STRONG VALUES • SOLID GROWTH

Lyons Bancorp, Inc.
It's all about people.

2017
ANNUAL REPORT

Hometown Values.

COMMUNITY-COMMITTED

Many banks claim to support their local communities, but none live their commitment each and every day quite like LNB.

PEOPLE-FOCUSED

At LNB, it's all about people. And it's been that way for more than 165 years. We don't just aim to serve, we WOW! every opportunity we get.

HIGH-TOUCH, HIGH-TECH

Delivering a personalized experience is paramount. Offering a full suite of convenient online and mobile banking technologies—well, that's just icing on the cake!

Chairman's Message

Robert A. Schick

Chairman of the Board and CEO
Lyons Bancorp, Inc. & The Lyons National Bank

One of the advantages of being a community bank is our size, which enables us to quickly connect internally with each other and respond to customers. This nimbleness gives us a competitive advantage over our behemoth brethren, the mega regional and money-centered banks who, more often than not, get bogged down in their large, self-imposed organizational maze. To enhance our competitive advantage, we ask our staff to adhere to the convention of "please, no last-minute unpleasant surprises." If employees know of a developing issue, they promptly notify their supervisor so the bank isn't caught "flat-footed." While our internal communication isn't perfect, it is much more effective than the many interactions we have with regulators and government agencies. At the risk of being accused of looking a gift horse in the mouth, the Tax Cuts and Jobs Act of 2017 (passed on December 22, 2017) is a great example of being confronted with a late, unexpected, unpleasant surprise with little time to plan or react effectively.

As you know, the Act lowered the corporate marginal tax rate to 21% from 35% for 2018 and beyond. That in itself is very good news for Lyons Bancorp, its shareholders, and employees (more on that later). But, of course, the devil is in the details—and the key detail was accounting guidance which required corporations like us to adjust the value of our deferred tax assets and liabilities in the few remaining days (there's the rub) of 2017. Not to bore you with all the fine points, but deferred tax assets and liabilities are created because of timing differences between the required "book" and "tax" accounting principles to which we adhere. Many corporations have both deferred tax assets and tax liabilities on their balance sheet. Since we had more of the former, we had a NET deferred tax asset that required revaluation. The difference between the old tax rate of 35% and the new rate of 21% applied to our net position amounted to almost $600,000. This reduced our operating earnings by $0.15 per common share, from $2.58 to $2.43. (For more information regarding deferred tax assets and liabilities, see Note #9—Income Taxes on page 31 in our financial statement.)

Had the Tax Act been passed earlier in the year, we would have been able to plan differently. Chad Proper, our Chief Financial Officer, worked his magic to offset a portion of the write-down, but there wasn't enough time left in 2017 to mitigate much more. The good news in all of this last-minute yearend tax juggling is that even an act of Congress didn't prevent us from recording our 21st consecutive year of higher earnings. In 2017, Lyons Bancorp earned $8 million or $400,000 more than we made in 2016. On a per common share basis, we earned $2.43 versus $2.42 in 2016. Not a lot higher but remember the yearend surprise.

In 2018, we will make up the one-time $600,000 write-down as a result of our lower federal tax obligation. Without considering the many other dynamics that affect our various sources of income, it looks like we will send approximately $1 million less to Uncle Sam each year with the reduced tax rate. Keep in mind, our operating earnings (excluding the tax adjustment) per common share for 2017 would have been $2.58. All things being equal, 2018 earnings will start from that level.

Driving our strong operating earnings results was again our growth—both in assets and customer relationships. In 2017, for the first time ever, Lyons Bancorp joined the $1 billion asset club. On December 31st, assets totaled $1.03 billion, an increase of almost 8% from 2016. The approximate $75 million increase in assets is the largest increase in any single year in our history. Key to the gain in assets was our growth in customer relationships. In 2017, we added 3,300 new customer relationships to The Lyons National Bank family. Never before in our 165-year history have we added so many relationships in one year. Chad Proper details our financial performance in his report on subsequent pages.

We opened a new branch in downtown Auburn, Cayuga County, in 2017. According to the 2010 census, the City of Auburn was home to over 27,000 people, making it our largest market outside of Monroe County. Plus, the Federal Deposit Insurance Corporation (FDIC) reports that Auburn is a $725 million deposit market. Furthermore, we estimate there are 1,045 small businesses located in and immediately around the City of Auburn. We made the decision to branch into Auburn because the two largest regional banks with branch offices in the market merged. Between the two, they "owned" 44% of Auburn's banking market. Past history of similar large-bank mergers has proven to be an opportunity for a nimble community bank to do very well as disruption takes its toll in the marketplace. We plan on being that community bank!

In February of 2018, we will enhance our presence and commitment to Auburn by opening a second branch office in the Town of Sennett on the eastern border of the Auburn city limits. I invite you all to stop by the branch and meet with Demetrius Murphy, our Branch Manager, and his staff.

Our new Auburn location was not the only source of our growth in 2017. Tom Kime, our President, digs deeper into our broad market successes in his write-up. Make sure to read his report.

While crossing the $1 billion asset threshold is an important milestone, so too is our market capitalization, which at yearend approximated $115 million. As I have mentioned in prior reports, $1 billion in assets and $100 million in market capitalization are characteristics that will help us gain the attention of institutional investors. Institutional investors, in turn, should help increase the liquidity of our common shares. We are currently working on multiple fronts to help us expand the market for our shares. One of the first building blocks toward that end was outsourcing the transfer agent and registrar function to Broadridge Corporate Issuer Solutions, Inc.

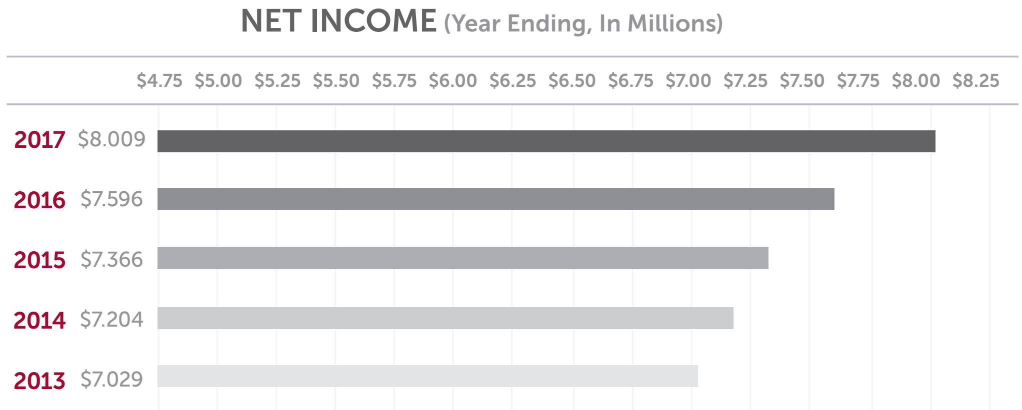
Completed in August of 2017, the conversion to Broadridge went relatively smoothly. Be assured, though—we closely watch the level of service they provide you, our shareholders. Feel free to contact me or Carol Snook, our Corporate Secretary, if you deem it necessary for us to become involved in an issue.

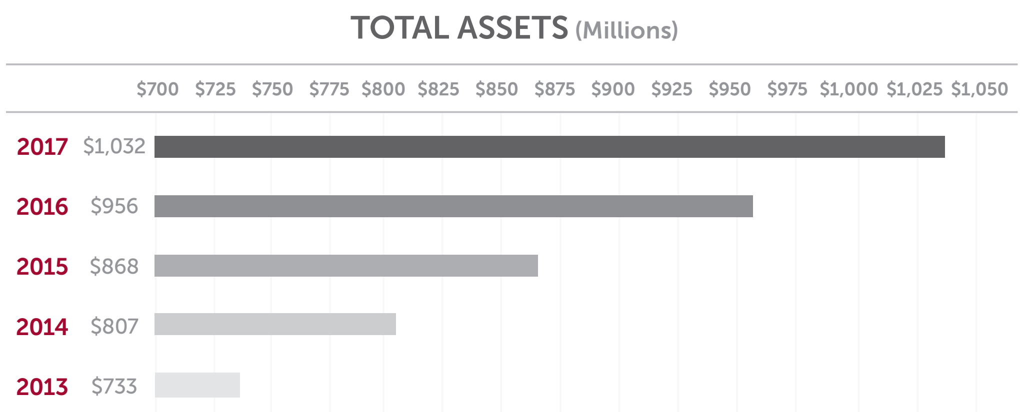
2017 marked the 20th consecutive year that we increased the dividend on our common shares. Our annual dividend of $1.08 divided by the closing price on December 29th (the last trading day of 2017) provided a yield in excess of 3%. As long as our income and financial strength remain strong, the Board remains committed to a dividend payout goal of approximately 40% of after-tax earnings.

Mid-year 2017, we applied for and received from the Federal Reserve Bank (FRB) of New York the designation of financial holding company. This initiative, led by our Chief Performance Officer, Kelly Mittiga, expands our financial powers, allowing us to venture into other financial, non-banking activities. While nothing has been finalized, we have been conducting due diligence on a couple of opportunities. We tread lightly in this arena as any purchase of an entity or entrance into an additional line of business must complement our basic banking business and enhance our market value.

> **"Past history of similar large-bank mergers has proven to be an opportunity for a nimble community bank to do very well as disruption takes its toll in the marketplace. We plan on being that community bank!"**
>
> —Robert A. Schick

Earlier, I mentioned a first estimate of $1 million in 2018 income tax savings due to the passage of the Tax Cuts and Jobs Act of 2017 in late December. The $1 million is both a first AND rough estimate.





We, like all other corporations affected by the bill, are still sorting through the myriad of provisions within the Act. Along with the change in the tax rate, there are numerous other changes to previous qualified business deductions. These changes will somewhat offset the reduced tax rate. Further complicating matters, New York State tax law does not align itself well with federal tax law. This fact also tends to mitigate some of the upside of the new bill. We are working with our tax advisors to better understand the ins and outs of the legislation so we can maximize its benefits.

That said, the actual tax savings will be substantial. In a media release in January, I stated that once we have a handle on what that number is, we will divide that savings three ways. First, we will allow a good portion to flow to the bottom line, rewarding shareholders for their confidence and support. Second, we will invest in technology, which will further improve our efficiency and enhance our future returns to shareholders. Last but not least, we will invest in our employees, the folks that make Lyons Bancorp the success that it is. Our goal is to have definitive plans in place in the second quarter of 2018.

The optimistic theory supporting the passage of the Tax Cuts and Jobs Act of 2017 is that the tax savings corporations realize will be channeled into new private investments that will create more jobs and lead to higher levels of economic growth. This growth, in turn, will produce new federal revenues, partially offsetting taxes the Act eliminates. In a January 2018 weekend edition, *The Wall Street Journal* reported the economy was picking up as firms planned new spending and hiring. Large corporations planned to repatriate U.S. dollars from their overseas subsidiaries and pay one-time taxes in doing so. All this plays to that theory. But if for some reason the theory doesn't pan out or if other federal expenditures are not reduced to offset the loss of tax revenues, government borrowing will increase, ballooning annual deficits and the national debt. What then? As more federal revenues are diverted away from social and infrastructure rebuilding programs to repay increased federal debt, will the gift horse turn out to be a Trojan horse? Stay tuned!

Thanks for your continued support and confidence.

Robert A. Schick

President's Message

Thomas L. Kime

President, The Lyons National Bank

Inasmuch as it is provided in more detail elsewhere in this Annual Report, it will suffice for me to note that LNB exceeded its profit plan, surpassing the $1 billion milestone in 2017 and achieving its 21st year of record earnings. Just as important, the LNB team of Board and Advisory Board members, officers, and staff accomplished this while still making a commitment to, and investing significantly in, our technology and security platforms, staffing, and training programs, as well as expanding into a new, key marketplace while covering one-time expenses related to year-end changes in the tax laws; all of which will benefit us in the coming years. While 2017 achieved solid results, our critical accomplishments were based on doing so while investing in our future, and the details behind those results are noted below.

Although we had strong growth in our deposits and loans in gross dollars, the growth in our new-to-bank customer base was even more impressive. Our growth in new customers exceeded 2016's growth rate by more than 30% and set a new record for LNB. This growth even exceeded those years when other banks in our markets closed offices, benefiting our growth at those times. While we have invested heavily in technology with enhanced customer accessibility, expanded features, and achieving higher levels of utilization, our in-office customer transaction volumes have continued to experience strong growth with a 35% increase in branch transaction volumes in 2017. Confirming studies showing that 75% of customers, if given the choice, desire both high-touch and high-tech banking options, not just one or the other. Our model of providing local, in-office community-based full service branch banking, from community-based banking professionals/decision makers, providing everything from residential mortgage origination to closings, commercial and agricultural lenders, consumer lenders, financial services representatives, coupled with a staff that is committed to consistently providing truly best in class customer service in combination with state of the art technology, have all been key to our success in consistently gaining share of market and a loyal customer base. Our goal remains to build true relationship accounts versus just growing deposits. In fact, as LNB has grown in customers and deposits, we have consistently grown true relationship-based checking accounts proportionately faster, increasing these balances to over 37% of our deposit base, significantly more than that of our industry. This is a testament to how well the LNB team does at building relationships with our customers.

> **Our growth in new customers exceeded 2016's growth rate by more than 30% and set a new record for LNB.**
>
> —Thomas L. Kime

The growth in our customer base and their utilization of services, has contributed directly to the consistent annual growth in LNB's noninterest income, hitting a record $9.8 million in 2017. Our strongest growth being in loan, financial services, and cardholder services at 61%, 19.5% and 12.7% annual growth respectively. As we look to diversify our income stream, this area remains a priority and an area of strategic opportunity we look to capitalize upon further.

In last year's President's Message, I announced LNB's commitment of expanding into and providing full service banking to the greater Auburn/Cayuga County marketplace. To that end, LNB's downtown Auburn office, located on Genesee Street, opened in April of 2017, and our newest full-service office, located on Grant Avenue, is set to be completed and open in February 2018. The successful expansion into any new market has been, and remains, a major priority for LNB, a focused commitment of time, resources and capital. Our Board, Advisory Boards and Management team have been and will remain actively involved in and committed to our Auburn Marketplace initiative. At this time last year, I noted the appointment of three community leaders and local businesspeople to our initial Auburn Advisory Board, (Joseph Bartolotta, Esq., John Bouck, and Salvatore Franzone), and that we would look to add three additional key members. I am proud to highlight the addition of Dick Beauchine, Wendy LaDuca and Mark DiVietro, all of whom accepted joining our Auburn Advisory Board. This group's commitment to the greater Auburn community, their input on and involvement in our Auburn initiative and how we can best meet the needs of this community has been invaluable, and combined with our local officers and staff will ensure that we do the best possible job in meeting those needs. Our Auburn Initiative has exceeded our expectations, with the establishment of more new customers over the same timeframe as any new market entry initiative to date. We invite you to stop in and take a tour of our newest offices and even ask Demetrius or any of our Auburn staff about utilizing our Cayuga Room at our Grant Avenue location.

In summary, we are positioned in markets that give us the opportunity to grow. We have an excellent team of professional staff and officers, supported by our local Board and Advisory Board members as well as a model of hometown banking that provides our customers and communities with a form of banking that allows us to build relationships and successfully grow LNB, as demonstrated by the results of all of our community-focused offices. We are committed to continuing to do so successfully to the benefit of our customers, employees, and shareholders.

Tom

Thomas L. Kime

LNB received United Way of Wayne County's Volunteer Award for providing the largest Day of Caring volunteer team. LNB was represented at four different sites—all organizations were incredibly grateful for the support!

WE'RE COMMUNITY-COMMITTED

Hometown banking is supporting community values.

LNB is proud to support local businesses and organizations because our mission is to help our communities thrive.

2017 Financial Highlights

Chad J. Proper

Vice President & Chief Financial Officer,
The Lyons National Bank

> “…average noninterest-bearing deposits increased $29.7 million, providing additional funding for our strong balance sheet growth.”
>
> —Chad J. Proper

RESULTS OF OPERATIONS

For the 21st consecutive year, Lyons Bancorp, Inc. experienced earnings growth and ended 2017 with record earnings of $8.0 million, an increase of $413,000 or 5.4% over 2016 despite the recently enacted tax law change. This translates into earnings per basic shares of $2.43 or a 0.4% increase year over year and a per diluted share of $2.42 or a 1.3% increase year over year. Return on average assets was 0.80%, and return on average shareholders' equity was 10.99%.

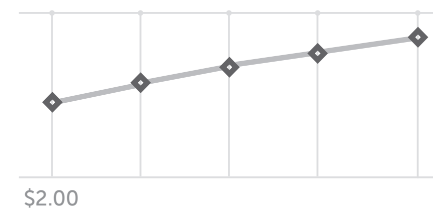
Our largest revenue source is net interest income, the difference between the interest income we earn on our interest-earning assets, primarily loans and investment securities, and the interest paid on our interest-bearing liabilities, primarily deposit accounts and borrowings. Net interest income for 2017 was $32 million, an increase of $3.7 million or 13.2% over 2016. This increase was due primarily to the strong growth of our earning assets funded by steady deposit growth, as average earning assets increased $71 million or 8% during 2017, and average interest-bearing deposits increased $27.0 million or 4% year over year. Completing our story, average noninterest-bearing deposits increased $29.7 million, providing additional funding for our strong balance sheet growth.

Our tax-equivalent margin increased year over year, measuring 3.36% during 2017, compared to 3.22% in 2016, as we were able to increase asset yields and reduce our overall funding costs.

Our provision for loan losses is based upon our assessment of a variety of factors, including loan credit quality, the general economic environment, and growth in our loan portfolio. In 2017, we provided $1.5 million for loan losses, compared to $1.1 million in 2016. At December 31, 2017, our nonperforming loans totaled 0.26% of total loans, as compared to 0.22% at December 31, 2016, and compared favorably to our peers' ratio of 0.59%. Our net charge-offs to average loans during 2017 totaled 0.10%, down from the prior year. The percent of our commercial and agriculture loan portfolio with an aggregate “pass” rating within our internal risk rating system improved to 97.2%, compared to 96.5% in 2016.

DILUTED EARNINGS PER SHARE

2013	2014	2015	2016	2017
$2.24	$2.29	$2.34	$2.39	$2.42



Noninterest income is an important revenue source for us and consists primarily of service charges on deposit accounts, loan servicing fees, cardholder fees, financial services fees, and gains on the sale of loans. In 2017, noninterest income represented 21% of all revenue sources and totaled $9.8 million, an increase of $133,000 or 1% over 2016 levels and is reflected across most major categories of noninterest income.

Noninterest expense consists primarily of compensation and employee benefits, occupancy and equipment expenses, advertising, data processing, professional fees, FDIC insurance, and other operating expenses. In 2017, total noninterest expense was $27.9 million, an increase of $1.9 million or 7% over 2016. Increases in salaries and wages totaled $1.04 million and were primarily the result of annual wage increases and a full year of expenses related to staffing at our newest branch locations in Auburn. Pension and other benefit expenses increased $325,000 or 9% in 2017, due primarily to an increase in base salaries and the number of employees covered by the plan, as well as an increase in health insurance premiums covered by the Bank. Cardholder costs increased $261,000 or 30% year over year, due in part to our VISA credit card program.

	2017			2016		
	AVERAGE BALANCE ($ in '000)	INTEREST INC/EXP ($ in '000)	AVERAGE YIELD/COST (%)	AVERAGE BALANCE ($ in '000)	INTEREST INC/EXP ($ in '000)	AVERAGE YIELD/COST (%)
INTEREST-EARNING ASSETS:						
Residential real estate	299,110	11,486	3.84%	259,800	9,900	3.81%
Commercial and agriculture real estate	207,694	9,968	4.80%	197,795	9,358	4.73%
Commercial and agriculture loans	160,978	7,572	4.70%	147,090	6,509	4.43%
Consumer installment loans	29,476	1,581	5.36%	27,280	1,529	5.61%
TOTAL LOANS	**697,258**	**30,607**	**4.39%**	**631,965**	**27,297**	**4.32%**
Investments	217,674	4,798	2.20%	212,974	4,808	2.26%
Federal funds sold & other interest-earning assets	28,150	295	1.05%	26,738	134	0.50%
TOTAL INTEREST-EARNING ASSETS	**943,082**	**35,700**	**3.79%**	**871,677**	**32,239**	**3.70%**
Noninterest-earning assets	51,901			51,416		
TOTAL ASSETS	**994,983**			**923,093**		
INTEREST-BEARING LIABILITIES:						
Interest-bearing checking	118,001	347	0.29%	105,137	288	0.27%
Money market and savings accounts	400,287	1,461	0.36%	384,374	1,867	0.49%
Time deposits	163,196	1,602	0.98%	165,008	1,544	0.94%
Borrowings	14,084	186	1.32%	7,280	82	1.13%
Junior subordinated debentures	6,190	385	6.22%	6,931	432	6.23%
TOTAL INTEREST-BEARING LIABILITIES	**701,758**	**3,981**	**0.57%**	**668,730**	**4,213**	**0.63%**
Noninterest-bearing deposits	212,411			182,721		
Other noninterest-bearing liabilities	7,949			7,313		
TOTAL LIABILITIES	**922,118**			**858,764**		
Total equity	72,865			64,329		
TOTAL LIABILITIES AND EQUITY	**994,983**			**923,093**		
Net interest spread			3.22%			3.07%
Net interest income/margin on earning assets		31,719	3.36%		28,026	3.22%
Tax equivalent adjustment		(741)			(717)	
Net interest income per financial statements		30,978			27,309	

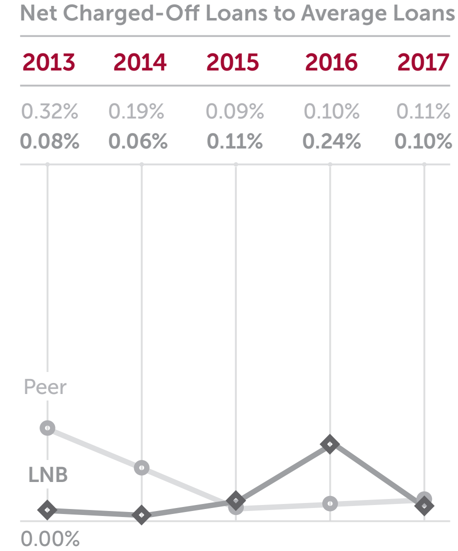
ANALYSIS OF FINANCIAL CONDITION

During 2017, we continued to experience solid loan and deposit growth, supported by a strong capital base. Total assets on December 31, 2017, were $1.032 billion, an increase of $75.7 million or 8% over December 31, 2016. Total equity at December 31, 2017, was $73.8 million, an increase of $5.0 million or 7% over December 31, 2016.

Total loans were $741.9 million at December 31, 2017, an increase of $63.2 million or 9% from December 31, 2016. We continued to support our strategy of maintaining balance within the loan portfolio between consumer and commercial loans, ending the year with 47% consumer-related loans versus 53% commercial-related loans, essentially unchanged from last year. We are well-positioned to continue prudent lending to the individuals, families, and businesses here in our Upstate New York marketplace and look forward to another year of solid loan growth.

TOTAL GROSS LOANS (Millions)

Net Charged-Off Loans to Average Loans



2017 Financial Highlights CONT.

We maintain an investment portfolio to provide us with important liquidity considerations and earnings potential. Our investment portfolio consists primarily of United States Agency debt, mortgage-backed securities either guaranteed by the U.S. government or issued by the Federal Home Loan Bank, and state and local government debt. As of December 31, 2017, our investment portfolio totaled $213.7 million, an increase of $8.1 million over December 31, 2016, and had an average tax-equivalent yield of 2.51% during 2017. The entirety of our portfolio is classified as available for sale and may be used for liquidity purposes as needed.

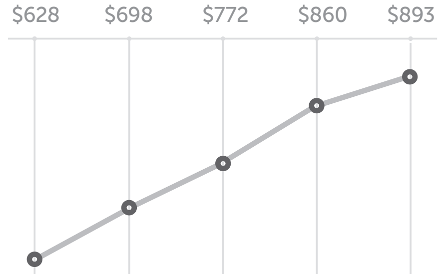
Deposits generated within our local markets are the major source of funds for our lending and investment activities. Total deposits at December 31, 2017, were $893.3 million, an increase of $33.2 million or 4% over December 31, 2016. We continued to experience strong growth in our core retail and commercial deposit base, with most of our branches increasing their presence in the communities they serve.

Total equity was $73.8 million at December 31, 2017. Our Board of Directors is committed to providing a solid return to our shareholders and declared a total of $1.05 per share in dividends during 2017. This represents a yield of 2.95% based on our yearend market price of $35.50 per share.

Please refer to our Consolidated Financial Report as of December 31, 2017, for more information regarding our 2017 results.

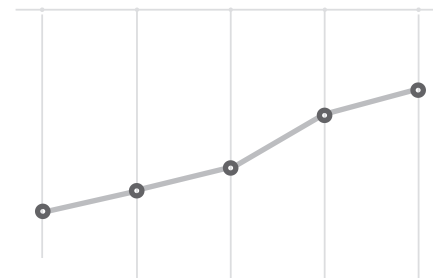
TOTAL DEPOSITS (Millions)

2013	2014	2015	2016	2017
$628	$698	$772	$860	$893



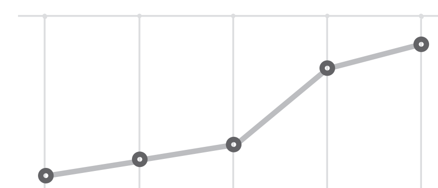
TOTAL EQUITY (Millions)

2013	2014	2015	2016	2017
$47.4	$52.5	$58.7	$68.9	$73.8



Dividends Declared to Net Income

2013	2014	2015	2016	2017
27.76%	29.37%	31.67%	41.84%	44.95%



Board of Directors

FROM LEFT TO RIGHT: **Robert A. Schick**, *Chairman of the Board, Lyons Bancorp and CEO, LNB,* **Joseph A. Fragnoli**, *Owner, Super Casuals,* **Carol A. Snook**, *Banking Officer & Corporate/Executive Secretary,* **Case A. Marshall**, *Lead Outside Director, CFO & Vice President, Marshall Companies,* **Clair J. Britt, Jr.**, *EVP & Chief Commercial Loan Officer,* **James A. Homburger**, *Real Estate Broker/Investor,* **Dale H. Hemminger**, *President & General Manager, Hemdale Farms & Greenhouses,* **James E. Santelli**, *Retired Vice President & Co-owner, Santelli Lumber Co.,* **Brad A. Person**, *President & General Manager, Nuttall Golf Cars, Inc. and Nuttall Golf Car Leasing, LLC,* **Kaye E. Stone-Ganz**, *President & CEO, Stone Goose Enterprises, Inc.,* **Andrew F. Fredericksen**, *CPA, Consultant, Petrella Phillips, LLC,* **David J. Breen, Jr.**, *Owner, Herrema's Market Place,* **Thomas L. Kime**, *President, LNB.*

Selected Financial Data

Year Ended December 31

	2017	2016	2015	2014	2013
FINANCIAL STATEMENT HIGHLIGHTS (IN THOUSANDS $)					
Assets	**1,031,844**	956,132	867,633	806,844	732,830
Loans, gross	**741,860**	678,691	605,201	544,464	500,884
Deposits	**893,256**	860,073	772,111	698,202	627,919
Other borrowings	**50,000**	18,000	20,126	38,791	42,000
Junior subordinated debentures	**6,190**	6,190	8,867	9,217	9,217
Total equity	**73,844**	68,853	58,678	52,506	47,410
Interest and dividend income	**35,700**	32,239	29,384	27,062	24,963
Interest expense	**3,981**	4,213	3,532	3,795	2,952
Net interest income	**31,719**	28,026	25,852	23,267	22,011
Provision for loan losses	**1,500**	1,100	1,275	750	525
Net securities gains	**(17)**	470	167	139	429
Net income	**8,009**	7,596	7,366	7,204	7,029
PER SHARE INFORMATION ($)					
Basic earnings per share	**2.43**	2.42	2.47	2.42	2.36
Cash dividends declared	**1.05**	0.95	0.78	0.71	0.66
Book value per share (incl. Conv. Pref.)	**22.31**	21.59	19.51	17.62	15.89
Book value per share (excl. Conv. Pref.)	**21.60**				
Company issued $5 million Conv. Pref. 12/2016					
Per share data reflects 2-for-1 stock split, effective 10/30/2015					
SELECTED RATIOS					
Return on average assets	**0.80%**	0.85%	0.88%	0.94%	1.01%
Return on average shareholders' equity	**10.99%**	10.70%	13.09%	13.96%	15.22%
Leverage ratio (Bank)	**8.33%**	8.49%	8.14%	8.21%	8.38%
Dividend payout ratio	**44.95%**	41.84%	31.21%	28.97%	20.12%
OTHER SELECTED DATA (IN WHOLE NUMBERS)					
Employees (full-time equivalent)	**213**	197	185	175	163
Banking offices	**14**	13	13	12	12

Thank you, James Santelli

After 30 years of service, Jim Santelli is retiring from the Board. Jim served us in various capacities, including Chairman of our Loan, Asset/Liability and Compensation Committees and as a member of our Executive and Governance Committees. He never took his responsibilities lightly. He always came prepared, ready to challenge management to ensure the Bank's policies and practices were effective and adhered to safety and soundness principles. Jim helped guide LNB to become the successful bank it is today. We will miss his sage advice and wise counsel, and we wish him, his wife Helen, and their entire family the very best. Thank you sir, you served us well.

Welcome, Teresa Jackson

We would like to welcome our newest director, Teresa Jackson. Along with joining the Board of our holding company, Teresa is also a Director of the Bank and Lyons Realty Associates Corporation. She is the owner of Dudley Poultry Company in Middlesex, New York, a wholesale food distributor serving restaurants and grocery stores in Upstate New York. Under her leadership, Dudley has expanded its product line extensively and has become a single-source supplier to its customer base. We look forward to Teresa offering her strategic insight to the Bank, and we believe she will play an integral role in the Bank's success and growth. Welcome to Lyons Bancorp, Teresa!

Advisory Boards

LNB's Advisory Boards are comprised of community leaders who live and operate their businesses in the communities we serve. These trusted advisors offer insight regarding important issues facing their local community and provide valuable feedback that helps keep LNB well-aligned with the local economy as well as with the people of the community.

Our Advisory Board members appreciate the value of hometown banking, which is why they choose not only to bank with LNB, but to serve on our Advisory Boards.

Thank you to each of our Advisory Board members. We appreciate your service and guidance!

CANANDAIGUA

J. David Damaske
Parkview Fairways Golf Course

April E. Dawson
Constellation Brands

Gail D. Herman
The Medicine Shoppe, Canandaigua

Eugene W. Hermenet
Retired, Curtice Burns Foods

Jack W. Moran
Roseland Bowl Family Fun Center

Charles W. Potter
Potter HVAC and Metal Fab, Inc.

CAYUGA COUNTY

Joseph P. Bartolotta, Esq.
R&M Real Estate Group

Richard L. Beauchine, CPA
Waterloo Container

John F. Bouck
Bouck Real Estate

Mark A. DiVietro, O.D.
Silbert Optical

Salvatore N. Franzone
Ciccino's Pizzeria and Restaurant

Wendy C. LaDuca
Reflections Medical and Cosmetic Dermatology

GENEVA

Stephen J. Blowers
Blowers Agri Service, Inc.

Peter J. D'Amico, Jr.
D'Amico Chrysler Dodge Jeep

Jason S. Feinberg, MD
Finger Lakes Health

Robert S. Flowers
Hobart and William Smith Colleges

Bernard G. Lynch
Lynch Furniture

Anne D. Nenneau
CCN International

Robert J. Tewksbury
Pearl Technologies, Inc.

PENN YAN

Bonnie B. Curbeau
Curbeau Realty

Jeffrey M. Kennedy
Morgan Marine

James H. Long
Longs' Cards and Books

Paul W. Marble, Jr.
Marble's Automotive and Glass

Henry H. Martin
Town of Benton Dairy Farmer

Steven D. Perry
Knapp & Schlappi Lumber Co., Inc.

Neil J. Simmons
Simmons Vineyards

PERINTON PARK

John A. Colaruotolo
ANCO Builders, LLC

Samuel A. DiPrima
DiPrima Properties, LLC

Arthur S. Elting
Country Rode Motowerks

Donald R. Fox, Esq.
Partner, Evans & Fox, LLP

Howard I. Sharp
RV & E Bike and Skate

J. Lincoln Swedrock, P.E.
BME Associates

SENECA COUNTY

Salvatore N. Franzone
Ciccino's Pizzeria and Restaurant

Rodney D. Littlejohn, DDS, MS
Littlejohn Orthodontics

Kenneth W. Padgett, DO
Past President & Current Chancellor of NYCC

Eugene F. Pierce
Glenora Wine Cellars, Inc. and Knapp Winery

Robert L. Sessler
Retired, Sessler Companies

Raymond A. Tuuri, Jr.
Finger Lakes Equipment Rental

Stephen J. Wadhams
Wadhams Enterprises, Inc.

WE'RE PEOPLE-FOCUSED

Hometown banking is an exceptional customer experience.

We pride ourselves on delivering a welcoming and highly personalized banking experience.

Executive Management

Robert A. Schick
Chairman of the Board & Chief Executive Officer

Thomas L. Kime
President

Clair J. Britt, Jr.
Executive Vice President & Chief Commercial Loan Officer

Phillip M. McCann
Executive Vice President & Chief Risk Officer

Stephen V. DeRaddo
Executive Vice President & Chief Development Officer

Kelly J. Mittiga
Executive Vice President & Chief Performance Officer

Todd F. Juffs
Senior Vice President & Chief Technology Officer

Chad J. Proper
Vice President & Chief Financial Officer

Bank Officers and Supervisors

ADMINISTRATION

Robert A. Schick
Chairman of the Board & Chief Executive Officer

Thomas L. Kime
President

Kelly J. Mittiga
Executive Vice President & Chief Performance Officer

Carol A. Snook
Banking Officer & Corporate/Executive Secretary

AUDIT

Ruth M. Columbus
Vice President & Director of Internal Audit

Melonie L. Tiffany
Assistant Vice President & Senior Auditor

BRANCH DIVISION

Stephen V. DeRaddo
Executive Vice President & Chief Development Officer

Susan K. Andersen
Senior Vice President & Director of Branch & Market Management

Jeffrey A. Friend
Senior Vice President & Director of Branch & Market Management

Thomas D. Muller
Senior Vice President

Demetrius Murphy
Vice President & Branch Manager – Auburn

James S. Bilotta
Assistant Vice President & Branch Manager – Perinton Park

Jarrod M. Crawford
Assistant Vice President & Cash Management/E-Business Solutions Officer

Julieann B. Downey
Assistant Vice President & Branch Manager – Lyons

William L. Dungey
Assistant Vice President & Branch Manager – Clyde and Jordan

Steven J. Hasseler
Assistant Vice President & Branch Manager – Newark

Jessica L. Mullins
Assistant Vice President & Branch Manager – Penn Yan

Charles K. Parkhurst
Assistant Vice President & Branch Manager – Canandaigua

Bank Officers and Supervisors CONT.

Emily E. Hilimire
Assistant Vice President & Branch Manager – Seneca County

Tara R. Rago
Assistant Vice President & Branch Manager – Geneva

Jean E. Tsepas
Assistant Vice President & Branch Manager – Ontario

Sherri A. Viele
Assistant Vice President & Branch Manager – Wolcott

Michele L. Waeghe
Assistant Vice President & Branch Manager – Macedon

Cathy J. DeMay
Banking Officer & Assistant Branch Manager – Ontario

Heidi E. King
Banking Officer & Assistant Branch Manager – Canandaigua

Susan L. Snyder
Banking Officer & Assistant Branch Manager – Penn Yan

COMMERCIAL LENDING

Clair J. Britt, Jr.
Executive Vice President & Chief Commercial Loan Officer

Anna M. Bridger
Vice President & Commercial Loan Officer

Stephen V. D'Orazio
Vice President & Commercial Loan Officer

Mark J. DeBacco
Vice President & Commercial Loan Officer

Ryan M. Hallings
Vice President & Agricultural/Commercial Loan Officer

James H. King
Vice President & Commercial Loan Officer

Scott A. MacKenzie
Vice President & Agricultural/Commercial Loan Officer

Gregory G. Lattimore
Assistant Vice President & Commercial Loan Officer

Michael E. Rusinko
Assistant Vice President & Small Business Development Officer

Kraig M. vonHahmann
Assistant Vice President & Agricultural/Commercial Loan Officer

CREDIT ADMINISTRATION & COMPLIANCE

Phillip M. McCann
Executive Vice President & Chief Risk Officer

Pamela J. Lee
Vice President & Portfolio Monitoring Officer

Joyce A. Marble
Assistant Vice President & Compliance/BSA Officer

Amanda M. McDonald
Assistant Vice President & Senior Credit Underwriter

FINANCE

Chad J. Proper
Vice President & Chief Financial Officer

Shannon M. Romano
Assistant Vice President & Senior Assistant Controller

MARKETING

Barbara H. Taney
Assistant Vice President & Director of Marketing

HUMAN RESOURCES

Kimberly A. Kelley
Vice President & Director of Human Resources

SECURITY/FACILITIES

Michael J. Colacino
Vice President & Director of Security & Facilities

TRAINING

Deborah A. Odell
Vice President & Director of Training

RETAIL & RESIDENTIAL MORTGAGE LENDING

Joshua N. Miller
Senior Vice President & Director of Retail Lending

Robert T. MacDonnell
Vice President & Consumer Loan Officer/Underwriter

Joseph M. Arbogast
Assistant Vice President & Mortgage Originator

Timothy H. Lead
Assistant Vice President & Mortgage Underwriter II

James M. Allison
Banking Officer & Mortgage Originator

Valorie A. Heinzman
Assistant Vice President & Mortgage Originator

Trisha A. Mastrodonato
Banking Officer & Mortgage Originator

Angela M. Merola
Assistant Vice President & Senior Collector

Craig R. Mietz
Banking Officer & Mortgage Originator

Matthew C. Morales
Banking Officer & Mortgage Underwriter II

Craig A. Schojan
Assistant Vice President & Mortgage Underwriter II

OPERATIONS & IT

Todd F. Juffs
Senior Vice President & Chief Technology Officer

Trevor Thomas
Senior Vice President & Director of Operations

Hope A. Alexanian
Assistant Vice President & Retail Loan Operations Supervisor

Cheryl M. Graham
Assistant Vice President & Deposit Operations Supervisor

Lynnette M. Zelias
Assistant Vice President & Commercial Loan Operations Supervisor

Karen D. Lombardozzi
Banking Officer & Systems Administrator

FINANCIAL SERVICES

Robert T. Koczent
Vice President & Director of Financial Services

David J. DeRaddo, CFP®
Banking Officer & Financial Services Representative

Celebrating WOW!

Our commitment to going the extra mile is celebrated quarterly through WOW! recognition awards and annually at our employee event. Congratulations to all staff members for their focus on customer service and to those who received special acknowledgment for their efforts.

WOW! 2017 Recognitions: *Standing with Robert Schick are Charles Parkhurst—Breakthrough Employee of the Year (left), and Valorie Heinzman—Employee of the Year, Ben Feidner—Rookie of the Year (right)*

2017 QUARTERLY WOW! WINNERS

Quarter 1

Devin Cobb—Floating Head Teller

Quarter 2

LeeAnna Hernandez—Macedon
Jennifer Goatseay—Deposit Operations

Quarter 3

Schyler Madsen—Canandaigua

Quarter 4

Anthony Valenti—Geneva
Caitlin Cieri—Deposit Operations
Diane McKinney—Accounting

Cultivating From Within

LNB is pleased to announce the promotion of several exceptional team members whose drive, hard work, and commitment to excellence make LNB not only a stronger organization, but a better place. If you see them, please be sure to congratulate them.

Valorie A. Heinzman
Assistant Vice President and Mortgage Originator

Promoted from Banking Officer and Mortgage Originator II

Trisha A. Mastrodonato
Banking Officer and Mortgage Originator

Promoted from Mortgage Originator II

Angela M. Merola
Assistant Vice President and Senior Collector

Promoted from Banking Officer and Senior Collector

Matthew C. Morales
Banking Officer and Mortgage Underwriter II

Promoted from Mortgage Underwriter II

Craig A. Schojan
Assistant Vice President and Mortgage Underwriter II

Promoted from Banking Officer and Mortgage Underwriter II

Barbara H. Taney
Assistant Vice President and Director of Marketing

Promoted from Banking Officer and Director of Marketing

Announcing New Leadership Roles

Ryan Hallings and Scott MacKenzie were recently tapped as team leaders in the Lending Department. As Commercial/Agricultural Loan Officers, each will bring their experience and expertise to their respective territories.

Ryan M. Hallings
Vice President & Commercial/Agricultural Loan Officer

Team Leader - Greater Penn Yan & Canandaigua markets

Scott A. MacKenzie
Vice President & Commercial/Agricultural Loan Officer

Team Leader - Eastern Ontario, Seneca and Cayuga counties

WE'RE HIGH-TOUCH AND HIGH-TECH

Hometown banking is personalized service and high-tech convenience.

LNB offers a complete suite of banking services at its full-service offices, in addition to the latest online and mobile banking technologies.

LNB Brings Hometown Banking to Cayuga County

On July 6, 2017, LNB broke ground at the site of the new full-service Grant Avenue office.

2017 marked LNB's official entry into a new market—Cayuga County. With the opening of its full-service downtown office in the spring of 2017 and the groundbreaking for its new two-story Grant Avenue location, LNB has wholeheartedly committed to serving the Auburn community.

"We are very excited to be in Auburn," said Thomas L. Kime, President at LNB. "The feedback we have already received from community members has been exceedingly positive. The community has seen a great deal of change among their banks, and I have no doubt our hometown-style of community banking will continue to prove to be a perfect fit for the area."

Since LNB first entered the market, its dedicated local staff has been focused on serving the community and demonstrating the difference hometown banking can make. Branch Manager and Auburn native Demetrius Murphy has a passion for exceeding customer expectations. Commercial Loan Officer Gregory Lattimore, Mortgage Originator Craig Mietz, and Agricultural/Commercial Loan Officer Kraig vonHahmann, work directly with Bank customers to ensure all needs are met.

"I'm thrilled to be part of LNB's expansion," said Murphy. "We have assembled a great team of people, and we are pleased to provide the quality products and services to the residents and businesses of my hometown."

Along with hiring local staff, LNB has partnered with area business and community leaders who share a passion for serving the Auburn community, including Joseph P. Bartolotta, Esq., from R&M Real Estate Group; Richard L. Beauchine, CPA, from Waterloo Container; John F. Bouck from Bouck Real Estate; Mark A. DiVietro, O.D., from Silbert Optical; Salvatore N. Franzone from Ciccino's Pizzeria and Restaurant; and Wendy C. LaDuca from Reflections Medical and Cosmetic Dermatology. These individuals provide insight and feedback that help keep LNB well-aligned with the local economy and with people of the community.

"To us, hometown banking is more than service with a smile," said Tom Kime. "We immerse ourselves on a local level by taking on leadership roles within local organizations, hiring local staff members, partnering with local businesses, and making local decisions—all for the betterment of the community and its continued economic growth."

Rendering of LNB's new Grant Avenue office.

STRONG VALUES • SOLID GROWTH

Lyons Bancorp, Inc.
It's all about people.

2017
FINANCIAL REPORT

Mission

The Lyons National Bank is an independent, hometown, community bank with an expanding geographic market. Our mission is to safely and profitably serve all of our customers and communities with the most professional service available. We will accomplish this by making a commitment to our most valuable assets—our employees—to treat them with integrity, compensate them appropriately and provide them with the necessary systems, technology, and appropriate training to enable them to become well-respected professionals. Our employees, in turn, will provide our growing customer base with superior service and respect and will be leaders in promoting the quality of life in the communities we serve.

Vision

The vision of The Lyons National Bank is to be the employer and financial institution of choice and to foster an environment of opportunity, growth, and prosperity for our employees, customers, shareholders, and local communities.

Profile

Lyons Bancorp, Inc. is a financial holding company headquartered in Lyons, New York, with assets of $1.03 billion at December 31, 2017. Lyons Bancorp, Inc. has one banking subsidiary, The Lyons National Bank. The Lyons National Bank is a community bank with offices in Clyde, Lyons, Macedon, Newark, Ontario, and Wolcott in Wayne County, Jordan in Onondaga County, Canandaigua and Geneva in Ontario County, Penn Yan in Yates County, Waterloo in Seneca County, Fairport in Monroe County, and Auburn in Cayuga County. The Lyons National Bank has one subsidiary, Lyons Realty Associates Corp.

Our Culture—WOW!

WOW! is a personal conviction to consciously provide our customers and fellow employees with a level of service that exceeds their expectations during each and every encounter we have with them.

Annual Meeting

The annual meeting of the stockholders will take place at 4:30 p.m. on May 16, 2018, at the historic Ohmann Theatre in Lyons, New York.

Lyons Bancorp, Inc.

Consolidated Financial Report

December 31, 2017

Bonadio & Co., LLP
Certified Public Accountants

Table of Contents December 31, 2017 and 2016

Bonadio & Co., LLP
Certified Public Accountants

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

March 2, 2018

To the Board of Directors and
Stockholders of Lyons Bancorp Inc.:

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Lyons Bancorp Inc. and subsidiary as of December 31, 2017 and 2016, and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for the years then ended, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Lyons Bancorp Inc. and subsidiary as of December 31, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These consolidated financial statements are the responsibility of Lyons Bancorp Inc. and subsidiary's management. Our responsibility is to express an opinion on Lyons Bancorp Inc. and subsidiary's consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to Lyons Bancorp Inc. and subsidiary in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB and in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

We have served as Lyons Bancorp Inc. and subsidiary's auditor since 2011.

Bonadio & Co., LLP

432 North Franklin Street, Suite 60
Syracuse, New York 13204
p (315) 476-4004
f (315) 475-1513

www.bonadio.com

Lyons Bancorp, Inc.

Consolidated Balance Sheets

December 31, 2017 and 2016

Assets	2017	2016
	(In thousands)	
Cash and due from banks	**$ 13,638**	$ 14,458
Interest-bearing deposits in banks	**19,596**	17,952
Cash and Cash Equivalents	**33,234**	32,410
Investment securities:		
Available for sale	**206,342**	142,983
Held to maturity	**-**	56,826
Restricted equity securities	**7,340**	5,792
Total Investment Securities	**213,682**	205,601
Loans	**741,860**	678,691
Less allowance for loan losses	**(8,629)**	(7,796)
Net Loans	**733,231**	670,895
Land, premises and equipment, net	**23,279**	20,097
Bank owned life insurance	**16,000**	15,610
Accrued interest receivable and other assets	**12,418**	11,519
Total Assets	**$ 1,031,844**	$ 956,132
Liabilities and Equity		
Liabilities		
Deposits:		
Interest-bearing	**$ 679,748**	$ 663,519
Non-interest-bearing	**213,508**	196,554
Total Deposits	**893,256**	860,073
Borrowings from Federal Home Loan Bank	**50,000**	18,000
Junior subordinated debentures	**6,190**	6,190
Accrued interest payable and other liabilities	**8,554**	3,015
Total Liabilities	**958,000**	887,278
Equity		
Lyons Bancorp, Inc. stockholders' equity:		
Preferred stock	**3**	3
Common stock	**1,599**	1,599
Paid-in capital	**19,317**	19,294
Retained earnings	**57,693**	52,449
Accumulated other comprehensive loss	**(4,527)**	(4,270)
Treasury stock, at cost	**(297)**	(277)
Total Lyons Bancorp, Inc. Stockholders' Equity	**73,788**	68,798
Noncontrolling interest	**56**	56
Total Equity	**73,844**	68,854
Total Liabilities and Equity	**$ 1,031,844**	$ 956,132

See notes to consolidated financial statements.

Lyons Bancorp, Inc.

Consolidated Statements of Income

Years Ended December 31, 2017 and 2016

	2017	2016
	(In thousands, except per share data)	
Interest Income		
Loans	**$ 30,607**	$ 27,297
Investment securities:		
Taxable	**3,591**	3,486
Non-taxable	**1,502**	1,456
Total Interest Income	**35,700**	32,239
Interest Expense		
Deposits	**3,410**	3,699
Borrowings	**571**	514
Total Interest Expense	**3,981**	4,213
Net Interest Income	**31,719**	28,026
Provision for Loan Losses	**1,500**	1,100
Net Interest Income after Provision for Loan Losses	**30,219**	26,926
Noninterest Income		
Service charges on deposit accounts	**3,036**	2,888
Cardholder fees	**2,223**	1,973
Financial services fees	**1,022**	855
Loan servicing fees	**1,540**	1,410
Net realized (losses) gains from sales of securities	**(17)**	470
Realized gains on loans sold	**1,180**	1,275
Earnings on investment in bank owned life insurance	**389**	416
Other	**467**	420
Total Noninterest Income	**9,840**	9,707
Noninterest Expense		
Salaries and wages	**11,757**	10,719
Pensions and benefits	**3,806**	3,481
Occupancy	**2,620**	2,828
Data processing	**1,867**	1,615
Professional fees	**1,825**	1,562
FDIC and OCC assessments	**733**	740
Advertising	**942**	952
Cardholder expense	**1,106**	845
Office supplies	**274**	277
Other	**3,019**	3,072
Total Noninterest Expense	**27,949**	26,091
Income before Income Taxes	**12,110**	10,542
Income Tax Expense	**4,096**	2,941
Net income attributable to noncontrolling interest and Lyons Bancorp, Inc.	**8,014**	7,601
Net income attributable to noncontrolling interest	**5**	5
Net income attributable to Lyons Bancorp, Inc.	**8,009**	7,596
Preferred stock dividends	**250**	-
Net Income available to common shareholders	**$ 7,759**	$ 7,596
Earnings Per Share – basic	**$ 2.43**	$ 2.42
Earnings Per Share – diluted	**$ 2.42**	$ 2.39

See notes to consolidated financial statements.

Consolidated Statements of Comprehensive Income
Years Ended December 31, 2017 and 2016

	2017	2016
	(In thousands)	
Net income	**$8,009**	$ 7,596
Other comprehensive income (loss) :		
Securities available for sale:		
Net unrealized losses during the year	**(219)**	(3,042)
Reclassification adjustment for transfer from held to maturity	**(165)**	-
Reclassification adjustment for (gains) losses included in income	**17**	(470)
Securities held to maturity:		
Reclassification adjustment for amortization of unrealized losses included in income	**136**	262
Changes in unrealized gains during the year of restricted equity securities	**42**	51
Pension and postretirement benefits:		
Amortization of prior service credit	**(3)**	(3)
Amortization of net loss	**233**	199
Net actuarial gain (loss)	**761**	(28)
Cash flow hedge:		
Gains (losses) on the effective portion of cash flow hedge	**10**	(26)
Reclassification adjustment for losses included in income	**151**	177
	963	(2,880)
Tax (expense) benefit	**(385)**	1,153
Other comprehensive income (loss)	**578**	(1,727)
Comprehensive income	**$ 8,587**	$ 5,869

See notes to consolidated financial statements.

Consolidated Statements of Stockholders' Equity
Years Ended December 31, 2017 and 2016

(In thousands, except per share data)

	Preferred Stock	Common Stock	Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Noncontrolling Interest	Total
Balance - January 1, 2016	-	$1,507	$11,840	$48,032	$(2,540)	$(217)	$56	$ 58,678
Net income attributable to noncontrolling interests and Lyons Bancorp, Inc.	-	-	-	7,596	-	-	5	7,601
Total other comprehensive loss, net	-	-	-	-	(1,730)	-	-	(1,730)
Conversion of trust preferred securities	-	92	2,489	-	-	-	-	2,581
Issuance of preferred stock	3	-	4,928	-	-	-	-	4,931
Purchase of treasury stock	-	-	-	-	-	(243)	-	(243)
Deferred compensation shares awarded, net	-	-	37	-	-	183	-	220
Dividends to noncontrolling interests	-	-	-	-	-	-	(5)	(5)
Cash dividends declared, $1.01 per share	-	-	-	(3,179)	-	-	-	(3,179)
Balance – December 31, 2016	3	1,599	19,294	52,449	(4,270)	(277)	56	$ 68,854
Net income attributable to noncontrolling interests and Lyons Bancorp, Inc.	-	-	-	8,009	-	-	5	8,014
Total other comprehensive income, net	-	-	-	-	578	-	-	578
Reclassification of stranded tax effect [1]	-	-	-	835	(835)	-	-	-
Purchase of treasury stock	-	-	-	-	-	(183)	-	(183)
Deferred compensation shares awarded, net	-	-	23	-	-	163	-	186
Dividends to noncontrolling interests	-	-	-	-	-	-	(5)	(5)
Preferred cash dividends declared, $50.00 per share	-	-	-	(250)	-	-	-	(250)
Cash dividends declared, $1.05 per share	-	-	-	(3,350)	-	-	-	(3,350)
Balance – December 31, 2017	$ 3	$ 1,599	$ 19,317	$ 57,693	$ (4,527)	$ (297)	$ 56	$ 73,844

(1) Reclassification adjustment from accumulated other comprehensive loss to retained earnings for stranded tax effects resulting from the newly enacted Federal corporate income tax rate of 21% in accordance with the early adoption of ASU 2018-02.

Consolidated Statements of Cash Flows

Years Ended December 31, 2017 and 2016

	2017	2016
	(In thousands)	
Cash Flows from Operating Activities		
Net income	**$ 8,009**	$ 7,596
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	**1,500**	1,100
Earnings on investment in bank owned life insurance	**(390)**	(415)
Net realized (gain) loss from sales of securities	**17**	(470)
Realized on loans sold	**(1,180)**	(1,275)
Gain on sale of real estate owned and other repossessed assets	**-**	(11)
Deferred compensation expense	**27**	291
Net amortization on securities	**419**	511
Depreciation and amortization	**1,099**	1,146
Deferred income tax expense (benefit)	**2,763**	(7)
Contribution to defined benefit pension plan	**(2,400)**	(1,000)
Increase in accrued interest receivable and other assets	**(1,868)**	(84)
Increase (decrease) in accrued interest payable and other liabilities	**6,986**	(4,276)
Loans originated for sale	**(66,357)**	(61,663)
Proceeds from sales of loans	**63,487**	62,558
Net Cash Provided by Operating Activities	**12,112**	4,001
Cash Flows from Investing Activities		
Purchases of securities available for sale	**(108,858)**	(98,694)
Proceeds from sales of securities available for sale	**-**	54,215
Proceeds from maturities and calls of securities available for sale	**92,413**	36,207
Purchases of held to maturity securities	**(850)**	(20,580)
Proceeds from maturities/sales of securities held to maturity	**10,107**	15,099
Net increase in restricted equity securities	**(1,506)**	(164)
Proceeds from sales of commercial loans	**-**	1,266
Net increase in portfolio loans	**(59,779)**	(75,736)
Proceeds from sale of real estate owned, net and other repossessed assets	**-**	137
Purchase of bank owned life insurance	**-**	(300)
Premises and equipment purchases, net	**(4,280)**	(363)
Net Cash Used in Investing Activities	**(72,753)**	(88,913)
Cash Flows from Financing Activities		
Net increase in demand and savings deposits	**10,214**	92,491
Net increase (decrease) in time deposits	**22,969**	(4,529)
Net increase in overnight borrowings from Federal Home Loan Bank	**32,000**	6,000
Repayment of term borrowings from Federal Home Loan Bank	**-**	(8,126)
Preferred stock dividend	**(250)**	-
Net proceeds from sale of stock	**-**	4,931
Purchase of treasury stock	**(183)**	(243)
Dividends paid	**(3,285)**	(2,983)
Net Cash Provided by Financing Activities	**61,465**	87,541
	824	2,629
Cash and Cash Equivalents – Beginning	**32,410**	29,781
Cash and Cash Equivalents – Ending	**$ 33,234**	$ 32,410
Supplementary Cash Flow Information		
Interest paid	**$ 3,970**	$ 4,226
Income taxes paid, net of refund received	**$ 1,474**	$ 3,104
Non-cash Disclosure		
Transfer of loans to foreclosed real estate and other repossessed assets	**$ -**	$ 271
Conversion of Trust III debentures to common stock	**$ -**	$ 2,582

See notes to consolidated financial statements.

Note 1 - Summary of Significant Accounting Policies

Nature of Operations

Lyons Bancorp, Inc. (the Company) provides a full range of commercial and retail banking services to individual and small business customers through its wholly-owned subsidiary, The Lyons National Bank (the Bank). The Bank's operations are conducted in fourteen branches located in Wayne, Onondaga, Yates, Ontario, Monroe, Seneca and Cayuga Counties, New York. The Company and the Bank are subject to the regulations of certain federal agencies and undergo periodic examinations by those regulatory authorities.

The Company owns all of the voting common shares of Lyons Capital Statutory Trust I (Trust I), Lyons Capital Statutory Trust II (Trust II), and Lyons Statutory Trust IV (Trust IV). Trust I was formed in 2003, Trust II was formed in 2004, and Trust IV was formed in 2016. The Trusts were each formed for the purpose of securitizing trust preferred securities, the proceeds of which were advanced to the Company and contributed to the Bank as additional capital.

The Bank owns all of the voting stock of Lyons Realty Associates Corp. (LRAC). LRAC is a real estate investment trust which holds a portfolio of real estate mortgages. In order to maintain its status as a real estate investment trust, LRAC holds the real estate mortgages until they are paid. The real estate mortgages held by LRAC are included in loans on the consolidated balance sheet.

Basis of Presentation

The consolidated financial information included herein combines the results of operations, the assets, liabilities, and shareholders' equity (including comprehensive income or loss) of the Company and all entities in which the Company has a controlling financial interest. All significant intercompany balances and transactions are eliminated in consolidation.

Variable interest entities (VIEs) are required to be consolidated if it is determined the company is the primary beneficiary of a VIE. The primary beneficiary of a VIE is the enterprise that has both the power and ability to direct the activities of the VIE that most significantly impact the VIE's economic performance and an obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE. The Company's wholly owned subsidiaries, Trust I, Trust II, and Trust IV are VIE's for which the Company is not the primary beneficiary. Accordingly, the accounts of these entities are not included in the Company's consolidated financial statements, as discussed in Note 8.

Reclassification

Amounts in the prior years' consolidated financial statements are reclassified when necessary to conform to the current year's presentation.

Note 1 - Summary of Significant Accounting Policies (Continued)

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near future relate to the determination of the allowance and provision for loan losses, actuarial assumptions associated with the Company's benefit plans and deferred tax assets and liabilities.

Recently Issued Accounting Pronouncements

Accounting Standards Update 2018-02 – Income Statement – Reporting Comprehensive Income amends ASC 220. This allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. ASU 2018-02 was implemented December 31, 2017.

Investment Securities

Securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them until maturity. Securities to be held for indefinite periods of time are classified as available for sale and carried at fair value, with the unrealized holding gains and losses reported as a component of other comprehensive income, net of tax. Securities held for resale for liquidity purposes are classified as trading and are carried at fair value, with changes in unrealized holding gains and losses included in income. Management determines the appropriate classification of securities at the time of purchase. Restricted equity securities consist primarily of Federal Reserve Bank and the Federal Home Loan Bank stock.

Purchase premiums and discounts are recognized in interest income using the interest method or methods that approximate the interest method over the terms of the securities. Interest and dividends on securities are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are determined using the specific identification method.

On a quarterly basis, the Company performs an assessment to determine whether there have been any events or economic circumstances indicating that a security with an unrealized loss has suffered other-than-temporary impairment. A security is considered impaired if the fair value is less than its amortized cost basis at the reporting date. If impaired, the Company then assesses whether the unrealized loss is other-than-temporary. The assessment considers (i) whether the Company intends to sell the security prior to recovery and/or maturity, (ii) whether it is more likely than not that the Company will have to sell the security prior to recovery and/or maturity and (iii) if the present value of the expected cash flows is not sufficient to recover the entire amortized cost basis. If a debt security is deemed to be other-than-temporarily impaired, the credit loss component of an other-than-temporary impairment write-down is recorded in earnings while the remaining portion of the impairment loss is recognized, net of tax, in other comprehensive income provided that the Company

Note 1 - Summary of Significant Accounting Policies (Continued)
Investment Securities (Continued)

does not intend to sell the underlying security and it is more-likely-than not that the Company would not have to sell the security prior to recovery.

The Company considers the following factors in determining whether a credit loss exists and the period over which the security is expected to recover:

- The length of time and the extent to which the fair value has been less than the amortized cost basis;
- The level of credit enhancement provided by the structure which includes, but is not limited to, credit subordination positions, excess spreads, overcollateralization, protective triggers;
- Changes in the near term prospects of the issuer or underlying collateral of a security, such as changes in default rates, loss severities given default and significant changes in prepayment assumptions;
- The level of excess cash flow generated from the underlying collateral supporting the principal and interest payments of the debt securities; and
- Any adverse change to the credit conditions of the issuer of the security such as credit downgrades by the rating agencies.

Loans

The Bank grants real estate, commercial and consumer loans to its customers. A substantial portion of the loan portfolio is represented by real estate loans in Wayne, Ontario, Monroe, Yates, Onondaga, Seneca and Cayuga Counties. The Company's loan portfolio includes residential real estate, commercial real estate, agricultural real estate, commercial and agricultural loans, and consumer installment classes. Residential real estate loans include classes for 1-4 family and home equity loans. Consumer installment loans include classes for direct and indirect loans.

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

Interest income is accrued on the unpaid principal balance. The accrual of interest on loans is discontinued at the time the loan is 90 days past due unless the credit is well-secured and in process of collection. Credit card loans and other personal loans are typically charged off no later than 180 days past due. Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual or charged off is

Note 1 - Summary of Significant Accounting Policies (Continued)
Loans - continued

reversed against interest income or the allowance for loan losses if the interest income was earned in a prior period. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Management, considering current information and events regarding the borrowers' ability to repay their obligations, considers a loan to be impaired when it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. When a loan is considered to be impaired, the amount of the impairment is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or at the loan's observable fair value or the fair value of underlying collateral if the loan is collateral-dependent. Impairment losses are included in the allowance for loan losses through a charge to the provision for loan losses. Cash receipts on impaired loans are generally applied to reduce the principal balance outstanding. In considering loans for evaluation of impairment, management generally excludes smaller balance, homogeneous loans: residential mortgage loans, home equity loans, and all consumer loans, unless subject to a troubled debt restructuring. These loans are collectively evaluated for risk of loss.

Loans Held for Sale

Generally, loans held for sale consist of residential mortgage loans that are originated and are intended to be sold through agreements the Bank has with the Federal Home Loan Bank (FHLB) and the Federal Home Loan Mortgage Corporation (Freddie Mac). Realized gains and losses on sales are computed using the specific identification method. These loans are carried on the consolidated balance sheet at the lower of cost or estimated fair value determined in the aggregate. Residential loans held for sale totaled $5.3 million and $1.2 million at December 31, 2017 and 2016, respectively, and are included in loans on the consolidated balance sheets.

During 2017 and 2016, the Company sold residential mortgage loans totaling $63.5 million and $62.6 million, respectively, and realized gains on these sales were $1.2 million and $1.2 million, respectively. These residential real estate loans are generally sold without recourse in accordance with standard secondary market loan sale agreements. When residential mortgage loans are sold, the Company typically retains all servicing rights, which provides the Company with a source of fee income. In connection with the sales in 2017 and 2016, the Company recorded mortgage-servicing assets of $586,000 and $589,000, respectively. Amortization of mortgage-servicing assets amounted to $246,000 in 2017 and $247,000 in 2016. Net mortgage-servicing assets included in the consolidated balance sheets totaled $1.6 million and $1.3 million, net of amortization, as of December 31, 2017 and 2016, respectively.

Government-guaranteed loans which may be sold after origination are not classified as held for sale in as much as sale of such loans is largely dependent upon the extent to which gains may be realized.

During 2017, the Company sold no commercial loans. During 2016, the Company sold commercial loans backed by Small Business Administration guarantees totaling $1.1 million, and realized gains on these sales were $72,000. There were no commercial loans held for sale at December 31, 2017 or 2016.

Note 1 - Summary of Significant Accounting Policies (Continued)

Loans Held for Sale - continued

Total loans serviced for others amounted to $302.9 million and $269.3 million at December 31, 2017 and 2016, respectively.

Allowance for Loan Losses

The allowance for loan losses (allowance) is established as losses are estimated to have occurred in the loan portfolio. The allowance is recorded 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 evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of general, specific and unallocated components as further described below.

General Component

The general component of the allowance is based on historical loss experience adjusted for qualitative factors stratified by the following loan classes: residential real estate, commercial real estate, agricultural real estate, commercial and agricultural loans, and consumer installment segments. Management uses a rolling average of historical losses based on a time frame appropriate to capture relevant loss data for each loan class. The historical loss factor is adjusted for the following qualitative factors: levels and trends in delinquencies; trends in volume and terms of loans; effects of changes in risk selection and underwriting standards and other changes in lending policies, procedures and practices; experience/ability/depth of lending management and staff; and national and local economic trends and conditions. There were no changes in the Company's policies or its methodology pertaining to the general component of the allowance during 2017 or 2016.

The qualitative factors are determined based on the various risk characteristics of each loan type. Risk characteristics relevant to each loan type are as follows:

Residential real estate - The Company generally does not originate loans with a loan-to-value ratio greater than 80 percent and does not grant subprime loans. The majority of loans in this segment are collateralized by owner-occupied residential real estate and repayment is dependent on the credit quality of the individual borrower. The overall health of the economy, including unemployment rates and housing prices, will have an effect on the credit quality in this class.

Commercial real estate - Loans in this class represent both extensions of credit for owner-occupied real estate and income-producing properties throughout the local region. The underlying cash flows of the operating commercial businesses (owner-occupied) and income properties (non-owner

Note 1 - Summary of Significant Accounting Policies (Continued)

Allowance for Loan Losses - continued

occupied) can be adversely impacted by a downturn in the economy as evidenced by increased vacancy rates, which in turn, will have an effect on the credit quality in this class. In a majority of cases, the Company obtains rent rolls annually and continually monitors the cash flows of non-owner occupied loans commensurate with sound lending practices.

Agricultural real estate – Loans in this class represent extensions of credit for owner-occupied agricultural real estate throughout the local region. The underlying cash flows generated by the agribusinesses can be adversely impacted by adverse climate and a weakened economy, which in turn, will have an effect on the credit quality in this class. Management obtains annual tax returns and continually monitors the cash flows of these loans commensurate with sound lending practices.

Commercial and Agricultural loans – Loans in these classes are made to businesses and generally secured by the assets of the business. Repayment is expected from the cash flows of the business. A weakened economy, and resultant decreased consumer spending, will have an effect on the credit quality in this class.

Consumer installment loans – Loans in this segment may be secured or unsecured and repayment is dependent on the credit quality of the individual borrower. Unemployment rates will have an effect on the credit quality in this class.

Specific Component

The specific component relates to loans that are classified as impaired. Impairment is measured on a loan by loan basis for commercial and agricultural loans, commercial real estate and agricultural real estate by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral, less costs to sell, if determined to be more appropriate. An allowance is established when the discounted cash flow or collateral value of the impaired loan is lower than the carrying value of that loan. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer or residential real estate loans for impairment disclosures, unless such loans are subject to a troubled debt restructuring agreement.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable 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.

All impaired loans require appraisals and/or chattel evaluations within 180 days of impairment, unless existing evaluation is less than 24 months old and no market or physical deterioration is noted. Re-appraisals and/or re-evaluations are conducted whenever deemed appropriate, but typically performed on a 24-month cycle if repayment is predicated upon liquidation of collateral and evidence suggests collateral values may have deteriorated.

Note 1 - Summary of Significant Accounting Policies (Continued)

Allowance for Loan Losses - continued

Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reason for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Unallocated Component

An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating allocated and general reserves in the portfolio.

Troubled Debt Restructurings

A modification of a loan constitutes a troubled debt restructuring ("TDR") when a borrower is experiencing financial difficulty and the modification constitutes a concession. Loans modified in a TDR often involve temporary interest-only payments, term extensions, reducing the interest rate for the remaining term of the loan, extending the maturity date at an interest rate lower than the current market rate for new debt with similar risk, requesting additional collateral, releasing collateral for consideration, or substituting or adding a new borrower or guarantor.

Nonaccrual loans that are restructured remain on nonaccrual status, but may move to accrual status after they have performed according to the restructured terms for a period of time of at least six months.

Land, Premises and Equipment

Land is stated at cost. Premises and equipment are recorded at cost and are generally depreciated by the straight-line method over the estimated useful lives of the assets. Buildings are generally depreciated over a useful life of thirty-nine and one half years, furniture and equipment over a useful life of three to seven years, and leasehold improvements over the lesser of the asset's useful life or the term of the lease.

Bank Owned Life Insurance

Bank owned life insurance (BOLI) was purchased by the Bank as a financing tool for employee benefits and to fund discriminatory retirement benefits for the Board of Directors and executive management. The value of life insurance financing is the tax preferred status of increases in life insurance cash values and death benefits and the cash flow generated at the death of the insured. The proceeds or increases in cash surrender value of the life insurance policy results in tax-exempt income to the Company. The largest risk to the BOLI program is credit risk of the insurance carriers. To mitigate this risk, annual financial condition reviews are completed on all carriers. BOLI is stated on the Company's consolidated balance sheets at its current cash surrender value. Increases in BOLI's

Note 1 - Summary of Significant Accounting Policies (Continued)

Bank Owned Life Insurance – continued

cash surrender value are reported as noninterest income in the Company's consolidated statements of income.

Foreclosed Real Estate

Included in other assets are real estate properties acquired through, or in lieu of, loan foreclosure. These properties are initially recorded at fair value less estimated selling costs at the date of foreclosure. Any write-downs based on the asset's fair value at date of foreclosure are charged to the allowance for loan losses. After foreclosure, property held for sale is carried at the lower of the new basis or fair value less any costs to sell. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. Valuations are periodically performed by management, and any subsequent write-downs are recorded as a charge to operations, if necessary, to reduce the carrying value of the property to the lower of its cost or fair value less cost to sell. The recorded investment in real estate in process of foreclosure at December 31, 2017 and 2016 was approximately $211,000 and $271,000, respectively. There was no foreclosed real estate at December 31, 2017 or 2016.

Treasury Stock

Treasury stock is recorded at cost. Shares are reissued on the average cost method on a first in, first out basis, except for issuance of deferred compensation shares, which are discussed in Note 11.

Interest Rate Swap Agreement

The Company utilizes an interest rate swap agreement as part of its management of interest rate risk to modify the repricing characteristics of its floating-rate junior subordinate debentures. For this swap agreement, amounts receivable or payable are recognized as accrued under the terms of the agreement, and the net differential is recorded as an adjustment to interest expense of the related debentures. The interest rate swap agreement is designated as a cash flow hedge. Therefore, the effective portion of the swap's unrealized gain or loss was initially recorded as a component of other comprehensive income, net of tax. The ineffective portion of the unrealized gain or loss, if any, is immediately reported in other operating income. The Company considers its interest rate swap agreement to be fully effective and accordingly it has not recorded any gains or losses in earnings during 2017 or 2016.

Advertising Costs

Advertising costs are expensed as incurred.

Noncontrolling Interest

Noncontrolling interest represents the portion of ownership and interest expense that is attributable to the minority owners of LRAC. The minority ownership is in the form of 8.50% cumulative preferred stock, and the dividends paid are included in noncontrolling interest as a charge against income.

Note 1 - Summary of Significant Accounting Policies (Continued)

Income Taxes

Income taxes are provided for the tax effects of certain transactions reported in the consolidated financial statements. Income taxes consist of taxes currently due plus deferred taxes related primarily to temporary differences between the financial reporting and income tax basis of available for sale securities, the allowance for loan losses, premises and equipment, and prepaid and accrued employee benefits. The deferred tax assets and liabilities represent the future tax return consequences of the temporary 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 Company recognizes interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense.

Transfers of Financial Assets

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

Earnings Per Share

Basic earnings per share represents income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued. Treasury shares are not deemed outstanding for earnings per share calculations. See Note 12 for earnings per share calculations.

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income.

Statements of Cash Flows

For the purpose of presentation in the consolidated statements of cash flows, cash and cash equivalents are defined as the sum of cash and due from banks, federal funds sold, and interest-bearing deposits in banks with an original maturity of less than three months.

Off-Balance-Sheet Financial Instruments

In the ordinary course of business, the Bank has entered into off-balance-sheet financial instruments consisting of commitments to extend credit and standby letters of credit. Such financial instruments

Note 1 - Summary of Significant Accounting Policies (Continued)

are recorded in the consolidated financial statements when they are funded or related fees are incurred or received.

Segment Reporting

The Company has evaluated the activities relating to its strategic business units, and determined that these strategic business units are similar in nature, and managed accordingly. The strategic business units are not reviewed separately to make operating decisions or assess performance. Therefore, the Company has determined it has no reportable segments.

Note 2 - Restrictions on Cash and Due from Banks

The Bank is required to maintain reserve funds in cash and/or on deposit with the Federal Reserve Bank. The required reserve at December 31, 2017 and 2016 was $18.5 million and $16.4 million, respectively.

Note 3 - Investments

In October 2017, the Company reclassified all of its securities classified as held to maturity to available for sale because certain held to maturity securities were sold in March 2017. As a result, the Company adjusted the carrying amount of those securities from amortized cost of $47,604,897 to fair value of $47,415,254 in accordance with accounting principles generally accepted in the United States of America, thereby decreasing the value of total assets by $189,643. In connection therewith, the deferred tax asset related to the net unrealized loss on securities available for sale increased by $75,857, and accumulated other comprehensive loss increased by $113,786.

The amortized cost and fair value of investment securities, with gross unrealized gains and losses, are as follows at December 31, 2017 and 2016:

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2017:				
Available for Sale:				
United States agencies	$ 43,473	$ 20	$ (1,201)	$ 42,292
State and local governments	76,527	390	(253)	76,664
Corporate	2,000	-	-	2,000
Mortgage-backed securities	87,545	88	(2,247)	85,386
Total Available for Sale	$ 209,545	$ 498	$ (3,701)	$ 206,342
Restricted Equity Securities	$ 7,223	$ 117	$ -	$ 7,340

Note 3 – Investments (Continued)

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2016:				
Available for Sale:				
United States agencies	$ 39,496	$ 0	$ (1,118)	$ 38,378
State and local governments	70,076	241	(731)	69,586
Mortgage-backed securities	36,395	-	(1,376)	35,019
Total Available for Sale	$ 145,967	$ 241	$ (3,225)	$ 142,983
Held to Maturity:				
State and local governments	$ 7,212	$ 29	$ -	$ 7,241
Mortgage-backed securities	47,614	359	(650)	47,223
Corporate	2,000	-	-	2,000
Total Held to Maturity	$ 56,826	$ 388	$ (650)	$ 56,564
Restricted Equity Securities	$ 5,717	$ 75	$ -	$ 5,792

All of the above mortgage-backed securities are residential direct pass through securities or collateralized mortgage obligations issued or backed by U.S. government sponsored enterprises (GSEs). Restricted equity securities primarily include non-marketable Federal Home Loan Bank New York (FHLBNY) stock and non-marketable Federal Reserve Bank (FRB) stock, both of which are required to be held for regulatory purposes and for borrowing availability. The required investment in FHLBNY stock is tied to both the Company's borrowing levels with the FHLB and commitments to sell residential mortgage loans to the FHLB. Holdings of FHLBNY stock and FRB stock totaled $6.2 million and $648,000 at December 31, 2017, respectively, and $4.8 million and $500,000 at December 31, 2016, respectively. These securities are carried at par, which is also cost. The Company has an investment in Federal Agricultural Mortgage Corp (Farmer Mac) class A stock totaling $157,000 and $116,000 at December 31, 2017 and 2016, respectively, in order to participate in certain lending activities with Farmer Mac. The stock is actively traded on the NYSE, pays a dividend, and is reflective of current market value. Restricted equity securities also include miscellaneous investments carried at par, which is also cost.

Restricted equity securities are held as a long-term investment and value is determined based on the ultimate recoverability of the par value. Impairment of these investments is evaluated quarterly and is a matter of judgment that reflects management's view of the issuer's long-term performance, which includes factors such as the following: its operating performance; the severity and duration of declines in the fair value of its net assets related to its capital stock amount; its commitment to make payments required by law or regulation and the level of such payments in relation to its operating performance; and its liquidity and funding position. After evaluating these considerations, the Company concluded that the par value of these investments will be recovered and, as such, has not recognized any impairment on its holdings of restricted equity securities during the current year.

Note 3 – Investments (Continued)

The following table sets forth the Company's investment in securities with unrealized losses of less than twelve months and unrealized losses of twelve months or more at December 31:

	Less than 12 Months		12 Months or More		Total	
(In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2017:						
United States agencies	$ 15,746	$ (242)	$ 28,539	$ (959)	$ 44,285	$ (1,201)
State and local governments	26,431	(139)	4,370	(114)	30,801	(253)
Mortgage-backed securities	28,280	(772)	44,486	(1,475)	72,766	(2,247)
	$ 70,457	$ (1,153)	$ 77,395	$ (2,548)	$ 147,852	$ (3,701)

	Less than 12 Months		12 Months or More		Total	
(In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2016:						
United States agencies	$ 42,278	$ (1,118)	$ -	$ -	$ 42,278	$ (1,118)
State and local governments	41,774	(731)	-	-	41,774	(731)
Mortgage-backed securities	60,357	(2,026)	-	-	60,357	(2,026)
	$ 144,409	$ (3,875)	$ -	$ -	$ 144,409	$ (3,875)

On a quarterly basis, the Company performs an assessment to determine whether there have been any events or economic circumstances indicating that a security with an unrealized loss has suffered other-than-temporary impairment. Consideration is given to (1) the length of time and the extent to which the fair value has been less than the amortized cost basis, (2) the financial condition of the issuer (and guarantor, if any) and adverse conditions specifically related to the security, industry or geographic area, (3) failure of the issuer of the security to make scheduled interest or principal payments, (4) any changes to the rating of a security by a rating agency, (5) the presence of credit enhancements, if any, including the guarantee of the federal government or any of its agencies, (6) whether the Company intends to sell or more likely than not be required to sell the debt security, and (7) if the present value of the expected cash flow is not sufficient to recover the entire amortized cost.

There were one hundred thirty-nine securities with unrealized losses at December 31, 2017, while at December 31, 2016 there were one hundred seventy-three securities with unrealized losses. Substantially all of the unrealized losses on the Company's securities were caused by market interest rate changes from those in effect when the securities were purchased by the Company. The contractual terms of these securities do not permit the issuer to settle the securities at a price less than par value. Except for certain state and local government obligations, all securities rated by an independent rating agency carry an

Note 3 – Investments (Continued)

investment grade rating. Financial information relating to unrated state and government obligations is reviewed for indications of adverse conditions that may indicate other-than-temporary impairment. The Company did not consider these investment securities to be other than temporarily impaired at December 31, 2017 and 2016.

The amortized cost and fair value of debt securities at December 31, 2017, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations without call or prepayment penalties.

(In thousands)	Available for Sale	
	Amortized Cost	**Fair Value**
Due in one year or less	**$ 9,044**	**$ 9,045**
Due after one year through five years	**64,173**	**64,188**
Due after five years through ten years	**46,106**	**45,056**
Due after ten years	**6,689**	**6,680**
Securities not due at a single maturity date	**83,533**	**81,373**
	$ 209,545	**$ 206,342**

During 2017, the Company sold $3.5 million held to maturity securities, while in 2016 the Company sold $54.2 million of available for sale securities. Gross loss on the sale of investments in 2017 was $17,000. Gross gains on the sales of investment securities in 2016 were $470,000. Investment securities with carrying amounts of $141.8 million and $153.4 million at December 31, 2017 and 2016, respectively, were pledged to secure deposits as required or permitted by law.

Note 4 – Loans

Loans consist of the following at December 31, 2017 and 2016:

	2017	**2016**
Real estate:	(In thousands)	
Residential:		
1-4 family	**$ 202,150**	$ 183,123
Home equity	**115,791**	102,436
Commercial	**172,381**	153,724
Agriculture	**54,792**	48,688
Total mortgage loans on real estate	**545,114**	487,971
Commercial loans	**120,637**	122,214
Agriculture loans	**44,824**	40,870
Consumer installment loans:		
Direct	**21,490**	17,612
Indirect	**9,795**	10,024
Total consumer installment loans	**31,285**	27,636
Total loans	**$ 741,860**	$ 678,691

Net unamortized loan origination costs totaled $1.9 million and $1.6 million at December 31, 2017 and 2016, respectively and are included with their related loan class.

The Company has transferred a portion of its originated commercial, commercial real estate, agriculture and agriculture real estate loans to participating lenders. The amounts transferred have been accounted for as sales and are therefore not included in the Company's accompanying consolidated balance sheets. The Company and participating lenders share ratably in cash flows and any gains or losses that may result from a borrower's lack of compliance with contractual terms of the loan. The Company continues to service the loans on behalf of the participating lenders and, as such, collects cash payments from the borrowers, remits payments (net of servicing fees) to participating lenders and disburses required escrow funds to relevant parties. At December 31, 2017 and 2016 the Company was servicing loans for participants aggregating $16.0 million and $18.8 million, respectively.

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments are due. Generally, loans are placed on nonaccrual status if principal or interest payments become 90 days or more past due and/or management deems the collectability of the principal and/or interest to be in question, as well as when required by regulatory requirements.

Note 4 – Loans (Continued)

The following table presents past due loans by classes of the loan portfolio at December 31, 2017 and 2016:

(In thousands)	Current	30-89 Days Past Due	90 Days and Greater	Total Loans	Loans on Nonaccrual
December 31, 2017:					
Commercial loans	$ 118,772	$ 185	$ 1,680	$ 120,637	$ 1,242
Commercial real estate	171,949	45	387	172,381	368
Agriculture loans	44,590	234	-	44,824	-
Agriculture real estate	54,348	444	-	54,792	-
Residential real estate:					
1-4 family	201,922	177	51	202,150	202
Home equity	115,712	79	-	115,791	85
Consumer installment loans:					
Direct	21,357	133	-	21,490	-
Indirect	9,668	127	-	9,795	21
Total	$ 738,318	$ 1,424	$ 2,118	$ 741,860	$ 1,918

(In thousands)	Current	30-89 Days Past Due	90 Days and Greater	Total Loans	Loans on Nonaccrual
December 31, 2016:					
Commercial loans	$ 120,127	$ 905	$ 1,182	$ 122,214	$ 1,297
Commercial real estate	153,369	355	-	153,724	-
Agriculture loans	40,870	-	-	40,870	-
Agriculture real estate	48,688	-	-	48,688	-
Residential real estate:					
1-4 family	182,460	663	-	183,123	-
Home equity	102,228	149	59	102,436	167
Consumer installment loans:					
Direct	17,569	43	-	17,612	-
Indirect	9,989	35	-	10,024	-
Total	$ 675,300	$ 2,150	$ 1,241	$ 678,691	$ 1,464

At December 31, 2017 and 2016, there were no loans that were over 90 days' delinquent and still accruing interest. During 2016, the Company resolved a large problem loan which had been recorded as a non-performing asset since 2010 and subject to litigation. The Company's settlement resulted in a $1.1 million charge-off. As a result, non-performing assets decreased by approximately $2.5 million at the time of the resolution.

Note 4 – Loans (Continued)

Activity in the allowance for loan losses for the Years Ended December 31, 2017 and 2016 follows:

(In thousands)

2017	Commercial	Commercial Real Estate	Agriculture	Agriculture Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Beginning balance	$ 2,167	$ 1,762	$ 465	$ 464	$ 1,782	$ 363	$ 793	$ 7,796
Provisions for loan losses	1,152	(25)	31	44	188	226	(116)	1,500
Recoveries of loans previously charged off	17	9	-	-	-	68	-	94
Loans charged off	(461)	(87)	-	-	(26)	(187)	-	(761)
Ending balance	$ 2,875	$ 1,659	$ 496	$ 508	$ 1,944	$ 470	$ 677	$ 8,629
2016								
Beginning balance	$ 2,007	$ 2,911	$ 453	$ 442	$ 1,729	$ 376	$ 270	$ 8,188
Provisions for loan losses	394	(99)	12	22	83	165	523	1,100
Recoveries of loans previously charged off	11	34	-	-	18	81	-	144
Loans charged off	(245)	(1,084)	-	-	(48)	(259)	-	(1,636)
Ending balance	$ 2,167	$ 1,762	$ 465	$ 464	$ 1,782	$ 363	$ 793	$ 7,796

The allocation of the allowance for loan losses by loan class is as follows at December 31, 2017 and 2016:

(In thousands)

December 31, 2017	Commercial	Commercial Real Estate	Agriculture	Agriculture Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Amount of allowance for loan losses on loans individually evaluated for impairment	$ 1,056	$ -	$ -	$ -	$ -	$ -	$ -	$ 1,056
Amount of allowance for loan losses on loans collectively evaluated for impairment	1,819	1,659	496	508	1,944	470	677	7,573
Total allowance for loan losses	$ 2,875	$ 1,659	$ 496	$ 508	$ 1,944	$ 470	$ 677	$ 8,629
Loans individually evaluated for impairment	$ 1,242	$ 368	$ -	$ -	$ -	$ -	$ -	$ 1,610
Loans collectively evaluated for impairment	119,395	172,013	44,824	54,792	317,941	31,285	-	740,250
Total Loans	$ 120,637	$ 172,381	$ 44,824	$ 54,792	$317,941	$ 31,285	$ -	$741,860

Note 4 – Loans (Continued)

December 31, 2016	Commercial	Commercial Real Estate	Agriculture	Agriculture Real Estate	Residential Real Estate	Consumer	Unallocated	Total
Amount of allowance for loan losses on loans individually evaluated for impairment	$ 900	$ -	$ -	$ -	$ -	$ -	$ -	$ 900
Amount of allowance for loan losses on loans collectively evaluated for impairment	1,267	1,762	465	464	1,782	363	793	6,896
Total allowance for loan losses	$ 2,167	$ 1,762	$ 465	$ 464	$ 1,782	$ 363	$ 793	$ 7,796
Loans individually evaluated for impairment	$ 1,297	$ -	$ -	$ -	$ -	$ -	$ -	$ 1,297
Loans collectively evaluated for impairment	120,917	153,724	40,870	48,688	285,559	27,636	-	677,394
Total Loans	$ 122,214	$ 153,724	$ 40,870	$ 48,688	$285,559	$ 27,636	$ -	$678,691

Management is committed to early recognition of loan problems and to maintaining an adequate allowance. At least quarterly, management reviews all commercial and commercial real estate loans and leases and agriculturally related loans with an outstanding principal balance of over $100,000 that are internally risk rated substandard or worse, giving consideration to payment history, debt service payment capacity, collateral support, strength of guarantors, local market trends, industry trends, and other factors relevant to the particular borrowing relationship. Through this process, management identifies impaired loans. For loans considered impaired, estimated exposure amounts are based upon collateral values or present value of expected future cash flows discounted at the original effective interest rate of each loan. For commercial loans, commercial mortgage loans, agricultural mortgages and agricultural loans not specifically reviewed, and for homogenous loan portfolios such as residential mortgage loans and consumer loans, estimated exposure amounts are assigned based upon historical net loss experience and current charge-off trends, past due status, and management's judgment of the effects of current economic conditions on portfolio performance. In determining and assigning historical loss factors to the various homogeneous portfolios, the Company calculates average net losses over a period of time and compares this average to current levels and trends to ensure that the calculated average loss factor is reasonable.

Significant factors that could give rise to changes in these estimates may include, but are not limited to, changes in economic conditions in the local area, concentration of risk, changes in interest rates, and declines in local property values. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

Note 4 – Loans (Continued)

The above allocation is neither indicative of the specific amounts or the loan categories in which future charge-offs may occur, nor is it an indicator of future loss trends. The allocation of the allowance to each category does not restrict the use of the allowance to absorb losses in any category.

The following table summarizes information regarding impaired loans by loan portfolio class as of December 31, 2017 and 2016:

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2017					
With no related allowance recorded:					
Commercial loans	$ -	$ -	$ -	$ -	$ -
Commercial real estate	368	368	-	27	-
With an allowance recorded:					
Commercial loans	1,242	2,059	1,056	1,197	-
Commercial real estate	-	-	-		-
Total	$ 1,610	$ 2,427	$ 1,056	$ 1,224	$ -
Summary:					
Commercial	$ 1,242	$ 2,059	$ 1,056	$ 1,197	$ -
Commercial real estate	368	368	-	27	-
Total	$ 1,610	$ 2,427	$ 1,056	$ 1,224	$ -

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2016					
With no related allowance recorded:					
Commercial loans	$ 241	$ 246	$ -	$ 232	$ -
Commercial real estate	-	-	-	42	-
With an allowance recorded:					
Commercial loans	1,056	1,731	900	1,006	-
Commercial real estate	-	-	-	2,093	-
Total	$ 1,297	$ 1,977	$ 900	$ 3,373	$ -
Summary:					
Commercial	$ 1,297	$ 1,977	$ 900	$ 3,373	$ -
Commercial real estate	-	-	-	-	-
Total	$ 1,297	$ 1,977	$ 900	$ 3,373	$ -

Note 4 – Loans (Continued)

There were no troubled debt restructurings for the years ended December 31, 2017 or 2016.

There were no troubled debt restructurings that defaulted in the first twelve months after restructuring was granted.

Credit Quality

The Company utilizes a ten grade internal loan rating system for commercial, commercial real estate, agriculture and agriculture real estate loans. Loans that are rated "1" through "6" are considered "pass" rated loans with low to average risk.

Loans rated a "7" are considered "special mention". These loans have potential weaknesses that deserve management's close attention. These weaknesses may, if not checked or corrected, weaken the asset or inadequately protect the Company's position at some future date. Borrowers may be experiencing adverse operating trends, or an ill-proportioned balance sheet. Adverse economic or market conditions may also support a special mention rating. These assets pose elevated risks, but their weakness does not yet justify a substandard classification.

Loans rated an "8" are considered "substandard". Generally, a loan is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligors and/or the collateral pledged. Substandard loans have a high probability of payment default or they have other well-defined weaknesses. They require more intensive supervision by Company management. Substandard loans are generally characterized by current or unexpected unprofitable operations, inadequate debt service coverage, inadequate liquidity, or marginal capitalization.

Loans rated a "9" are considered "doubtful". Loans classified as doubtful have all the weaknesses inherent in those classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, highly questionable and improbable. There were no doubtful loans at December 31, 2017 or 2016.

Loans rated a "10" are considered uncollectible ("loss") and of such little value that their continuance as loans is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off this basically worthless loan even though partial recovery may be affected in the future. There were no loss loans at December 31, 2017 or 2016.

On an annual basis, or more often if needed, the Company formally reviews the ratings on all commercial, commercial real estate, agriculture and agriculture real estate loans. The Company also annually engages an independent third party to review a significant portion of loans within these classes. Management uses the results of these reviews as part of its annual review process.

The following table presents the classes of the commercial and agriculture loan portfolios summarized by the aggregate pass rating and the criticized and classified ratings of special mention and substandard within the Company's internal risk rating system as of December 31, 2017 and 2016:

Note 4 – Loans (Continued)

Credit Quality – continued

(In thousands)

	Commercial	Commercial Real Estate	Agriculture	Agriculture Real Estate	Total
December 31, 2017					
Grade:					
Pass	$ 116,179	$ 168,682	$ 43,145	$ 53,453	$ 381,459
Special Mention	2,709	2,729	1,631	1,124	8,193
Substandard	1,749	970	48	215	2,982
Total	$ 120,637	$ 172,381	$ 44,824	$ 54,792	$ 392,634
December 31, 2016					
Grade:					
Pass	$ 116,568	$ 148,577	$ 40,277	$ 47,454	$ 352,876
Special Mention	3,702	4,293	179	1,075	9,249
Substandard	1,944	854	414	159	3,371
Total	$ 122,214	$ 153,724	$ 40,870	$ 48,688	$ 365,496

Loans within the residential real estate and consumer portfolios do not have an internal loan rating system. Instead, they are monitored for past due status. If a residential real estate or consumer loan becomes 90 days past due, it is placed into nonaccrual status and the accrual of interest is discontinued.

Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual if collection of principal or interest is considered doubtful.

Note 4 – Loans (Continued)

Credit Quality – continued

The following table presents the classes of the residential real estate and consumer loan portfolios summarized by performing or nonaccrual as of December 31, 2017 and 2016:

(In thousands)

	1-4 Family	Home Equity	Consumer - Direct	Consumer - Indirect	Total
December 31, 2017					
Performing	$ 201,948	$ 115,706	$ 21,490	$ 9,774	$ 348,918
Nonaccrual	202	85	-	21	308
Total	$202,150	$ 115,791	$ 21,490	$ 9,795	$ 349,226
December 31, 2016					
Performing	$ 183,123	$ 102,269	$ 17,612	$ 10,024	$ 313,028
Nonaccrual	-	167	-	-	167
Total	$ 183,123	$ 102,436	$ 17,612	$ 10,024	$ 313,195

Note 5 - Land, Premises and Equipment

Land, premises and equipment, net consist of the following at December 31, 2017 and 2016:

	2017	2016
	(In thousands)	
Land	**$ 5,230**	$ 4,330
Buildings	**15,109**	15,099
Furniture and equipment	**6,763**	6,380
Leasehold improvements	**3,055**	2,858
Construction in progress	**2,825**	35
	32,982	28,702
Less: Accumulated depreciation	**(9,703)**	(8,605)
	$ 23,279	$ 20,097

Note 5 - Land, Premises and Equipment (Continued)

Depreciation and amortization expense in 2017 and 2016 are included in noninterest expense as follows:

	2017	2016
	(In thousands)	
Buildings	**$ 388**	$ 389
Furniture and equipment	**568**	622
Leasehold improvements	**143**	135
	$ 1,099	$ 1,146

At December 31, 2017, the Bank leased five of its branch facilities, as well as two operations facilities under non-cancelable operating leases. Future minimum rental payments under these leases are as follows:

Years Ending December 31,	(In thousands)
2018	$ 343
2019	333
2020	250
2021	182
2022	165
Thereafter	1,177
	$ 2,450

Rent expense under the operating leases totaled $332,000 and $311,000 in 2017 and 2016, respectively.

At December 31, 2017, the Bank leased out space under non-cancelable operating leases. Future minimum rental payments to be received by the Company under these leases are as follows:

Years Ending December 31,	(In thousands)
2018	$ 77
2019	77
2020	79
2021	81
2022	14
Thereafter	-
	$ 328

Rent income under the operating leases totaled $89,000 and $87,000 in 2017 and 2016, respectively.

Note 6 - Deposits

Certificates of deposit in denominations of $250,000 and over were $63.3 million and $50.8 million at December 31, 2017 and 2016, respectively.

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

Years Ending December 31,	(In thousands)
2018	$ 112,677
2019	61,060
2020	2,664
2021	2,444
2022	790
	$ 179,635

Note 7 - Borrowings

Borrowings consist of overnight advances and amortizing borrowings. At December 31, 2017 and 2016, there were $50 million and $18 million in overnight advances outstanding, respectively. The table below details additional information related to overnight advances for the years ended December 31, 2017 and 2016:

	2017	**2016**
	(Dollars in thousands)	
Average outstanding balance	**$ 13,966**	$ 2,595
Interest expense	**$ 186**	$ 18
Weighted average interest rate during the year	**1.34%**	0.69%
Weighted average interest rate at end of year	**1.53%**	0.74%

There was not any long term debt at December 31, 2017 and 2016.

As a member of the FHLB, the Bank can use certain unencumbered mortgage-related assets to secure borrowings from the FHLB. At December 31, 2017, total unencumbered mortgage-related loans were $41.1 million. Additional assets may also qualify as collateral for FHLB advances.

The Company, through the Bank, can use certain unencumbered collateral to secure borrowings at the Federal Reserve Bank. At December 31, 2017, total unencumbered collateral in the form of home equity loans and other consumer loans was $63.3 million.

The Company, through the Bank, had available unsecured line of credit agreements with correspondent banks permitting borrowings to a maximum of $17.0 million at December 31, 2017 and 2016, respectively. There were no outstanding advances against those lines at December 31, 2017 or 2016.

Note 8 - Junior Subordinated Debentures

On June 27, 2003, the Company issued $1.035 million in junior subordinated debentures due June 27, 2033, to Trust I. The Company owns all of the $35,000 in common equity of Trust I and the debentures are the sole asset of Trust I. Trust I issued $1.0 million of floating-rate trust capital securities in a non-public offering. The floating-rate capital securities provide for quarterly distributions at a variable annual coupon rate, reset quarterly, based on three-month LIBOR plus 2.75%. The coupon rate was 4.44% at December 31, 2017 and 3.75% at December 31, 2016. The securities are callable by the Company, subject to any required regulatory approval, at par, after June 2008.

The Company unconditionally guarantees the Trust I capital securities. The terms of the junior subordinated debentures and the common equity of Trust I mirror the terms of the trust capital securities issued by Trust I. The Company used the net proceeds from this offering to fund an additional $1.0 million capital investment in the Bank to fund its operations and future growth.

On August 23, 2004, the Company issued $5.155 million in junior subordinated debentures due August 23, 2034, to Trust II. The Company owns all of the $155,000 in common equity of Trust II and the debentures are the sole asset of Trust II. Trust II issued $5.0 million of floating-rate trust capital securities in a non-public offering. The floating-rate capital securities provide for quarterly distributions at a variable annual coupon rate, reset quarterly, based on three-month LIBOR plus 2.65%. The coupon rate was 4.10% at December 31, 2017 and 3.57% at December 31, 2016. The securities are callable by the Company subject to any required regulatory approval, at par, after August 2009.

The Company unconditionally guarantees the Trust II capital securities. The terms of the junior subordinated debentures and the common equity of Trust II mirror the terms of the trust capital securities issued by Trust II. The Company used the net proceeds from this offering to fund an additional $5.0 million capital investment in the Bank to fund its operations and future growth.

In December 2009, the Company entered into an interest rate swap agreement (swap) with an effective date of February 23, 2011. The Company designated the swap as a cash flow hedge and it is intended to protect against the variability of cash flows associated with Trust II. The swap modifies the pricing characteristic of Trust II, wherein the Company receives interest at three-month LIBOR plus 2.65% from a counterparty and pays a fixed rate of interest of 6.80% to the same counterparty calculated on a notional amount of $5.0 million. This agreement will expire on November 23, 2019. The swap agreement was entered into with a counterparty that met the Company's credit standards, and the agreement contains collateral provisions protecting the at-risk party. The Company believes that the credit risk inherent in this contract is not significant. At December 31, 2017, the Company pledged $420,000 cash collateral to the counterparty.

At December 31, 2017 and 2016, the fair value of the swap agreement was a loss of $216,000 and $377,000, respectively, and was the amount the Company would have expected to pay to terminate the agreement. The fair value of the swap is included in other liabilities in the accompanying consolidated balance sheets. The net effect of the swap increased interest expense by $151,000 and $177,000 in 2017 and 2016, respectively.

On February 12, 2010, the Company issued $3.027 million in junior subordinated debentures due February 12, 2040, to Trust III. The Company owned all of the $95,000 in common equity of Trust III and the debentures were the sole asset of Trust III. Trust III issued $2.932 million of fixed rate

Note 8 - Junior Subordinated Debentures (Continued)

convertible trust capital securities in a non-public offering. These capital securities provided for quarterly distributions at a fixed annual coupon rate of 6.00%. The securities were callable by the Company, subject to any required regulatory approval, at par, after February 2015. Holders of the trust securities were able to convert the securities, at any time, into shares of the Company's common stock at a conversion price of $13.89 per share, subject to adjustments for splits, stock dividends, recapitalization and the like and issuances on a pro rata basis below the current market value, in-kind dividends and tender offers above market value.

The Company unconditionally guaranteed the Trust III capital securities. The terms of the junior subordinated debentures and the common equity of Trust III mirror the terms of the convertible trust capital securities issued by Trust III. The Company used the net proceeds from this offering to fund an additional $2.9 million capital investment in the Bank for its operations and future growth. In 2016 the shareholders of Trust III elected to convert all remaining shares into shares of LYBC common stock and Trust III was fully dissolved. The conversion of the Trust III capital securities resulted in 186,000 shares converted to common stock increasing additional paid in capital by $2.5 million.

The accounts of Trust I, Trust II and Trust III are not included in the consolidated financial statements of the Company. However, for regulatory purposes, the trust capital securities qualify as Tier I capital of the Company subject to a 25% of capital limitation under risk-based capital guidelines. The portion that exceeds the 25% of capital limitation qualifies as Tier II capital. At December 31, 2017 and 2016, $6.0 million in trust capital securities qualified as Tier I capital, respectively.

Note 9 - Income Taxes

The provision for income taxes consists of the following for the years ended December 31:

	2017	**2016**
	(In thousands)	
Current tax provision:		
Federal	**$ 1,247**	$ 2,617
State	**86**	331
Total current tax provision	**1,333**	2,948
Deferred tax expense (benefit):		
Federal	**2,750**	(42)
State	**13**	35
Total deferred tax expense (benefit)	**2,763**	(7)
	$ 4,096	$ 2,941

Note 9 - Income Taxes (Continued)

Income tax expense differed from the statutory federal income tax rate for the years ended December 31 as follows:

	2017	2016
Statutory federal tax rate	**34.0%**	34.0%
Increase (decrease) resulting from:		
Tax-exempt interest income	**(4.5)**	(5.2)
Non-taxable earnings on bank-owned life insurance	**(1.0)**	(1.3)
Nondeductible expenses	**0.2**	0.1
Disallowed interest expense	**0.2**	0.2
Tax rate reduction	**5.4**	-
Other, net	**(0.5)**	0.1
Effective tax rate	**33.8%**	27.9%

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Components of the Company's net deferred tax assets at December 31, included in other assets in the accompanying consolidated balance sheets, are as follows:

	2017	**2016**
	(In thousands)	
Deferred tax assets:		
Allowance for loan losses	**$ 2,195**	$ 2,933
Compensation and benefits	**1,515**	3,458
Net unrealized loss on available for sale securities	**815**	1,164
Net unrealized loss on held to maturity securities transferred from available for sale	**-**	54
Other	**477**	706
Total deferred tax assets	**$ 5,002**	$ 8,315
Deferred tax liabilities:		
Prepaid pension	**$ 343**	$ 851
Depreciation	**402**	647
REIT	**1,334**	-
Other	**932**	1,053
Total deferred tax liabilities	**$ 3,011**	$ 2,551
Net deferred tax assets	**$ 1,991**	$ 5,764

Management believes it is more likely than not that all of the deferred tax assets will be realized. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income are reduced.

Note 9 - Income Taxes (Continued)

During 2017, the Tax Cuts and Jobs Act (the Act) was signed into law. The most significant impact of the Act is the reduction in the corporate federal income tax rate from a maximum rate of 35% to 21% beginning in 2018. As a result, the Company revalued its deferred tax assets and liabilities at its new effective tax rate and recorded a net adjustment of $583,776 to deferred tax expense to reduce the carrying value of the net deferred tax assets.

Note 10 - Stockholders' Equity

Preferred Stock – The Company is authorized to issue 5,000 shares of preferred stock having a par value of $0.50 per share and a stated value of $1,000 per share. The board of directors is authorized to issue these shares of preferred stock without stockholder approval in different classes and series and, with respect to each class or series, to determine the dividend rate, the redemption provisions, conversion provisions, liquidation preference, and other rights, privileges, and restrictions.

On November 15, 2016, the Company offered a private placement of 5,000 shares, par value of $0.50 per share, Series A Non-Cumulative Convertible Preferred Stock at $1,000 per share. The preferred stock is convertible, at any time, into shares of common stock, par value $0.50 per share, at the option of the holder. Upon a deemed liquidation event of Lyons Bancorp, the holders of the preferred shares are entitled to receive a liquidation distribution of $1,000 per share plus any declared and unpaid dividends, before any distribution of assets to holders of common stock. Dividends will be paid quarterly, if declared by the board of directors, at a rate per annum equal to 5%. As of December 31, 2017 and 2016, all 5,000 shares, par value $0.50 per share, of the authorized preferred stock have been issued and are outstanding.

Common Stock – The holders of the Company's common stock are entitled to receive dividends, if any, the board of directors may declare from time to time from funds legally available therefore, subject to the preferential rights of the holders of any shares of preferred stock that the Company may issue in the future. The holders of the Company's common stock are entitled to one vote per share on any matter to be voted upon by stockholders.

The common stock and treasury stock of the Company at December 31, 2017 and 2016 are as follows:

	2017	**2016**
Common stock, authorized shares, $0.50 par value	**5,000,000**	5,000,000
Issued shares	**3,198,660**	3,198,660
Less: treasury stock shares	**(8,788)**	(8,954)
Outstanding shares	**3,189,872**	3,189,706

Note 10 - Stockholders' Equity (Continued)

The amounts of income tax expense (benefit) allocated to each component of other comprehensive income are as follows for the Years Ended December 31, 2017 and 2016:

	2017	2016
	(In thousands)	
Securities available for sale:		
Net unrealized (losses) during the year	**$ (87)**	$ (1,219)
Reclassification adjustment for transfer from held to maturity	**(66)**	-
Reclassification adjustment for losses (gains) included in income	**7**	(188)
Securities held to maturity:		
Reclassification adjustment for amortization of unrealized losses included in income	**55**	105
Changes in unrealized gains during the year of restricted equity securities	**16**	20
Pension and postretirement benefits:		
Amortization of prior service credit	**(1)**	(1)
Amortization of net loss	**93**	80
Net actuarial gain (loss)	**304**	(11)
Cash flow hedge		
Gains (losses) on the effective portion of cash flow hedge	**4**	(10)
Reclassification adjustment for losses included in income	**60**	71
Tax expense (benefit)	**$ 385**	$ (1,153)

Note 10 - Stockholders' Equity (Continued)

Reclassifications out of accumulated other comprehensive (loss) income for the Years Ended December 31, 2017 and 2016 are as follows:

Details About Accumulated Other Comprehensive (Loss) Income Components	Amount Reclassified from Accumulated Other Comprehensive (Loss) Income		Affected Line Item In The Statement Where Net Income is Presented
	2017	2016	
	(In Thousands)		
Unrealized gains and losses on available for sale securities (before tax)	**$ (17)**	$ 470	Net realized gains from sales/calls of available for sale securities
Tax benefit (expense)	**7**	(188)	Income tax expense
Net of tax	**(10)**	282	
Amortization of unrealized losses on securities transferred to held to maturity (before tax):	**(136)**	(262)	Interest Income – investment securities, taxable
Tax benefit	**55**	105	Income tax expense
Net of tax	**(81)**	(157)	
Amortization of pension and postretirement benefit plan items (before tax):			
Prior service credit	**3**	3	
Net losses	**(233)**	(199)	
	(230)	(196)	Pensions and benefits expense
Tax benefit	**92**	79	Income tax expense
Net of tax	**(138)**	(117)	
Gains and losses on cash flow hedge (before tax)	**(151)**	(177)	Interest expense - borrowings
Tax benefit	**60**	71	Income tax expense
Net of tax	**(91)**	(106)	
Total reclassification for the year, net of tax	**$ (320)**	$ (98)	

Note 10 – Stockholders' Equity (Continued)

The balances and changes in the components of accumulated other comprehensive loss, net of tax, are as follows:

(In thousands)	Unrealized gains (losses) on securities available for sale	Unrealized losses on securities transferred to held to maturity	Unrealized gains on restricted equity securities	Pension and postretirement benefits	Unrealized losses on cash flow hedge	Total
Balance – January 1, 2016	$ 318	$ (238)	$ 14	$ (2,318)	$ (316)	$ (2,540)
Other comprehensive income (loss) before reclassifications	(1,825)	-	31	(17)	(16)	(1,827)
Amounts reclassified from accumulated other comprehensive income	(282)	157	-	118	105	98
Other comprehensive income (loss) for 2016	(2,107)	157	31	101	89	(1,727)
Balance – December 31, 2016	$ (1,789)	$ (81)	$ 45	$ (2,217)	$ (227)	$ (4,270)
Other comprehensive income (loss) before reclassifications	(259)	-	25	486	6	258
Amounts reclassified from accumulated other comprehensive income	10	81	-	138	91	320
Other comprehensive income for 2017	(249)	81	25	624	97	578
Reclassification of stranded tax effect	(420)			(384)	(31)	(835)
Balance – December 31, 2017	$ (2,458)	$ -	$ 70	$ (1,978)	$ (161)	$ (4,527)

Note 11 - Pension and Postretirement Benefit Plans

The Company participates in the New York State Bankers Retirement System (the "System"), a non-contributory defined benefit pension plan (the "Pension Plan") covering substantially all employees. The benefits are based on years of service and the employee's highest average compensation during five consecutive years of employment.

The Company also maintains an unfunded postretirement health insurance plan (the "Healthcare Plan") for certain employees meeting eligibility requirements.

The Company engages independent, external actuaries to compute the amounts of liabilities and expense relating to these plans, subject to the assumptions that the Company selects. The benefit obligation for these plans represents the liability of the Company for current and retired employees, and is affected primarily by the following: service cost (benefits attributed to employee service during the period); interest cost (interest on the liability due to the passage of time); actuarial gains/losses (experience during the year different from that assumed and changes in plan assumptions); and benefits paid to participants.

Note 11 - Pension and Postretirement Benefit Plans (Continued)

The following table provides a reconciliation of the changes in the Pension Plan's benefit obligations and fair value of assets and the accumulated benefit obligation for the Healthcare Plan for the years ending December 31, 2017 and 2016:

	Pension Plan		Healthcare Plan	
	2017	**2016**	**2017**	**2016**
	(In thousands)			
Change in benefit obligation:				
Benefit obligation at beginning of year	**$ 14,053**	$ 12,744	**$ 599**	$ 652
Service cost	**1,186**	1,082	**6**	6
Interest cost	**568**	540	**28**	25
Actuarial (gain) loss	**323**	220	**96**	(49)
Expected expenses	**(119)**	(104)	**-**	-
Benefits paid	**(380)**	(429)	**(60)**	(35)
Benefit obligation at end of year	**15,631**	14,053	**669**	599
Change in plan assets:				
Fair value of plan assets at beginning of year	**12,984**	11,639	**-**	-
Actual return on plan assets	**2,104**	893	**-**	-
Employer contribution	**2,400**	1,000	**36**	32
Actual expenses paid	**(128)**	(119)	**-**	-
Benefits paid	**(380)**	(429)	**(36)**	(32)
Fair value of plan assets at end of year	**16,980**	12,984	**-**	-
Funded status recognized	**$ 1,349**	$ (1,069)	**$ 669**	$ (599)
Accumulated benefit obligation	**$ 13,030**	$ 11,700	**$ 669**	$ 599

The underfunded status of the Pension and Healthcare Plans as of December 31, 2017 and 2016 has been recognized in other assets in the consolidated balance sheets. The unfunded status of the Healthcare

Note 11 - Pension and Postretirement Benefit Plans (Continued)

Plan has been recognized in other assets in the consolidated balance sheets at December 31, 2017 and 2016.

The components of net periodic benefit cost and other comprehensive income are as follows:

	Pension Plan		Healthcare Plan	
	2017	**2016**	**2017**	**2016**
Components of net periodic benefit cost:		(In thousands)		
Service cost	**$ 1,186**	$ 1,083	**$ 6**	$ 6
Interest cost	**568**	540	**28**	25
Expected return on plan assets	**(889)**	(740)	**-**	-
Amortization of prior service cost (credit)	**1**	1	**(4)**	(4)
Amortization of net loss	**214**	175	**19**	24
Net periodic benefit cost	**$ 1,080**	$ 1,059	**$ 49**	$ 51
Other changes in plan assets and benefit obligations recognized in other comprehensive income:				
Net (gain) loss	**$ (883)**	$ 82	**$ 122**	$ (54)
Recognized actuarial loss	**(214)**	(175)	**(19)**	(24)
Recognized prior service (cost) credit	**(1)**	(1)	**4**	4
Recognized in other comprehensive income	**$ (1,098)**	$ (94)	**$ 107**	$ (74)
Total recognized in net periodic benefit cost and other comprehensive income	**$ (18)**	$ 965	**$ 156**	$ (23)

The following table presents the components of accumulated other comprehensive loss, net of taxes, as of December 31:

	Pension Plan		Healthcare Plan	
	2017	**2016**	**2017**	**2016**
		(In thousands)		
Prior service cost (credit)	**$ 1**	$ 1	**$ (8)**	$ (10)
Net actuarial loss	**1,414**	2,073	**184**	153
	$ 1,415	$ 2,074	**$ 176**	$ 143

Note 11 - Pension and Postretirement Benefit Plans (Continued)

The estimated costs that will be amortized from accumulated other comprehensive loss into net periodic cost during 2017 are as follows:

	Pension Plan	Healthcare Plan	Total
		(In thousands)	
Prior service cost (credit)	$ 1	$ (4)	$ (3)
Net actuarial loss	66	20	86
Total	**$ 67**	**$ 16**	**$ 83**

Weighted-average assumptions used in accounting for the plans were as follows:

	Pension Plan		Healthcare Plan	
	2017	**2016**	**2017**	**2016**
Discount rates:				
Benefit cost for Plan Year	**4.12%**	4.32%	**4.00%**	4.16%
Benefit obligation at end of Plan Year	**3.96%**	4.12%	**3.51%**	4.00%
Expected long-term return on plan assets	**6.50%**	6.50%	**N/A**	N/A
Rate of compensation increase:				
Benefit cost for Plan Year	**3.00%**	3.00%	**N/A**	N/A
Benefit obligation at end of Plan Year	**3.00%**	3.00%	**N/A**	N/A

The assumed health care cost trend rate used in the postretirement benefit plan at December 31, 2017 was 4.00%. Assumed health care trend rates may have a significant effect on the amounts reported for this plan. A 1% increase in the trend rate would increase the periodic benefit cost by $5,000 and increase the accumulated postretirement benefit obligation by $101,000.

The discount rate used for each period was based upon the rates of return on high-quality fixed income investments. The objective of using this approach is to measure the single amount that, if invested at the measurement date in a portfolio of high-quality debt instruments, would provide the necessary future cash flows to pay benefits when they became due. The discount rates are evaluated at each measurement date to give effect to changes in the general level of interest rates.

The Company utilizes the Healthy Annuitant/Employee Mortality Table (RP-2017) to measure its pension plan obligation. In 2017, the Company used RP-2017 adjusted to reflect the Mortality Improvement Scale of 2017 (MP-2017), while in 2016, the Company utilized RP-2016 adjusted to reflect the Mortality Improvement Scale of 2016 (MP-2016). The change in the mortality table projection scale from MP-2016 to MP-2017 decreased the projected benefit obligation by approximately $0.1 million.

The Company's funding policy is to contribute, at a minimum, an actuarially determined amount that will satisfy the minimum funding requirements determined under the appropriate sections of the Internal Revenue Code. While the Company has satisfied the minimum funding requirement for 2017, it expects to contribute to the Pension Plan during 2018. However, the amount of the contribution is not known at this time.

Note 11 - Pension and Postretirement Benefit Plans (Continued)

Estimated future benefit payments, which reflect expected future service, as appropriate, are as follows:

	Pension Plan	Healthcare Plan
Years Ending December 31,	(In thousands)	
2018	$ 355	$ 34
2019	439	34
2020	463	33
2021	498	33
2022	537	33
2023 - 2027	3,551	180
	$ 5,843	$ 347

The fair value of the Company's pension plan assets at December 31, 2017 and 2016 by asset category are as follows:

	Total	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
		(In thousands)		
December 31, 2017:				
Cash equivalents:				
Foreign currencies	$ 148	$ 148	$ -	$ -
Short term investment funds	41	-	41	-
Total cash equivalents	189	148	41	-
Equity securities:				
Common stock	2,959	2,959	-	-
Depository receipts	75	75	-	-
Commingled pension trust funds	4,653	-	4,653	-
Preferred stock	65	65	-	-
Total equity securities	7,752	3,099	4,653	-
Fixed income securities:				
Collateralized mortgage obligations	119	-	119	-
Commingled pension trust funds	3,689	-	3,689	-
Corporate bonds	625	-	625	-
Federal National Mortgage Corporation	34	-	34	-
Government issues	2,061	-	2,061	-
Other securities	12	-	12	-
Total fixed income securities	6,540	-	6,540	-
Other financial instruments				
Commingled pension trust funds	538	-	-	538
Total other financial instruments	538	-	-	538
Investments valued using Net Asset Value	1,961			
Total	$ 16,980	$ 3,247	$ 11,234	$ 538

Note 11 - Pension and Postretirement Benefit Plans (Continued)

	Total	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
		(In thousands)		
December 31, 2016:				
Cash equivalents:				
Foreign currencies	$ 17	$ 17	$ -	$ -
Short term investment funds	54	-	54	-
Total cash equivalents	71	17	54	-
Equity securities:				
Common stock	2,299	2,299	-	-
Depository receipts	68	68	-	-
Commingled pension trust funds	2,702	-	2,702	-
Exchange traded funds	-	-	-	-
Total equity securities	5,069	2,367	2,702	-
Fixed income securities:				
Collateralized mortgage obligations	109	-	109	-
Commingled pension trust funds	2,785	-	2,785	-
Corporate bonds	494	-	494	-
Federal Home Loan Mortgage Corporation	100	-	100	-
Government issues	1,688	-	1,688	-
Other securities	6	-	6	-
Total fixed income securities	5,182	-	5,182	-
Other financial instruments				
Commingled pension trust funds	455	-	-	455
Total other financial instruments	455	-	-	455
Investments valued using Net Asset Value	2,207			
Total	$ 12,984	$ 2,384	$ 7,938	$ 455

At December 31, 2017 and 2016, the portfolio was managed by two investment firms. In addition, as of December 31, 2017 and 2016, approximately $523,000 and $729,000, respectively, of Pension Plan monies had not yet been allocated to either investment manager. At December 31, 2017, control was split at approximately 59%, 37% and 4%. At December 31, 2016, control was split at approximately 58%, 38% and 4%.

Note 11 - Pension and Postretirement Benefit Plans (Continued)

At December 31, 2017, there were the following investment concentrations:

- Two commingled pension trust funds, which were 6% and 14% of the total portfolio,
- An exchange traded fund, which was 6% of the total portfolio, and
- The short term investment fund, which was 6% of the total portfolio.

At December 31, 2016, there were the following investment concentrations:

- Two commingled pension trust funds, which were 7% and 11% of the total portfolio,
- An exchange traded fund, which was 7% of the total portfolio, and
- The short term investment fund, which was 5% of the total portfolio.

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

- Level 1—Quoted prices in active markets for identical assets or liabilities.

- Level 2—Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

- Level 3—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

In instances in which the inputs used to measure fair value fall into different levels of the fair value hierarchy, the fair value measurement has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. Investments valued using the Net Asset Value (NAV) are classified as Level 2 if the Pension Plan can redeem its investment with the investee at the NAV at the measurement date. If the Pension Plan can never redeem the investment with the investee at the NAV, it is considered a Level 3. If the Pension Plan can redeem the investment at the NAV at a future date, the Pension Plan's assessment of the significance of a particular item to the fair value measurement in its entirety requires judgment, including the consideration of inputs specific to the asset.

The Pension Plan uses the Thomson Reuters Pricing Service to determine the fair value of equities excluding commingled pension trust funds, the pricing service of IDC Corporate USA to determine the fair value of fixed income securities excluding commingled pension trust funds and JP Morgan Chase Bank, N.A. and Northern Trust to determine the fair value of equity and fixed income commingled pension trust funds.

Note 11 - Pension and Postretirement Benefit Plans (Continued)

The following is a table of the pricing methodology and unobservable inputs used by JPMorgan in pricing commingled pension trust funds:

Commingled Pension Trust Funds (CPTF) – Fixed Income	Principal Valuation Technique(s) Used	Unobservable Inputs
CPTF (Corporate High Yield) of JPMorgan Chase Bank, N.A.	Market	None
CPTF (High Yield) of JPMorgan Chase Bank, N.A.	Market Comparables Companies	EBITDA multiple, discount rate of cash flows and discounts for lack of marketability
CPTF (Long Duration Investment Grade) of JPMorgan Chase Bank, N.A.	Market	None
CPTF (Emerging Markets Currency Debt) of JPMorgan Chase Bank, N.A.	Market	None
CPTF (Emerging Markets – Fixed Income Debt) of JPMorgan Chase Bank, N.A.	Market	None
NY Collective Aggregate Bond Index Fund – Lending	NAV	None

Commingled Pension Trust Funds (CPTF) –Other	Principal Valuation Technique(s) Used	Unobservable Inputs
CPTF (Strategic Property) of JPMorgan Chase Bank, N.A.	Market, income, debt service and sales comparison	Credit spreads, discount rate, loan to value ratio, terminal capitalization rate and value per square foot

When valuing Commingled Pension Trust Funds (Equity), JPMorgan uses a market methodology and does not rely on unobservable inputs in those valuations.

The following table sets forth a summary of the changes in Level 3 assets for the years ended December 31, 2017 and 2016:

January 1, 2016	**$ 430**
Sales	**(66)**
Realized gains	**9**
Unrealized gains	**82**
Balances, December 31, 2016	**$ 455**
Sales	**(46)**
Purchases	**21**
Realized gains	**9**
Unrealized gains	**99**
Balances, December 31, 2017	**$ 538**

There were no transfers in or out of Level 3 in the Years Ended December 31, 2017 and 2016.

Note 11 - Pension and Postretirement Benefit Plans (Continued)

The Pension Plan was established in 1938 to provide for the payment of benefits to employees of participating banks. The Pension Plan is overseen by a Board of Trustees who meet quarterly and set the investment policy guidelines.

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

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

Equity securities: Dividend discount model, the smoothed earnings yield model, and the equity risk premium model

Fixed income securities: Current yield-to-maturity and forecasts of future yields

Other financial instruments: Comparison of the specific investment's risk to that of fixed income and equity instruments and using judgment.

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

Investment managers are prohibited from purchasing any security greater than 5% of the portfolio at the time of purchase or greater than 8% at market value in any one issuer. The issuer of any security purchased must be located in a country in the Morgan Stanley Capital International World Index. In addition, the following investments are prohibited:

Equity securities:

- Short sales,
- Unregistered securities, and
- Margin purchases.

Note 11 - Pension and Postretirement Benefit Plans (Continued)

Fixed income securities:

- Mortgage backed derivatives that have an inverse floating rate coupon or that are interest only securities,
- Any asset backed security that is not issued by the U.S. government or its agencies or instrumentalities,
- In general, securities of less than Baa2/BBB quality,
- Securities of less than A-quality may not in the aggregate exceed 13% of the investment manager's portfolio, and
- An investment manager's portfolio of commercial mortgage-backed securities and asset-backed securities may not exceed 10% of the portfolio at the time of purchase.

Other financial instruments:

- Unhedged currency exposure in countries not defined as "high income economies" by the World Bank

All other investments not prohibited by policy are permitted. At December 31, 2017 and 2016 the Pension Plan held certain investments which are no longer deemed acceptable to acquire. These positions will be liquidated when the investment managers deem that such liquidation is in the best interest of the Pension Plan.

The target allocation for 2017 and actual allocation of plan assets as of December 31, 2017 and 2016 are as follows:

		% of Plan Assets at December 31,	
Asset Category	Target Allocation 2017	2017	2016
Cash equivalents	0-20%	6.4%	6.1%
Equity securities	40-60%	50.2%	47.9%
Fixed income securities	40-60%	40.2%	42.6%
Other financial instruments	0-5%	3.2%	3.4%

Defined Contribution Plan

The Bank has a contributory 401(k) Plan for substantially all employees. Employees are eligible to contribute a percentage of their salary up to the maximum as determined by the Internal Revenue Service. The Bank is required to match 75% of the employees' contributions up to a maximum of 6% of the employees' salaries. The Bank contributed $419,000 and $385,000 under these provisions during 2017 and 2016, respectively.

Note 11 - Pension and Postretirement Benefit Plans (Continued)

Supplemental Employee Retirement Plans

The Company maintains supplemental employee retirement plans (the "SERP") for certain executives. All benefits provided under the SERP are unfunded and, as these executives retire, the Company will make payments to plan participants. The unfunded status of the SERP at December 31, 2017 and 2016 was $3.7 million and $3.5 million, respectively, and is recorded in other liabilities in the consolidated balance sheets. Compensation expense related to the SERP was $220,000 and $300,000 for the years ended December 31, 2017 and 2016.

Deferred Compensation Plans

Prior to 2007, the Company had entered into employment agreements with key executives. These employment agreements established deferred compensation plans whereby Company stock was awarded and vested each year. In 2007, the Company terminated the employment agreements and related deferred compensation plans and established new deferred compensation plans for key executives. The new plans require a vesting period of three years from the original date the executive entered the plan. Awarded shares from both the prior plan and the current plan are restricted from being sold until employment is terminated.

The Company obtains shares for the new deferred compensation plan either through open market purchases or from treasury shares. The amount of awarded shares is based on the amount earned by each executive under the deferred compensation plan. The executives are awarded a number of shares based on the amount of deferred compensation earned divided by the value of the shares. The value of the shares purchased on the open market is the price paid. The value of the shares from treasury is the average daily closing price of the stock for each day within the past quarter. Total deferred compensation shares were 146,497 and 141,266 at December 31, 2017 and 2016 respectively. Total shares awarded were 5,231 and 7,288 for 2017 and 2016, respectively. Compensation expense is recognized over the vesting period, and is based upon the total amount of the value of the shares awarded to each executive. Compensation expense related to the plan was approximately $184,000 and $161,000 for the Years Ended December 31, 2017 and 2016, respectively.

Note 12 - Earnings Per Share

The following table presents a reconciliation of the earnings and shares used in calculating basic and diluted EPS for each of the years ended December 31:

	2017	2016
	(in thousands, except per share data)	
Net income	**$ 8,009**	$ 7,596
Adjustment for dilutive potential common shares	**-**	23
Preferred stock dividends	**250**	-
Net income available for diluted common shares	**$ 7,759**	$ 7,619
Weighted average common shares used to calculate basic EPS	**3,190,774**	3,140,523
Add: effect of common stock equivalents(1)	**120,000**	46,734
Weighted average common shares used to calculate diluted EPS	**3,310,774**	3,187,257
Earnings per common share :		
Basic	**$ 2.43**	$ 2.42
Diluted	**$ 2.42**	$ 2.39

(1) For 2017 only, 5,000 shares of convertible preferred stock are convertible into 120,000 shares of LYBC common stock.

Note 13 - Related Party Transactions

In the ordinary course of business, the Bank has and expects to continue to have transactions, including loans and deposit accounts, with the Company's and the Bank's executive officers and directors and their affiliates. In the opinion of management, such transactions were on substantially the same terms, including interest rates and collateral, as those prevailing at the time of comparable transactions with other unrelated persons and did not involve more than a normal risk of collectability or present any other unfavorable features.

The roll-forward of loans to related parties for the years ended December 31, 2017 and December 31, 2016 is as follows:

	2017	2016
	(In thousands)	
Beginning balance, January 1	**$ 10,556**	$ 10,517
New loans	**3,332**	2,005
New (Former) Directors	**294**	(30)
Sold Loans	**-**	(250)
Repayments	**(3,793)**	(1,686)
Ending balance, December 31	**$ 10,389**	$ 10,556

Note 14 - Commitments and Contingent Liabilities

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the consolidated balance sheets. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments summarized as follows at December 31:

	2017	2016
	(In thousands)	
Commitments to extend credit:		
Commitments to grant loans	**$ 84,811**	$ 68,235
Unfunded commitments under commercial lines of credit	**100,523**	76,862
Unfunded commitments under consumer lines of credit	**76,293**	70,143
Standby letters of credit	**13,584**	9,697
	$275,211	$ 224,937

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. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount and type of collateral obtained, if deemed necessary by the Bank upon extension of credit, varies and is based on management's credit evaluation of the counterparty.

Standby letters of credit are conditional lending commitments issued by the Bank to guarantee the performance of a customer to a third party. These letters of credit are primarily issued to support public and private borrowing arrangements. Generally, letters of credit issued have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank's policy for obtaining collateral, and the nature of such collateral, is essentially the same as that involved in making commitments to extend credit. The Bank generally holds collateral supporting those commitments. Such collateral amounted to $12.4 million and $7.7 million at December 31, 2017 and 2016, respectively. The amount of the liability related to guarantees under standby letters of credit was not material at December 31, 2017 and 2016.

Note 14 - Commitments and Contingent Liabilities (Continued)

In addition to other investors, the Bank sells residential mortgage loans to the FHLB. The agreement with the FHLB includes a maximum credit enhancement liability of $3.6 million and $9.4 million at December 31, 2017 and 2016 respectively, which the Bank may be required to pay if realized losses on any of the sold mortgages exceed the amount held in the FHLB's spread account. The FHLB is funding the spread account annually based on the outstanding balance of loans sold. The Bank's historical losses on residential mortgages have been lower than the amount being funded to the spread account. As such, the Bank does not anticipate recognizing any losses and, accordingly, has not recorded a liability for the credit enhancement.

In addition to pledging investment securities to secure deposits, the Bank has entered into an agreement with the FHLB whereby the FHLB agrees to issue letters of credit for the benefit of securing deposits. In the event the FHLB makes a payment under this agreement, such payment will constitute an advance to the Bank and shall be immediately due and payable. The Bank has pledged unencumbered mortgage-related assets to secure letters of credit from the FHLB. As of December 31, 2017 and 2016, the Bank had letters of credit outstanding with the FHLB of $33.1 million.

Note 15 - Concentrations of Credit

The Company's loan customers are located primarily in the New York communities served by the Bank. Investments in state and local government securities also involve governmental entities within the Company's market area. Although operating in numerous communities in New York State, the Company is still dependent on the general economic conditions of New York. The largest concentration of credit by industry is Lessor's of Nonresidential Buildings, with loans outstanding of $41 million or 5.47% of total loans as of December 31, 2017. Risk related to this concentration is controlled through adherence to loan policy guidelines, including appropriate debt service coverage, adequate property values substantiated by current appraisals, and obtaining guarantors where appropriate. The Company, as a matter of policy, does not extend credit to any single borrower, or group of related borrowers, in excess of its legal lending limit. Further information on the Company's lending activities is provided in "Note 4 Loans" in Notes to Consolidated Financial Statements.

Note 16 - Regulatory Matters

The supervision and regulation of financial and bank holding companies and their subsidiaries is intended primarily for the protection of depositors, the deposit insurance funds regulated by the Federal Deposit Insurance Corporation ("FDIC") and the banking system as a whole, and not for the protection of shareholders or creditors of bank holding companies. The various bank regulatory agencies have broad enforcement power over financial holding companies and banks, including the power to impose substantial fines, operational restrictions and other penalties for violations of laws and regulations and for safety and soundness considerations.

Note 16 - Regulatory Matters (Continued)

Capital

The Company (on a consolidated basis) and the Bank are subject to various regulatory capital requirements administered by 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 Company's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of their 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 Company and the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined by regulation) and of Tier I capital (as defined) to average assets (as defined). The Company's and the Bank's capital amounts and ratios are also presented in the table below.

In July 2013, the Federal Reserve approved and published the final Basel III Capital Rules establishing a new comprehensive capital framework for U.S. banking organizations. The rules implement the Basel Committee's December 2010 framework known as "Basel III" for strengthening international capital standards as well as certain provisions of the Dodd-Frank Act. The Basel III Capital Rules substantially revise the risk-based capital requirements applicable to bank holding companies and depository institutions, including the Company and the Bank, compared to the current U.S risk-based capital rules. The Basel III Capital Rules define the components of capital, and address risk weights and other issues affecting the denominator in the banking institutions' regulatory capital ratios. It also replaces the existing risk-weighting approach, with a more risk-sensitive approach based, in part, on the standardized approach in the Basel Committee's 2004 "Basel II" capital accords and implements the requirements of Section 939A of the Dodd-Frank Act to remove references to credit ratings utilized in the federal banking agencies' rules. The Basel III Capital Rules were effective for the Company and the Bank on January 1, 2015 (subject to a phase-in period).

As required under Dodd-Frank, a new capital ratio, "common equity tier 1 capital ratio" (CET1) was established. This ratio allows only common equity to qualify as tier 1 capital. The new CET1 ratio also will include most elements of accumulated other comprehensive income, including unrealized securities gains and losses, as part of both total regulatory capital (numerator) and total assets (denominator). Community banks, however, were given the opportunity to make a one-time irrevocable election to include or not to include certain elements of other comprehensive income, most notably unrealized securities gains or losses. The Company and the Bank elected to not include the certain items of other comprehensive income in their capital calculations.

In addition to setting higher minimum capital ratios, the new rules, introduce a capital conservation buffer, which must be added to each of the minimum capital ratios and is designed to absorb losses during periods of economic stress. The capital conservation buffer will be phased-in over five years beginning on January 1, 2016 and will be set at 2.5% when fully phased-in. If a banking organization fails to hold capital above minimum capital ratios, including the capital conservation buffer, it will be subject to certain restrictions on capital distribution and discretionary bonus payments.

Note 16 - Regulatory Matters (Continued)

The final rules eliminated the proposed phase-out over 10 years or Trust Preferred Securities, or "TRUPs" as tier 1 capital for bank holding companies and bank, such as the Company and the Bank, that have less than $15 billion in total assets. Under the final rule, grandfathered TRUPs would continue to qualify as tier 1 capital until they mature or are redeemed, up to a limit of 25% of tier 1 capital (for grandfathered TRUPs and other grandfathered tier 1 capital components).

(Dollars in thousands)	Actual		For Capital Adequacy Purposes		To be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2017:						
Total risk-based capital						
Consolidated	**$94,127**	**12.4** %	**$≥60,621**	**≥8.0** %	**$≥75,776**	**≥10.0** %
Bank	**$94,061**	**12.4** %	**$≥60,598**	**≥8.0** %	**$≥75,748**	**≥10.0** %
Tier 1 capital						
Consolidated	**$78,372**	**10.3** %	**$≥45,466**	**≥6.0** %	**$≥60,621**	**≥8.0** %
Bank	**$84,602**	**11.2** %	**$≥45,449**	**≥6.0** %	**$≥60,598**	**≥8.0** %
Tier 1 leverage						
Consolidated	**$78,372**	**7.7** %	**$≥41,082**	**≥4.0** %	**$≥51,353**	**≥ 5.0** %
Bank	**$84,602**	**8.3** %	**$≥41,104**	**≥4.0** %	**$≥51,380**	**≥ 5.0** %
Common Equity Tier 1						
Consolidated	**$73,383**	**9.7** %	**$≥34,099**	**≥4.5** %	**$≥49,255**	**≥ 6.5** %
Bank	**$79,619**	**10.5** %	**$≥34,087**	**≥4.5** %	**$≥49,236**	**≥ 6.5** %
December 31, 2016:						
Total risk-based capital						
Consolidated	$80,191	11.3 %	$≥56,683	≥8.0 %	$≥70,853	≥10.0 %
Bank	$87,350	12.3 %	$≥56,631	≥8.0 %	$≥70,789	≥10.0 %
Tier 1 capital						
Consolidated	$73,124	10.3 %	$≥42,512	≥6.0 %	$≥56,683	≥8.0 %
Bank	$79,498	11.2 %	$≥42,474	≥6.0 %	$≥56,631	≥8.0 %
Tier 1 leverage						
Consolidated	$73,124	7.8 %	$≥38,048	≥4.0 %	$≥47,560	≥ 5.0 %
Bank	$79,498	8.5 %	$≥37,555	≥4.0 %	$≥46,944	≥ 5.0 %
Common Equity Tier 1						
Consolidated	$68,137	9.6 %	$≥31,884	≥4.5 %	$≥46,055	≥ 6.5 %
Bank	$79,498	11.2 %	$≥31,855	≥4.5 %	$≥46,013	≥ 6.5 %

Note 16 - Regulatory Matters (Continued)

Management believes, as of December 31, 2017, that the Company and the Bank meet all capital adequacy requirements to which they are subject.

As of the most recent notification from the Office of the Comptroller of the Currency, the Bank was categorized as well capitalized. There are no conditions or events since the notification that management believes have changed the institution's category

Dividend Restrictions

In the ordinary course of business, the Company is dependent upon dividends from the Bank to provide funds for the payment of interest expense on the junior subordinated debentures, dividends to shareholders and to provide for other cash requirements. Banking regulations may limit the amount of dividends that may be paid. Approval by regulatory authorities is required if the effect of dividends declared would cause the regulatory capital of the Bank to fall below specified minimum levels. Approval is also required if dividends declared exceed the net profits for that year combined with the retained net profits for the preceding two years.

At December 31, 2017, the Bank's retained earnings available for the payment of dividends was approximately $13.6 million.

Note 17 - Fair Value Measurements and Fair Values of Financial Instruments

Determination of Fair Value

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various assets and liabilities. 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 instrument.

Fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment.

Note 17 - Fair Value Measurements and Fair Values of Financial Instruments (Continued)

Fair Value Hierarchy

The Company groups its financial assets and financial liabilities generally measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

Level 1: Valuation is based on unadjusted quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date. Level 1 assets and liabilities generally include debt and equity securities that are traded in an active exchange market.

Level 2: Valuation is based upon inputs other than quoted prices included within level 1 that are observable either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

Level 3: Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value measurement. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires significant management judgment or estimation.

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

The following information should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only provided for a limited portion of the Company's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Company's disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Company's financial instruments at December 31, 2017 and 2016:

Cash, Due From Banks, and Interest-bearing Deposits in Banks

The carrying amounts reported in the consolidated balance sheets for these assets approximate fair values based on the short-term nature of the assets.

Investment Securities

The fair value of securities available for sale and held to maturity are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or pricing models (Level 2), which consider standard input factors such as observable market data, benchmark yields, interest rate volatilities, broker/dealer quotes, credit spreads and new issue data. For certain securities which are not traded in active markets or are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments are generally based on available market evidence (Level 3). In the absence of such evidence, management's best estimate is used.

Note 17 - Fair Value Measurements and Fair Values of Financial Instruments (Continued)

Management's best estimate consists of external support on certain Level 3 investments. Management has determined that the fair value of local government securities in the held to maturity portfolio approximate their carrying value. Restricted equity securities have restrictions on their sale and are primarily carried at cost due to their limited marketability. The fair value of the Company's investment in Farmer Mac is determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1).

Loans Held for Sale

The fair value of loans held for sale is determined using quoted secondary-market prices. If no such quoted prices exist, the fair value of a loan is determined using quoted prices for a similar loan or loans, adjusted for the specific attributes of that loan, resulting in a Level 2 classification.

Loans

The fair values of loans are estimated using discounted cash flow analyses, using market rates at the balance sheet date that reflect the credit and interest rate-risk inherent in the loans, resulting in a Level 3 classification. Projected future cash flows are calculated based upon contractual maturity or call dates, projected repayments and prepayments of principal.

Impaired Loans

The fair value of loans considered impaired is generally determined based upon independent third party appraisals of the properties (market approach), or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements. The fair value consists of the loan balances of \$1.6 million and \$1.3 million, net of valuation allowances of \$1.1 million and \$0.9 million as of December 31, 2017 and 2016, respectively.

Accrued Interest Receivable and Payable

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

Mortgage Servicing Rights

The carrying amount of mortgage servicing rights approximates their fair value.

Deposits

The fair values disclosed for demand and savings deposits are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates on comparable instruments to a schedule of aggregated expected monthly maturities on time deposits, resulting in a Level 2 classification.

Borrowings from the Federal Home Loan Bank

Fair values of borrowings from the FHLB are estimated using discounted cash flow analysis, based on quoted prices for new borrowings from the FHLB with similar credit risk characteristics, terms

Note 17 - Fair Value Measurements and Fair Values of Financial Instruments (Continued)

and remaining maturity, resulting in a Level 2 classification. These prices obtained from this active market represent a market value that is deemed to represent the transfer price if the liability were assumed by a third party.

Junior Subordinated Debentures

The fair values of junior subordinated debentures are estimated using discounted cash flow analysis, based on market rates currently offered on such debt with similar credit risk characteristics, terms and remaining maturity, resulting in a Level 2 classification.

Interest Rate Swap Agreements

The fair value of the interest rate swap derivative is calculated based on a discounted cash flow model. All future floating cash flows are projected and both floating and fixed cash flows are discounted to the valuation date. The curve utilized for discounting and projecting is built by obtaining publicly available third party market quotes for various swap maturity terms, resulting in a Level 2 classification.

Off-Balance Sheet Financial Instruments

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

Note 17 - Fair Value Measurements and Fair Values of Financial Instruments (Continued)

Assets and Liabilities Measured at Fair Value on a Recurring Basis

For financial assets measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2017 and 2016 are as follows:

	Carrying Value	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
		(In thousands)		
December 31, 2017:				
Securities available for sale:				
United States agencies	**$ 42,292**	**$ -**	**$ 42,292**	**$ -**
State and local governments	**76,664**	**-**	**76,664**	**-**
Mortgage-backed securities	**85,386**	**-**	**85,386**	**-**
Corporate securities	**2,000**	**-**	**2,000**	**-**
Total securities available for sale	**$ 206,342**	**$ -**	**$ 206,342**	**$ -**
Restricted equity security	**$ 157**	**$ 157**	**$ -**	**$ -**
Interest rate swap agreements	**$ (216)**	**$ -**	**$ (216)**	**$ -**
December 31, 2016:				
Securities available for sale:				
United States agencies	$ 38,378	$ -	$ 38,378	$ -
State and local governments	69,586	-	69,586	-
Mortgage-backed securities	35,019	-	35,019	-
Total securities available for sale	$ 142,983	$ -	$ 142,983	$ -
Restricted equity security	$ 116	$ 116	$ -	$ -
Interest rate swap agreements	$ (377)	$ -	$ (377)	$ -

Note 17 - Fair Value Measurements and Fair Values of Financial Instruments (Continued)

Assets Measured at Fair Value on a Nonrecurring Basis

There were no assets measured at fair value on a nonrecurring basis at December 31, 2017 and 2016.

The carrying amounts and estimated fair values of the Company's financial instruments at December 31, 2017 and 2016 are as follows:

		2017		2016	
	Fair Value Hierarchy	**Carrying Amount**	**Fair Value**	Carrying Amount	Fair Value
			(In thousands)		
Financial assets:					
Cash and due from banks	1	**$ 13,638**	**$ 13,638**	$ 14,458	$ 14,458
Interest-bearing deposits in banks	1	**19,596**	**19,596**	17,952	17,952
Investment securities	1 and 2	**213,682**	**214,139**	205,601	205,339
Loans, net of allowance	2 and 3	**733,231**	**731,556**	670,895	677,205
Accrued interest receivable	1	**3,516**	**3,516**	3,052	3,052
Mortgage servicing rights	2	**1,625**	**1,625**	1,286	1,286
Financial liabilities:					
Demand and savings deposits	1	**$ 713,840**	**$ 713,840**	$ 703,626	$ 703,626
Certificates of deposit	2	**179,635**	**178,626**	156,447	157,761
Borrowings from FHLB	2	**50,000**	**50,000**	18,000	18,000
Junior subordinated debentures	2	**6,190**	**6,170**	6,190	6,177
Interest rate swap agreements	2	**216**	**216**	377	377
Accrued interest payable	1	**156**	**156**	145	145

Amounts in the preceding table are included in the consolidated balance sheets under the applicable captions. The fair values of off-balance sheet financial instruments are not significant.

Lyons Bancorp, Inc.
It's all about people.

PROFILE

Lyons Bancorp, Inc. is a financial holding company headquartered in Lyons, New York, with assets of $1.03 billion at December 31, 2017. Lyons Bancorp, Inc. has one banking subsidiary, The Lyons National Bank.

The Lyons National Bank is a community bank with offices in Clyde, Lyons, Macedon, Newark, Ontario, and Wolcott in Wayne County, Jordan in Onondaga County, Canandaigua and Geneva in Ontario County, Penn Yan in Yates County, Waterloo in Seneca County, Fairport in Monroe County, and Auburn in Cayuga County. The Lyons National Bank has one subsidiary, Lyons Realty Associates Corp.

STOCK SYMBOL

LYBC

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