,073	36,161
Total	8,797,563	8,104,573
Accumulated depreciation	(4,281,898)	(4,017,236)
Net premises and equipment	$ 4,515,665	$ 4,087,337

Depreciation expense for the years ended December 31, 2017 and 2016 amounted to $290,111 and $273,354, respectively.

Note 6 – Deposits

The following is a summary of the distribution of deposits at December 31:

	2017	2016
Demand deposits	$ 33,351,542	$ 36,151,748
NOW accounts	38,753,381	37,024,683
Savings and money market accounts	74,672,907	62,035,807
Time:		
Under $100,000	23,077,864	24,529,115
$100,000 and over	9,962,004	8,229,963
Total	$179,817,698	$167,971,316

At December 31, 2017, the scheduled maturities of time deposits are as follows:

2016	$ 16,602,636
2017	12,049,842
2018	1,715,151
2019	1,322,150
2020	1,350,089
Total	$ 33,039,868

Note 7 – Federal Home Loan Bank Advances

The Bank has a borrowing arrangement with the Federal Home Loan Bank of Cincinnati. Advances under the borrowing arrangement are supported by individual agreements. At December 31, 2017, the Bank has advances outstanding with an interest rate ranging from 1.09 percent to 2.41 percent.

The advances are collateralized by investment securities with a carrying value of $34,933,704 at December 31, 2017.

At December 31, 2017, the advances mature as follows:

2018	$ 63,164
2019	4,064,703
2020	66,280
2021	50,768
2022	-
2023 and thereafter	-
Total	$ 4,244,915

Note 8 – Bank Line of Credit

During 2008, the Corporation entered into a $5,000,000 line of credit arrangement with a bank. The line of credit is collateralized by First National Bank stock owned by the Corporation. The Corporation makes quarterly interest-only payments and the principal balance is due on demand and subject to an annual review. The balance outstanding as of December 31, 2017 and 2016 was $3,699,073 and $3,699,073, respectively. The interest rate was 4.50 percent and 4.00 percent as of December 31, 2017 and 2016, respectively.

Note 9 – Minimum Regulatory Capital Requirements

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined) and Tier I capital (as defined) to average assets (as defined).

As of December 31, 2017, the Bank was categorized as well capitalized under regulatory frame work for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the following table. There are no conditions or events since December 31, 2017 that management believes have changed the Bank's category. The Bank's actual capital amounts and ratios as of December 31, 2017 and 2016 are also presented in the table.

	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions	
(000's omitted)	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2017						
Total capital to risk-weighted assets	$22,931	11.8%	$15,529	8.0%	$19,411	10.0%
Tier I capital to risk-weighted assets	20,831	10.7%	11,647	6.0%	15,529	8.0%
Common equity Tier I capital to risk-weighted assets	20,831	10.7%	8,735	4.5%	12,617	6.5%
Tier I capital to average assets	20,831	9.7%	8,586	4.0%	10,732	5.0%
As of December 31, 2016						
Total capital to risk-weighted assets	$21,579	12.0%	$14,422	8.0%	$18,027	10.0%
Tier I capital to risk-weighted assets	19,417	10.8%	10,816	6.0%	14,422	8.0%
Common equity Tier I capital to risk-weighted assets	19,417	10.8%	8,112	4.5%	11,718	6.5%
Tier I capital to average assets	19,417	9.6%	8,101	4.0%	10,126	5.0%

Note 10 – Restrictions on Dividends

Banking regulations place certain restrictions on dividends paid and loans or advances made by the Bank to the Corporation. Prior approval of the Bank's federal regulator is required if the total dividends declared by the Bank exceed the sum of the net profits of the Bank for the current year-to-date and the net profits of the Bank for the preceding two years, less any required transfers to surplus. In addition, dividends paid by the Bank would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum standards. At December 31, 2017, retained earnings of approximately $3,938,000 was available for the payment of dividends without regulatory approval.

Note 11 – Employee Benefit Plan

The Bank sponsors a defined contribution benefit plan for substantially all employees. Bank contributions are based on matching one-half of participant contributions up to 6 percent of the participant's salary. Additional contributions may be made at the discretion of the board of directors. Discretionary contributions of $140,262 and $109,503 were made for the years ended December 31, 2017 and 2016, respectively. Bank contributions to the plan totaled $220,529 and $172,008 for the years ended December 31, 2017 and 2016, respectively.

Note 12 – Income Taxes

The components of the net deferred tax assets, included in other assets are as follows:

	2017	2016
Deferred tax assets:		
Other real estate owned writedowns	$ 3,455	$ -
Allowance for loan losses	267,708	437,594
Net deferred loan fees	14,785	27,294
Accrued employee benefits	117,579	178,291
Impairment on investment securities	273,420	442,680
Other	2,442	3,954
Total deferred tax assets	$ 679,389	$1,089,813
Deferred tax liabilities:		
Depreciation	$ 176,627	$ 246,712
Mortgage servicing rights	129,164	174,928
Federal Home Loan Bank stock dividends	58,065	94,010
Net unrealized gain on securities available for sale	8,491	31,170
Other	16,004	60,575
Total deferred tax liabilities	388,351	607,395
Net deferred tax assets	$ 291,038	$ 482,418

The components of deferred taxes are valued using the 21% federal income tax rate in 2017. In 2016, they were valued at the 34% tax rate.

Allocation of income tax recovery between current and deferred portions is as follows:

	2017	2016
Current	$ 494,257	$ 566,463
Deferred	720,303	164,741
Total	$ 1.214,560	$ 731,204

The reasons for the difference between the income tax (recovery) expense at the federal statutory income tax rate and the recorded income tax recovery are summarized as follows:

	2017	2016
Income tax expense at federal statutory rate of 34 percent	$ 960,951	$ 878,190
Increases resulting from nondeductible expenses	6,067	5,322
Decreases resulting from nontaxable investment income	(87,487)	(110,630)
Decreases resulting from life insurance contract income	(23,150)	(23,348)
Other	(3,265)	(18,330)
Effect of tax rate change on deferred taxes	361,444	-
Total	$ 1,214,560	$ 731,204

Note 13 – Commitments and Credit Risk

Credit-related Financial Instruments – The Corporation is a party to credit-related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial

Note 13 – Commitments and Credit Risk (Continued)

instruments include commitments to extend credit, standby letters of credit, and commercial letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidate balance sheet.

The Corporation's exposure to credit loss is represented by the contractual amount of these commitments. The Corporation follows the same credit policies in making commitments as it does for on-the-balance sheet instruments.

At December 31, 2017 and 2016, the following financial instruments were outstanding whose contract amounts represent credit risk:

	Contract Amount	
	2017	2016
Commitments to grant loans and unused lines of credit	$28,612,000	$30,518,000
Commercial and standby letters of credit	32,000	85,000

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The commitments for equity lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Corporation, is based on management's credit evaluation of the customer.

Unfunded commitments under commercial lines of credit, revolving credit lines, and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit are generally collateralized and may not be drawn upon to the total extent to which the Corporation is committed.

Commercial and standby letters of credit are conditional commitments issued by the Corporation to guarantee the performance of a customer to a third party. Those letters of credit are used primarily to support public and private borrowing arrangements. The credit risk involved is extending loan facilities to customers. The Corporation generally holds collateral supporting those commitments if deemed necessary.

Collateral Requirements – To reduce credit risk related to the use of credit-related financial instruments, the Corporation might deem it necessary to obtain collateral. The amount and nature of the collateral obtained are based on the Corporation's credit evaluation of the customer. Collateral held varies but may include cash, securities, accounts receivable, inventory, property, plant, and equipment, and real estate.

If the counterparty does not have the right and ability to redeem the collateral or the Corporation is permitted to sell or repledge the collateral on short notice, the Corporation records the collateral in its balance sheet at fair value with a corresponding obligation to return it.

Legal Contingencies – Various legal claims arise from time to time in the normal course of business. In the opinion of management, any outstanding claims will not have a material effect on the Corporation's consolidated financial statements.

Note 14 – Condensed Financial Statements of Parent Company

Presented below is condensed financial information as to financial position, results of operations, and cash flows of the Corporation as of and for the years ended December 31:

Balance Sheet

	2017	2016
Cash	$ 2,507	$ 33,152
Investment in common stock of subsidiaries	20,901,603	19,721,341
Premises and equipment – Net	491,122	491,121
Other assets	142,236	141,087
Total assets	$ 21,537,468	$ 20,386,701
Liabilities – Borrowings	$ 3,699,073	$ 3,699,073
Other liabilities	47,083	-
Stockholders' equity	17,791,312	16,687,628
Total liabilities and stockholders' equity	$ 21,537,468	$ 20,386,701

Note 14 – Condensed Financial Statements of Parent Company (Continued)

Statement of Operations

	2017	2016
Total income – Dividends from subsidiaries	$ 718,000	$ 1,225,000
Operating expenses	272,653	239,349
Income (loss) before equity in undistributed net income of subsidiaries and income tax benefit	445,347	985,651
Equity in undistributed net income of subsidiaries	1,083,663	783,752
Income tax benefit	86,488	82,305
Net income	$ 1,615,498	$ 1,851,708

Statement of Cash Flows

	2017	2016
Cash flows from operating activities:		
Net income	$ 1,615,498	$ 1,851,708
Adjustments to reconcile net income to net cash from operating activities:		
Distributions from subsidiaries in excess of net income equity in undistributed net income of subsidiaries	(1,170,400)	(2,008,752)
Net change in other assets	(1,149)	(2,472)
Net change in other liabilities	11,992	(75,115)
Net cash provided by operating activities	455,941	(234,631)
Cash flows from financing activities:		
Cash dividends paid on common stock	(483,540)	(410,028)
Change in note payable	-	650,000
Purchase of treasury stock	(3,046)	(1,780)
Net cash used in financing activities	(486,586)	238,192
Net increase (decrease) in cash	(30,645)	3,561
Cash – Beginning of year	33,152	29,591
Cash – End of year	$ 2,507	$ 33,152

Note 15 – Fair Value of Financial Instruments

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Corporation's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instruments. FAS ASC 825 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Corporation.

Note 15 – Fair Value of Financial Instruments (Continued)

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

Cash and Cash Equivalents – The carrying amounts of cash and cash equivalents approximate fair value.

Securities – Fair values of securities are based on quoted market prices. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities. The carrying value of Federal Home Loan Bank and Federal Reserve Bank stock approximates fair value based on the redemption provisions of the issuers.

Loan Receivable – For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values of nonperforming loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

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

Federal Home Loan Bank Advances and Bank Line of Credit – The fair values of the Corporation's borrowings are estimated using discounted cash flow analyses based on the Corporation's current incremental borrowing rates for similar types of borrowing arrangements.

Accrued Interest – The carrying amounts of accrued interest approximate fair value.

Other Financial Instruments – The fair value of other financial instruments, including loan commitments and unfunded letters of credit, based on discounted cash flow analyses, is not material.

The estimated fair values and related carrying or notional amounts of the Corporation's financial instruments are as follows (000s omitted):

			(Dollars in thousands) Fair Value Measurements		
	Carrying Amount	Fair Value	Quoted Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2017					
FINANCIAL ASSETS					
Cash and cash equivalents	$ 5,715	$ 5,715	$ 5,715	$ -	$ -
Investment securities					
Available-for-sale	20,537	20,537	-	-	-
Held-to-maturity	1,655	1,778	-	-	-
Net loans	169,438	171,123	-	-	171,123
FINANCIAL LIABILITIES					
Deposits	$179,818	$167,153	$ -	$ -	$167,153
FHLB borrowings	4,245	4,256	-	-	4,256
Federal funds purchased	2,288	2,288	2,288	-	-
Bank line of credit	3,699	3,699	-	-	3,699

Note 15 – Fair Value of Financial Instruments (Continued)

			(Dollars in thousands) Fair Value Measurements		
	Carrying Amount	Fair Value	Quoted Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2016					
FINANCIAL ASSETS					
Cash and cash equivalents	$ 5,686	$ 5,686	$ 5,686	$ -	$ -
Investment securities					
Available-for-sale	25,418	25,418	-	21,155	4,264
Held-to-maturity	2,653	2,482	-	1,589	893
Net loans	157,596	158,589	-	-	159,589
FINANCIAL LIABILITIES					
Deposits	$167,971	$160,827	$ -	$ -	$160,827
FHLB borrowings	9,301	9,321	-	-	9,321
Bank line of credit	2,463	2,463	2,463	-	-
	3,699	3,699	-	-	3,699

Note 16 – Fair Value Measurements

Accounting standards require certain assets and liabilities be reported at fair value in on the financial statements and provides a framework for establishing other fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

The following table presents information about the Corporation's assets and liabilities measured at fair value on a recurring basis at December 31, 2017, and the valuation techniques used by the Corporation to determine those fair values.

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities that the Corporation has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, similar techniques taking into account the characteristics of the asset.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Corporation's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

Note 16 – Fair Value Measurements (Continued)

Assets Measured at Fair Value on a Recurring Basis at December 31, 2017 and 2016

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31
2017 – Investment securities available for sale	$ -	$ 17,316,105	$ 3,711,496	$ 21,027,601
2016 – Investment securities available for sale	$ -	$ 21,154,822	$ 4,263,575	$ 25,418,397
2017 – Investment securities held to maturity	$ -	$ 1,608,374	$ 170,000	$ 1,778,374
2016 – Investment securities held to maturity	$ -	$ 1,588,770	$ 893,564	$ 2,482,334

The Corporation also has certain assets that are measured at fair value on a nonrecurring basis. These assets are not measured at fair value on an ongoing basis, but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

Held-to-maturity investment securities categorized as Level 3 assets consist of tax-exempt bonds issued by local municipalities and trust preferred securities. The balance of these Level 3 securities was $170,000 and $893,564 at December 31, 2017 and 2016, respectively. The Corporation estimates the fair value of these investments based on the present value of expected future cash flows using management's best estimate of key assumptions, including forecasted interest yield and payment rates, credit quality, and a discount rate commensurate with the current market and other risks involved. Both observable and unobservable inputs may be used to determine the fair value of Level 3 assets

The fair value of impaired loans is estimated using either discounted cash flows or collateral value. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At December 31, 2017, substantially all of the total impaired loans were evaluated based on the fair value of the collateral. Impaired loans are categorized as Level 3 assets because the values are based on available collateral (typically based on outside appraisals) and customized discounting criteria, if deemed necessary. At December 31, 2017 and 2016, impaired loans total $2,177,040 and $498,980, respectively. The change in fair value of impaired loans is accounted for in the allowance for loan losses (see Note 4).

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