Cornerstone Bancorp, Inc. and Subsidiary

Consolidated Financial Report

December 31, 2018

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Independent Auditor's Report

To the Board of Directors
Cornerstone Bancorp, Inc. and Subsidiary

We have audited the accompanying consolidated financial statements of Cornerstone Bancorp, Inc. and Subsidiary (the "Corporation"), which comprise the consolidated balance sheet as of December 31, 2018 and 2017 and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

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

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

To the Board of Directors
Cornerstone Bancorp, Inc. and Subsidiary

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Cornerstone Bancorp, Inc. and Subsidiary as of December 31, 2018 and 2017 and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Plante & Moran, PLLC

March 15, 2019

Cornerstone Bancorp, Inc. and Subsidiary

Consolidated Balance Sheet

	December 31, 2018	December 31, 2017
Assets		
Cash and cash equivalents	$ 45,540,801	$ 24,102,875
Investment securities - Available-for-sale (Note 2)	99,446,645	132,400,655
Other securities	1,148,400	1,108,400
Loans held for sale	1,005,700	1,224,898
Loans, net of allowance for loan losses (Note 3)	413,806,182	369,095,051
Premises and equipment (Note 4)	3,210,222	3,244,986
Accrued interest receivable	1,681,074	1,676,748
Other real estate owned	513,625	240,000
Other assets	2,541,968	2,414,424
Total assets	**$ 568,894,617**	**$ 535,508,037**
Liabilities and Stockholders' Equity		
Liabilities		
Deposits:		
Noninterest-bearing deposits	$ 147,707,994	$ 136,461,133
Interest-bearing deposits	360,094,842	335,306,302
Total deposits (Note 5)	507,802,836	471,767,435
Securities sold under agreements to repurchase	4,416,601	6,948,232
Junior subordinated debentures (Note 6)	10,310,000	10,310,000
Borowings under line of credit (Note 10)	2,500,000	-
Accrued interest payable	138,670	43,580
Other liabilities	1,945,971	1,318,189
Total liabilities	527,114,078	490,387,436
Stockholders' Equity		
Preferred Stock - $0.001 par value:		
Authorized - 500,000 shares	-	-
No shares issued or outstanding at December 31, 2018 or 2017		
Common stock - $.001 par value:		
Authorized - 1,000,000 shares		
Issued - 751,840 shares at December 31, 2018 and 2017		
Outstanding - 706,713 and 693,671 shares at December 31, 2018 and 2017, respectively	752	752
Additional paid-in capital	20,116,333	19,900,245
Retained earnings	25,157,772	29,203,336
Accumulated other comprehensive loss	(553,364)	(467,790)
Treasury stock - 45,127 and 58,169 shares at December 31, 2018 and 2017, respectively	(2,940,954)	(3,515,942)
Total stockholders' equity	41,780,539	45,120,601
Total liabilities and stockholders' equity	**$ 568,894,617**	**$ 535,508,037**

Consolidated Statement of Income

	Year Ended December 31, 2018	Year Ended December 31, 2017
Interest Income		
Loans, including fees	$ 20,334,668	$ 15,906,415
Investment securities	2,535,285	2,840,062
Total interest income	22,869,953	18,746,477
Interest Expense		
Deposits	2,417,944	1,329,739
Securities sold under agreements to repurchase	16,347	12,064
Borrowings under line of credit	43,291	-
Junior subordinated debentures	538,402	416,938
Total interest expense	3,015,984	1,758,741
Net Interest Income - Before provision for loan losses	19,853,969	16,987,736
Provision for Loan Losses (Note 3)	(400,000)	(800,000)
Net Interest Income - After provision for loan losses	20,253,969	17,787,736
Noninterest Income		
Service charges on deposits	646,557	592,968
Trust fees	2,935,593	2,524,191
Gains on sales of loans held for sale	545,465	871,497
Other operating	253,431	282,100
Total noninterest income	4,381,046	4,270,756
Noninterest Expenses		
Salaries and employee benefits (Notes 8 and 9)	11,071,719	9,770,119
Occupancy (Note 4)	991,804	925,949
Data processing	1,211,752	1,113,908
Mortgage commissions and third-party fees	230,775	359,132
Legal, audit, and professional fees	379,289	498,004
Other real estate owned	96,165	799
Regulatory assessments	315,579	311,788
Other operating	1,364,111	1,374,732
Total noninterest expenses	15,661,194	14,354,431
Income - Before income tax expense	8,973,821	7,704,061
Income Tax Expense (Note 7)	2,433,690	3,437,894
Net Income	**$ 6,540,131**	**$ 4,266,167**

Cornerstone Bancorp, Inc. and Subsidiary

Consolidated Statement of Comprehensive Income

	Year Ended	
	December 31, 2018	December 31, 2017
Net Income	$ 6,540,131	$ 4,266,167
Other Comprehensive Income (Loss):		
Unrealized holding gains (losses) on investment securities - Available-for-sale	126,558	(35,201)
Unrealized holding losses on interest rate swap	(246,232)	-
Tax effect	34,100	13,665
Other Comprehensive Loss - Net of tax	(85,574)	(21,536)
Comprehensive Income	**$ 6,454,557**	**$ 4,244,631**

Consolidated Statement of Stockholders' Equity

	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity
Balance - January 1, 2017	$ 752	$ 19,831,821	$ 31,786,401	$ (378,776)	$ (3,401,610)	$ 47,838,588
Net income	-	-	4,266,167	-	-	4,266,167
Other comprehensive loss, net	-	-	-	(21,536)	-	(21,536)
Dividends paid	-	-	(6,916,710)	-	-	(6,916,710)
Early adoption of Accounting Standard Update 2018-02 (Note 1)	-	-	67,478	(67,478)	-	-
Redemption - 3,667 shares of common stock	-	-	-	-	(267,444)	(267,444)
Issuance - 3,188 shares of treasury stock	-	68,424	-	-	153,112	221,536
Balance - December 31, 2017	752	19,900,245	29,203,336	(467,790)	(3,515,942)	45,120,601
Net income	-	-	6,540,131	-	-	6,540,131
Other comprehensive loss, net	-	-	-	(85,574)	-	(85,574)
Dividends paid	-	-	(10,585,695)	-	-	(10,585,695)
Redemption - 2,210 shares of common stock	-	-	-	-	(190,060)	(190,060)
Issuance - 15,252 shares of treasury stock	-	216,088	-	-	765,048	981,136
Balance - December 31, 2018	**$ 752**	**$ 20,116,333**	**$ 25,157,772**	**$ (553,364)**	**$ (2,940,954)**	**$ 41,780,539**

Cornerstone Bancorp, Inc. and Subsidiary

Consolidated Statement of Cash Flows

	Year Ended	
	December 31, 2018	December 31, 2017
Cash Flows from Operating Activities		
Net income	$ 6,540,131	$ 4,266,167
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization on premises and equipment	216,548	240,810
Provision for loan losses	(400,000)	(800,000)
Amortization and accretion on securities - Net	901,247	951,079
Losses (Gains) on sale of other real estate owned	7,492	(41,620)
Gains on sales of loans held for sale	(545,465)	(871,497)
Originations of loans held for sale	(35,519,988)	(44,690,262)
Proceeds from sale of loans held for sale	35,624,620	46,896,801
Deferred income tax (benefit) expense	(433,838)	178,676
Change in enacted tax rate	-	648,748
Changes in operating assets and liabilities that provided (used) cash:		
Accrued interest receivable	(4,326)	(125,272)
Other assets	340,394	(421,327)
Accrued interest payable	95,090	10,165
Other liabilities	381,550	128,666
Net cash provided by operating activities	7,203,455	6,371,134
Cash Flows from Investing Activities		
Activity in available-for-sale investment securities:		
Maturities, prepayments, and calls	42,292,297	7,799,655
Purchases	(10,112,976)	(4,982,726)
Maturity of interest-bearing deposits in banks	-	249,000
(Purchase) redemption of Federal Home Loan Bank stock	(40,000)	73,000
Net increase in loans	(44,164,725)	(48,976,921)
Proceeds from sale of other real estate owned	232,508	516,620
Additions to premises and equipment	(181,784)	(178,996)
Net cash used in investing activities	(11,974,680)	(45,500,368)
Cash Flows from Financing Activities		
Net change in deposits	36,035,401	6,331,489
Net change in securities sold under agreements to repurchase	(2,531,631)	2,201,429
Borrowings under line of credit	2,500,000	-
Dividends paid on common stock	(10,585,695)	(6,916,710)
Redemption of treasury stock	(190,060)	(267,444)
Issuance of treasury stock	981,136	221,536
Net cash provided by financing activities	26,209,151	1,570,300
Net Change in Cash and Cash Equivalents	21,437,926	(37,558,934)
Cash and Cash Equivalents - Beginning of year	24,102,875	61,661,809
Cash and Cash Equivalents - End of year	**$ 45,540,801**	**$ 24,102,875**
Supplemental Cash Flow and Noncash Information		
Cash paid for:		
Interest	2,920,894	$ 1,748,576
Income taxes	2,625,000	2,971,420
Noncash transactions		
Net transfer of loans to other real estate owned	134,608	-
Loans held-for-sale transferred to loans, net	660,031	656,942

Note 1 – Nature of Business and Significant Accounting Policies

Nature of Operations - Cornerstone Bancorp, Inc. (the "Corporation") and its wholly owned subsidiary, Cornerstone National Bank & Trust Company (the "Bank"), provide a variety of financial services to individuals and businesses in the Chicago metropolitan area through their main office in Palatine, Illinois, and branch offices in Crystal Lake, Lake Zurich, and Naperville Illinois. Their primary deposit products are demand deposits, savings, money market, and term certificate accounts, and their primary lending products are commercial and commercial mortgage loans. The Corporation has a mortgage banking operation in which residential mortgage loans are originated and sold to the secondary market.

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

Basis of Presentation and Consolidation - The consolidated financial statements include the accounts of the Corporation and the Bank. All significant intercompany balances and transactions have been eliminated in consolidation.

Cash and Cash Equivalents - For the purpose of the consolidated statement of cash flows, cash and cash equivalents include cash and balances due from banks and federal funds sold which have original maturities within 90 days.

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

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

Other Securities - Other securities consist of Federal Home Loan Bank and Federal Reserve Bank Stock. These investments are restricted as to redemption and are carried at cost.

Loans Held for Sale - Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses, if any, are recognized in a valuation allowance by charges to income. For the years ended December 31, 2018 and 2017, the majority of such loans were sold to three investors.

Loans - The Corporation grants mortgage, commercial, and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans in the Chicago metropolitan area. The ability of the Corporation's debtors to honor their contracts is partially dependent upon the real estate and general economic conditions in this area.

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

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding unpaid principal balances adjusted for chargeoffs, the allowance for loan losses, and any deferred fees or costs on originated loans. 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 to the related loan yield using the interest method.

The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent unless the credit is well secured and in process of collection. 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 reversed against interest income. 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.

Loans are considered delinquent when customers fail to make their payments in accordance with the contractual loan agreement. If a loan matures and principal remains outstanding, the loan is considered delinquent until the loan is paid off or renewed.

Gross loans are reported at the Corporation’s recorded investment. The recorded investment is the borrower’s principal balance less partial charge-offs, if any.

Allowance for Loan Losses - The allowance for loan losses (the “allowance”) is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses 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 specific, general, and unallocated components. The specific component relates to loans that are classified as either doubtful, substandard, or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan are lower than the carrying value of that loan. The general component covers nonimpaired loans and is based on historical loss experience adjusted for qualitative factors. 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 specific and general losses in the portfolio.

A loan is considered impaired when, based on current information and events, it is probable that the Corporation 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. 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 length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the

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

shortfall in relation to the principal and interest owed. Specific reserves are measured on a loan-by-loan basis for impaired loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of homogeneous loans are collectively evaluated for impairment. Accordingly, the Corporation does not separately identify individual consumer loans for impairment disclosures.

Troubled debt restructuring of loans is undertaken to improve the likelihood that the loan will be repaid in full under the modified terms in accordance with a reasonable repayment schedule. All modified loans are evaluated to determine whether the loans should be reported as a Troubled Debt Restructure (TDR). A loan is a TDR when the Corporation, for economic or legal reasons related to the borrower’s financial difficulties, grants a concession to the borrower by modifying or renewing a loan under terms that the Corporation would not otherwise consider. To make this determination, the Corporation must determine whether (a) the borrower is experiencing financial difficulties and (b) the Corporation granted the borrower a concession. This determination requires consideration of all of the facts and circumstances surrounding the modification. An overall general decline in the economy or some deterioration in a borrower’s financial condition does not automatically mean the borrower is experiencing financial difficulties.

Premises and Equipment - Land is carried at cost. Buildings and equipment are carried at cost, less accumulated depreciation computed on the straight-line method over the estimated useful lives of the assets, ranging from 3 years to 40 years.

Other Real Estate Owned - Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value less costs to sell at the date of the foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less costs to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from other real estate owned.

Securities Sold Under Agreements to Repurchase - Securities sold under agreements to repurchase, which are classified as secure borrowings, generally mature within one to four days from the transaction date. Securities sold under agreements to repurchase are reflected at the amount of cash received in connection with the transaction. The Corporation may be required to provide additional collateral based on the fair value of the underlying securities.

Treasury Stock - Treasury stock represents shares of the Corporation that were repurchased. These shares are carried at cost and are reissued using the first-in-first-out method.

Income Taxes - Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the various temporary differences between the book and tax basis of the various consolidated balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws.

At December 31, 2018 and 2017, the Corporation evaluated tax positions taken for filing with the Internal Revenue Service and all state jurisdictions in which it operates. The Corporation believes that income tax filing positions will be sustained under examination and does not anticipate any adjustments that would result in a material adverse effect on the Corporation’s financial condition, results of operations, or cash flows. Accordingly, the Corporation has not recorded any reserves or related accruals for interest and penalties for uncertain tax positions at December 31, 2018 and 2017.

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

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, such as unrealized gains and losses on available-for-sale securities and certain interest rate swap agreements, are reported as a separate component of the equity section of the consolidated balance sheet, such items, along with net income, are components of comprehensive income. At December 31, 2018, the components of accumulated other comprehensive loss consist of net unrealized holding losses on securities available-for-sale of $527,740, unrealized holding losses on interest rate swap contracts of $246,233, and a net income tax benefit of $220,609.

In February 2018, the Financial Accounting Standards Board issued Accounting Standards Update ("ASU") 2018-02, *Income Statement – Reporting Comprehensive Income: Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. The ASU would require a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the newly enacted federal corporate income tax rate. The amendments in this standard are effective for years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted, including adoption in any interim period, for which financial statements have not been issued or made available for issuance. The Corporation early adopted the standard as of December 31, 2017 with a reclassification entry in the statement of equity between accumulated other comprehensive income and retained earnings.

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 Corporation, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of the right) to pledge or exchange the transferred assets, and (3) the Corporation does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Advertising Costs - All advertising costs incurred by the Corporation are expensed in the period in which they are incurred.

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

Stock Option Plan - The Corporation measures the cost of employee services received in exchange for equity awards, including stock options, based on the calculated grant date fair value of the awards. The cost is recognized as compensation expense over the vesting period of the awards.

Trust Assets - Assets held by the Corporation in a fiduciary, agency, or custody capacity for its trust department customers are not included in the accompanying consolidated financial statements since such items are not assets of the Corporation. Income and expense of the Corporation are recognized when earned or incurred, respectively.

Subsequent Events - The consolidated financial statements and related disclosures include evaluation of events up through and including March 15, 2019, which is the date the consolidated financial statements were available to be issued.

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

Recent Accounting Pronouncements – In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which will supersede the current revenue recognition requirements in Topic 605, *Revenue Recognition*. The ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. The new guidance will be effective for the Corporation's year ending December 31, 2019. The ASU permits application of the new revenue recognition guidance to be applied using one of two retrospective application methods. The Corporation has determined this standard will not have a significant impact on the financial statement as most of the Corporation's revenue sources are scoped out of the standard.

In January 2016, the FASB issued ASU No. 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*. The ASU covers various changes to the accounting, measurement, and disclosures related to certain financial instruments, including requiring equity investments to be accounted for at fair value with changes recorded through earnings, the use of the exit price when measuring fair value, and disaggregation of financial assets and liabilities by category for disclosure purposes. The new guidance is effective for the Corporation's year ending December 31, 2019. The adoption of this ASU is not expected to have a material impact on the consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*, which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right of use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The reporting of lease related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for the Corporation's year ending December 31, 2020 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The new lease standard is expected to have a significant effect on the Corporation's financial statements as a result of the leases for the Bank's two branches and its business banking center, currently classified as operating leases. The effect of applying the new lease guidance on the financial statements will require the Corporation to record a lease obligation for the operating leases described in Note 4, with a corresponding right to use asset. The exact impact on the financial statements has not yet been determined.

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

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses: Measurement of Credit Losses on Financial Instruments*. The ASU includes increased disclosures and various changes to the accounting and measurement of financial assets including the Corporation's loans and available-for-sale debt securities. Each financial asset presented on the balance sheet would have a unique allowance for credit losses valuation account that is deducted from the amortized cost basis to present the net carrying value at the amount expected to be collected on the financial asset. The amendments in this ASU also eliminate the probable initial recognition threshold in current GAAP and, instead, reflect an entity's current estimate of all expected credit losses using reasonable and supportable forecasts. The new credit loss guidance will be effective for the Corporation's year ending December 31, 2022. Upon adoption the ASU will be applied using a modified retrospective transition method to the beginning of the first reporting period in which the guidance is effective. A prospective transition approach is required for debt securities for which an other-than-temporary impairment had been recognized before the effective date. Early adoption for all institutions is permitted for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. This standard is expected to have a significant effect on the Corporation's consolidated financial statements. The Corporation is assessing the impact of ASU 2016-13 on its accounting and disclosures, and has determined that a loss rate model will be used for calculation of future risk assessments upon the ASU's adoption in 2022. The Corporation has accumulated historical data by loan pools and collateral classifications, and anticipates calculation of estimates in 2019 through 2021 on a test basis to confirm model processes and to determine financial statement impact prior to adoption in 2022.

In August 2017, the FASB issued ASU No. 2017-12, *Derivatives and Hedging (Topic 815)*, to permit entities to better portray the economic results of their hedging strategies in their financial statements. In addition, the amendments make certain targeted improvements to simplify the application of the hedge accounting guidance in current GAAP. One of the targeted improvements of the ASU eliminates the Corporation's requirement to measure and reclassify ineffective portions of a cash flow hedge to earnings. The amendment is effective for fiscal years beginning after December 15, 2019, with early adoption permitted, including adoption in an interim period. The Corporation has chosen to early adopt this amendment in connection with the interest rate swap that commenced in July 2018 with no material impact on its results of operation, financial position, or liquidity.

Note 2 - Investment Securities

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

	December 31, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Securities Available-for-Sale				
U.S. government agencies	$ 22,052,842	$ 70,178	$ (75,103)	$ 22,047,917
Mortgage-backed securities and collateralized mortgage obligations	2,461,904	683	(67,594)	2,394,993
State and municipal securities	61,415,533	80,397	(463,718)	61,032,212
Corporate debt securities	13,044,106	-	(52,235)	12,991,871
Community reinvestment fund	1,000,000	-	(20,348)	979,652
Total	$ 99,974,385	$ 151,258	$ (678,998)	99,446,645

	December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Securities Available-for-Sale				
U.S. government agencies	$ 49,957,873	$ 110,653	$ (89,455)	$ 49,979,071
Mortgage-backed securities and collateralized mortgage obligations	2,826,974	1,973	(44,749)	2,784,198
State and municipal securities	62,027,250	32,857	(642,116)	61,417,991
Corporate debt securities	17,242,856	1,544	(27,462)	17,216,938
Community reinvestment fund	1,000,000	2,457	-	1,002,457
Total	$ 133,054,953	$ 149,484	$ (803,782)	$ 132,400,655

At December 31, 2018 and 2017, securities with a carrying value of approximately $12,714,000 and $13,968,000, respectively, were pledged to secure repurchase agreements, borrowings, public deposits and for other purposes required or permitted by law.

Note 2 - Investment Securities (Continued)

The amortized cost and estimated fair value of debt securities by contractual maturity at December 31, 2018 are as follows:

	December 31, 2018	
	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 27,885,244	$ 27,814,120
Due after one year through five years	67,640,116	67,283,052
Due after five years through ten years	987,121	974,828
Total	96,512,481	96,072,000
Community reinvestment fund	1,000,000	979,652
Mortgage-backed securities and collateralized mortgage obligations	2,461,904	2,394,993
Total	$ 99,974,385	$ 99,446,645

There were no sales of investments in 2018 or 2017.

Note 2 - Investment Securities (Continued)

Information pertaining to securities with gross unrealized losses at December 31, 2018 and 2017, aggregated by investment category and length of time that individual securities have been in a continuous loss position, is as follows:

	December 31, 2018			
	<12 Months		>12 Months	
	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value
U.S. government agencies	$ (428)	$ 983,872	$ (74,675)	$ 9,944,740
Mortgage-backed securities and collateralized mortgage obligations	(1,539)	186,784	(66,055)	2,181,708
State and municipal securities	(24,913)	6,547,766	(438,805)	41,622,458
Corporate debt securities	(12,293)	974,828	(39,942)	12,017,043
Community reinvestment fund	(20,348)	979,652	-	-
Total	$ (59,521)	$ 9,672,902	$ (619,477)	$ 65,765,949

	December 31, 2017			
	<12 Months		>12 Months	
	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value
U.S. government agencies	$ (81,563)	$ 35,048,185	$ (7,892)	$ 4,988,605
Mortgage-backed securities and collateralized mortgage obligations	-	-	(44,749)	2,556,926
State and municipal securities	(475,558)	43,973,733	(166,558)	8,287,318
Corporate debt securities	(27,462)	14,211,852	-	-
Total	$ (584,583)	$ 93,233,770	$ (219,199)	$ 15,832,849

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

Other securities, totaling $1,148,400 and $1,108,400 at December 31, 2018 and 2017, consist of restricted Federal Home Loan Bank and Federal Reserve Bank stock. These stocks are carried at cost, which approximates fair value.

Note 3 - Loans

A summary of the balances of loans follows:

	December 31	
	2018	2017
Mortgage loans on real estate:		
1-4 family residential	$ 57,846,627	$ 63,126,952
Commercial	212,425,254	179,054,252
Construction and land development	3,959,642	8,667,508
Vacant land and farm land	2,104,314	2,273,201
Multi-family residential	26,297,944	26,910,901
Total mortgage loans on real estate	302,633,781	280,032,814
Commercial and industrial loans	115,662,782	93,705,414
Consumer loans	1,433,453	831,030
Cash secured loans	1,606,912	1,300,160
Total loans	421,336,928	375,869,418
Less allowance for loan losses	6,989,739	6,456,437
Net deferred loan fees	541,007	317,930
Total loans, net	$ 413,806,182	$ 369,095,051

In the ordinary course of business, the Bank has granted loans to principal officers and directors and their affiliates amounting to approximately $801,000 at December 31, 2018 and $1,612,000 at December 31, 2017.

Note 3 - Loans (Continued)

Activity in the allowance for loan losses for 2018 and 2017 is summarized as follows:

	Year Ended December 31, 2018				
	Beginning Balance	Charge-Offs	Recoveries	Provision	Ending Balance
Allowance for loan losses:					
Commercial and industrial	$ 1,355,943	$ -	$ 157,870	$ 24,976	$ 1,538,789
Consumer	11,898	-	-	7,754	19,652
Construction and land development	130,135	-	-	(66,364)	63,771
Commerical real estate	3,540,241	-	775,432	(285,199)	4,030,474
1-4 family residential	999,318	-	-	(159,068)	840,250
Multi-family residential	336,386	-	-	13,377	349,763
Vacant land and farm land	35,235	-	-	(935)	34,300
Unallocated	47,281	-	-	65,459	112,740
Total	$ 6,456,437	$ -	$ 933,302	$ (400,000)	$ 6,989,739

	Year Ended December 31, 2017				
	Beginning Balance	Charge-Offs	Recoveries	Provision	Ending Balance
Allowance for loan losses:					
Commercial and industrial	$ 1,180,385	$ (782,020)	$ -	$ 957,578	$ 1,355,943
Consumer	16,373	-	13,274	(17,749)	11,898
Construction and land development	110,692	-	-	19,443	130,135
Commerical real estate	4,570,651	-	58,230	(1,088,640)	3,540,241
1-4 family residential	1,315,555	-	196,607	(512,844)	999,318
Multi-family residential	291,532	-	171,810	(126,956)	336,386
Vacant land and farm land	52,084	-	-	(16,849)	35,235
Unallocated	61,264	-	-	(13,983)	47,281
Total	$ 7,598,536	$ (782,020)	$ 439,921	$ (800,000)	$ 6,456,437

Note 3 - Loans (Continued)

The allowance for loan losses and loan balances as of December 31, 2018 and 2017 are as follows:

	Year Ended December 31, 2018		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Ending Balance
Ending allowance attributable to loans:			
Commercial and industrial	$ -	$ 1,538,789	$ 1,538,789
Consumer	-	19,652	19,652
Construction and land development	-	63,771	63,771
Commerical real estate	-	4,030,474	4,030,474
1-4 family residential	-	840,250	840,250
Multi-family residential	-	349,763	349,763
Vacant land and farm land	-	34,300	34,300
Unallocated	-	112,740	112,740
Total	$ -	$ 6,989,739	$ 6,989,739
Ending loans:			
Commercial and industrial	$ 1,011,751	$ 114,651,031	$ 115,662,782
Consumer	-	1,433,453	1,433,453
Construction and land development	273,448	3,686,194	3,959,642
Commerical real estate	3,770,792	208,654,462	212,425,254
1-4 family residential	575,244	57,271,383	57,846,627
Multi-family residential	-	26,297,944	26,297,944
Vacant land and farm land	-	2,104,314	2,104,314
Cash secured	-	1,606,912	1,606,912
Total	$ 5,631,235	$ 415,705,693	$ 421,336,928

Note 3 - Loans (Continued)

	Year Ended December 31, 2017		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Ending Balance
Ending allowance attributable to loans:			
Commercial and industrial	$ -	$ 1,355,943	$ 1,355,943
Consumer	-	11,898	11,898
Construction and land development	-	130,135	130,135
Commerical real estate	-	3,540,241	3,540,241
1-4 family residential	-	999,318	999,318
Multi-family residential	-	336,386	336,386
Vacant land and farm land	-	35,235	35,235
Unallocated	-	47,281	47,281
Total	$ -	$ 6,456,437	$ 6,456,437
Ending loans:			
Commercial and industrial	$ 2,745,653	$ 90,959,761	$ 93,705,414
Consumer	-	831,030	831,030
Construction and land development	780,562	7,886,946	8,667,508
Commerical real estate	5,554,403	173,499,849	179,054,252
1-4 family residential	542,684	62,584,268	63,126,952
Multi-family residential	-	26,910,901	26,910,901
Vacant land and farm land	-	2,273,201	2,273,201
Cash secured	-	1,300,160	1,300,160
Total	$ 9,623,302	$ 366,246,116	$ 375,869,418

Note 3 - Loans (Continued)

Credit Risk Rating

The following is a summary of the loan portfolio by loan risk grades at December 31, 2018 and 2017:

	December 31, 2018				
	Pass	Special Mention	Substandard	Doubtful	Total
Commercial and industrial	$ 114,651,031	$ 351,624	$ 660,127	$ -	$ 115,662,782
Consumer	1,433,453	-	-	-	1,433,453
Construction and land development	3,686,194	-	273,448	-	3,959,642
Commerical real estate	208,654,462	1,431,617	2,339,175	-	212,425,254
1-4 family residential	57,271,383	-	575,244	-	57,846,627
Multi-family residential	26,297,944	-	-	-	26,297,944
Vacant land and farm land	2,104,314	-	-	-	2,104,314
Cash secured	1,606,912	-	-	-	1,606,912
Total	$ 415,705,693	$ 1,783,241	$ 3,847,994	$ -	$ 421,336,928

	December 31, 2017				
	Pass	Special Mention	Substandard	Doubtful	Total
Commercial and industrial	$ 90,959,761	$ 2,665,000	$ 80,653	$ -	$ 93,705,414
Consumer	831,030	-	-	-	831,030
Construction and land development	7,886,946	-	780,562	-	8,667,508
Commerical real estate	174,732,046	775,559	3,546,647	-	179,054,252
1-4 family residential	62,584,268	28,691	513,993	-	63,126,952
Multi-family residential	26,910,901	-	-	-	26,910,901
Vacant land and farm land	2,273,201	-	-	-	2,273,201
Cash secured	1,300,160	-	-	-	1,300,160
Total	$ 367,478,313	$ 3,469,250	$ 4,921,855	$ -	$ 375,869,418

The Corporation categorized each loan into credit risk categories based on current financial information, overall debt service coverage, comparison against industry averages, collateral coverage, historical payment experience, and current economic trends. The Corporation uses the following definitions for credit risk ratings:

Pass - Credits not covered by the definitions presented below are pass credits, which are not considered to be adversely rated.

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

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

Note 3 - Loans (Continued)

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

Age Analysis of Past Due and Nonaccrual Loans

The following tables detail the age analysis of past due and nonaccrual loans at December 31, 2018 and 2017:

	Year Ended December 31, 2018						
	Loans on Accrual Status						
	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days	Nonaccrual Loans	Total Past Due and Nonaccrual	Current	Total Loans Receivable
Commercial and industrial	$ -	$ -	$ -	$ 65,127	$ 65,127	$ 115,597,655	$ 115,662,782
Consumer	-	-	-	-	-	1,433,453	1,433,453
Construction and land development	-	-	-	273,448	273,448	3,686,194	3,959,642
Commercial real estate	-	-	-	2,046,721	2,046,721	210,378,533	212,425,254
1-4 family residential	-	-	-	575,244	575,244	57,271,383	57,846,627
Multi-family residential	-	-	-	-	-	26,297,944	26,297,944
Vacant land and farm land	-	-	-	-	-	2,104,314	2,104,314
Cash secured	-	-	-	-	-	1,606,912	1,606,912
Total	$ -	$ -	$ -	$ 2,960,540	$ 2,960,540	$ 418,376,388	$ 421,336,928

	Year Ended December 31, 2017						
	Loans on Accrual Status						
	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days	Nonaccrual Loans	Total Past Due and Nonaccrual	Current	Total Loans Receivable
Commercial and industrial	$ -	$ -	$ -	$ 80,653	$ 80,653	$ 93,624,761	$ 93,705,414
Consumer	-	-	-	-	-	831,030	831,030
Construction and land development	-	-	-	780,562	780,562	7,886,946	8,667,508
Commercial real estate	1,350,068	-	-	2,196,579	3,546,647	175,507,605	179,054,252
1-4 family residential	-	-	-	150,267	150,267	62,976,685	63,126,952
Multi-family residential	-	-	-	-	-	26,910,901	26,910,901
Vacant land and farm land	-	-	-	-	-	2,273,201	2,273,201
Cash secured	-	-	-	-	-	1,300,160	1,300,160
Total	$ 1,350,068	$ -	$ -	$ 3,208,061	$ 4,558,129	$ 371,311,289	$ 375,869,418

Note 3 - Loans (Continued)

Impaired Loans

A loan is considered impaired when it is probable that not all principal and interest amounts will be collected according to the loan contract. Individual commercial loans are evaluated for impairment. Impaired loans are written down by the establishment of a specific allowance where necessary.

The Corporation had $655,000 additional funds committed to be advanced in connection with impaired loans at December 31, 2018. The Corporation had no additional funds committed to be advanced in connection with impaired loans at December 31, 2017.

Information regarding impaired loans is as follows as of and for the years ended December 31, 2018 and 2017:

	Year Ended December 31, 2018				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial and industrial	$ 660,127	$ 668,227	$ -	$ 813,136	$ 27,511
Construction and land development	273,448	824,656	-	307,320	-
Commercial real estate	2,339,175	2,617,390	-	2,425,011	10,196
1-4 family residential	575,244	646,425	-	589,566	11,936
Total	$ 3,847,994	$ 4,756,698	$ -	$ 4,135,033	$ 49,643

	Year Ended December 31, 2017				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial and industrial	$ 80,653	$ 80,653	$ -	$ 901,021	$ 33,395
Construction and land development	780,562	1,283,027	-	866,329	-
Commercial real estate	3,546,647	3,721,437	-	3,607,683	57,357
1-4 family residential	150,267	487,842	-	179,440	-
Total	$ 4,558,129	$ 5,572,959	$ -	$ 5,554,473	$ 90,752

For purposes of the disclosure above, recorded investment represents the borrowers unpaid principal balance, less partial charge-offs to date.

Note 3 - Loans (Continued)

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. The Corporation offers various types of concessions when modifying a loan; however, forgiveness of principal is rarely granted.

The following tables present information related to loans modified in a TDR during the years ended December 31, 2018 and 2017:

	Year Ended December 31, 2018		
Type of Loan	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial and industrial	2	$ 73,227	$ 65,127

	Year Ended December 31, 2017		
Type of Loan	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial real estate	2	$ 2,177,215	$ 2,014,536

None of the troubled debt restructurings that were modified or renewed during 2018 or 2017 subsequently defaulted.

Note 4 - Premises and Equipment

A summary of the cost and accumulated depreciation and amortization of premises and equipment at December 31 is as follows:

	2018	2017
Land	$ 810,000	$ 810,000
Buildings and building improvements	4,371,486	4,296,108
Furniture, fixtures, and equipment	2,299,204	2,247,962
Leasehold improvements	312,071	305,966
Total premises and equipment	7,792,761	7,660,036
Accumulated depreciation	(4,582,539)	(4,415,050)
Net premises and equipment	$ 3,210,222	$ 3,244,986

The Bank operates its Crystal Lake and Lake Zurich branch facilities, its Naperville business banking center, and a loan operations center subject to operating leases. Future minimum rental commitments under these leases are as follows:

2019	$ 265,099
2020	200,963
2021	182,650
2022	84,577
2023	41,533
Thereafter	-
Total	$ 774,822

The Crystal Lake lease expires in December 2021 and contains a three-year option to extend with an increase to the base rent of 2.5% per year.

The Lake Zurich lease expires in March 2020 and contains a two-year option to extend with an increase to the base rent of 2.8% per option period.

The Naperville lease expires in June 2022 and contains two options to extend the term of the lease for five years at the conclusion of the initial lease term at a market rate of rent in effect at the commencement of each option period.

The loan operations center lease expires in October 2023 and contains two options to extend the term of the lease for five years at the conclusion of the initial lease term with an increase to the base rent of 2.0% per year.

Total rent expense approximated $242,000 and $233,000 for the years ended December 31, 2018 and 2017, respectively.

Note 5 - Deposits

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

	2018	2017
Noninterst-bearing deposits	$ 147,707,994	$ 136,461,133
NOW accounts	56,188,245	55,291,727
Savings and money market accounts	245,607,735	241,778,364
Time:		
Under $250,000	35,046,169	21,388,758
$250,000 and over	23,252,693	16,847,453
Total	$ 507,802,836	$ 471,767,435

At December 31, 2018, the scheduled maturities of time deposits are as follows:

2019	$ 38,863,096
2020	13,747,174
2021	2,104,436
2022	2,255,733
2023	1,328,423
Total	$ 58,298,862

Deposits from related parties held by the Corporation totaled approximately $24,511,000 and $23,007,000 at December 31, 2018 and 2017, respectively.

Note 6 - Junior Subordinated Debentures

The Corporation has established a Delaware statutory trust (the "Trust") for the sole purpose of issuing trust-preferred securities and related trust common securities. The proceeds from the issuance were used by the Trust to purchase junior subordinated debentures of the Corporation, which is the sole asset of the Trust. Concurrently with the issuance of the trust-preferred securities, the Corporation issued guarantees for the benefit of the holders of the trust-preferred securities. The trust-preferred securities are issues that qualify, and are treated by the Corporation, as Tier I regulatory capital. The Corporation wholly owns all of the common securities of the Trust. The trust-preferred securities issued by the Trust rank equally with the common securities in right of payment, except that if an event of default under the indenture governing the debentures has occurred and is continuing, the preferred securities will rank senior to the common securities in right of payment.

At December 31, 2018 and 2017, the outstanding balance of the junior subordinated debentures was $10,310,000. The subordinated debentures have a stated maturity date of March 31, 2034 and a floating interest rate per annum reset quarterly equal to the three-month LIBOR plus 2.85% (5.65% at December 31, 2018 and 4.54% at December 31, 2017). Interest is payable quarterly and all payments have been paid as agreed.

In 2018, the Corporation entered into an interest rate swap contract with a notional value of $5,000,000 to convert a portion of its junior subordinated debentures to a fixed rate of interest. The swap contract expires with the maturity of the underlying junior subordinated debentures and carries a fixed rate of 5.997%. The interest rate swap qualifies as a cash flow hedge and, as a result, the unrealized gain (loss) on the swap instrument is reflected in other comprehensive income (loss) until the swap is terminated or matures. At December 31, 2018, an unrealized loss of $246,233 was recorded in other comprehensive income.

The trust-preferred securities are subject to mandatory redemption, in whole or in part, upon repayment of the junior subordinated debentures at the stated maturity date or upon redemption. The debentures are callable by the Corporation with 90 days' notice to the holders. The Trust's ability to pay amounts due on the trust-preferred securities is solely dependent upon the Corporation making payment on the related junior subordinated debentures. The Corporation has the right to defer payment of interest on the debentures.

The Corporation's obligation under the junior subordinated debentures and other relevant trust agreements, in aggregate, constitutes a full and unconditional guarantee by the Corporation of the Trust's obligations under the trust-preferred securities issued by the Trust.

Note 7 - Income Taxes

The components of the net deferred tax asset, included in other assets at December 31, are as follows:

	2018	2017
Deferred tax assets:		
Allowance for loan losses	$ 1,723,728	$ 1,370,184
Deferred compensation	192,090	138,874
Nonaccrual loan interest	139,934	114,752
Net unrealized loss on securities available for sale and interest rate swap	220,609	186,509
Total deferred tax assets	2,276,361	1,810,319
Deferred tax liabilities:		
Depreciation and amortization	90,233	74,540
Accretion on securities available for sale	111,696	130,088
Prepaid expenses	27,129	26,326
Total deferred tax liabilities	229,058	230,954
Net deferred tax asset	$ 2,047,303	$ 1,579,365

The allocation of income taxes between current and deferred portions at December 31 is as follows:

	2018	2017
Current expense	$ 2,867,528	$ 2,610,470
Deferred (benefit) expense	(433,838)	178,676
Change in enacted tax rate	-	648,748
Total	$ 2,433,690	$ 3,437,894

In late December 2017, the “Tax Cuts and Jobs Act” was enactment and required the revaluation of the Corporation’s deferred tax assets and liabilities at the new corporate income tax rates. The revaluation triggered a nonrecurring, noncash charge of $648,748 recorded as tax expense in 2017. This revaluation also affected the impact to deferred tax assets or liabilities related to items presented in accumulated other comprehensive income.

Note 7 - Income Taxes (Continued)

The reason for the differences between income tax expense at the federal statutory income tax rate and the recorded income tax expense at December 31 are summarized as follows:

	2018	2017
Income tax calculated at statutory rate (21% - 2018; 34% - 2017)	$ 1,884,503	$ 2,619,381
Add (subtract) tax effect of:		
State income tax - net of federal tax benefit	811,204	414,601
Tax-exempt securities	(196,386)	(339,631)
Meals, entertainment and related expenses	59,478	64,775
Change in enacted tax rate	-	648,748
Other items - net	(125,109)	30,020
Provision for income taxes	$ 2,433,690	$ 3,437,894

Note 8 - Employee Benefit Plans

The Corporation sponsors a 401(k) profit-sharing plan for substantially all employees. The plan provides for the Corporation to make a required matching contribution up to 25% of employee contributions up to 8% of their salary. The Corporation may also make additional profit-sharing contributions at the discretion of the board of directors. Contributions to the plan totaled $833,000 and $563,000 for the years ended December 31, 2018 and 2017, respectively.

The Corporation also maintains a stock appreciation rights plan. Under this plan, senior management and key officers are granted share unit awards, the value of which is calculated using the intrinsic value method and is equal to the incremental increase in the net book value, as defined, per share of the common stock of the Bank between the date of award and the date of full vesting. The share unit awards vest over a four-year period from the date of the grant. Plan liabilities of approximately $674,000 and $487,000 were recorded at December 31, 2018 and 2017, respectively. Share units matured totaled approximately $242,000 and $124,000 during 2018 and 2017, respectively. The Corporation incurred plan expenses of $311,000 and $245,000 during the years ended December 31, 2018 and 2017, respectively.

Note 9 - Stock Option Plan

The Corporation's stock incentive plan (the "Plan") permits the grant of both incentive stock options and nonqualified stock options to its directors, officers, and employees for up to 107,470 shares of common stock. Option awards are granted with an exercise price equal to the market price of the entity's stock at the date of grant; those option awards generally vest based on five years of continuous service and must be exercised within 10 years of the grant date. There are 8,326 shares available for grant at December 31, 2018.

The Corporation estimates the value of its stock options using the calculated value on the grant date. The Corporation measures compensation cost of employee stock options based on the calculated value instead of fair value because it is not practical to estimate the volatility of its share price. The Corporation does not maintain an internal market for its shares and its shares are rarely traded privately. The calculated value method requires that the volatility assumption used in an option-pricing model be based on the historical volatility of an appropriate industry sector index.

Note 9 – Stock Option Plan (Continued)

The Corporation uses a Black-Scholes formula to estimate the calculated value of its share-based payments. The weighted average assumptions used in the Black-Scholes model are noted in the following table. The Corporation uses historical data to estimate option exercise and employee termination within the valuation model. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

A summary of option activity under the Plan for the year ended December 31, 2018 is presented below:

Options	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (In Years)
Outstanding at January 1, 2018	2,000	$ 35.00	2.40
Exercised	(2,000)	(35.00)	-
Forfeited	-	-	-
Outstanding at December 31, 2018	-	-	-
Vested or expected to vest at December 31, 2018	-	-	-
Exerciseable at December 31, 2018	-	-	-

There were no options granted during 2018 or 2017. No options were exercised or forfeited during 2017.

The compensation cost that has been charged against income for the Plan was insignificant for 2018 and 2017.

Note 10 - Off-Balance-Sheet Activities and Borrowings

Credit-Related Financial Instruments - The Corporation is a party to credit-related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit, and commercial letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheet.

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

Note 10 - Off Balance-Sheet Activities and Borrowings (Continued)

At December 31, 2018 and 2017, the following financial instruments, whose contract amounts represent credit risk, were outstanding:

	Contract Amount	
	2018	2017
Unfunded commitments under lines of credit	$ 155,749,668	$ 162,290,160
Commercial and standby letters of credit	2,387,797	2,105,277
Commitments to originate mortgage loans subject to interest rate lock contracts	1,789,150	4,271,700

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

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

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

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

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

Repurchase Agreements – Securities sold under agreements to repurchase totaled approximately $4,417,000 and $6,948,000 at December 31, 2018 and 2017, respectively. At December 31, 2018, all of these financings had overnight maturities and were secured by approximately $8,740,000 of agency and mortgage backed securities which were owned and under the control of the Corporation. Risk could arise when the collateral pledged for the repurchase agreement declines in fair value. The Corporation minimizes the risk by monitoring the value of the collateral pledged. At the point in time where the collateral has declined in fair value, the Corporation is required to provide additional collateral based on the value of the underlying securities.

Legal Contingencies – Various legal claims also arise from time to time in the normal course of business which, in the opinion of management, will have no material effect on the Corporation's consolidated financial statements.

Note 10 - Off Balance-Sheet Activities and Borrowings (Continued)

Restrictions on Cash and Cash Equivalents – The Bank is required to maintain average balances on hand or with the Federal Reserve Bank. At December 31, 2018 and 2017, the restricted reserve balance amounted to $2,822,000 and $2,771,000, respectively.

Other Contingencies – The Corporation sells mortgage loans on a nonrecourse basis. In connection with the Corporation's loan sales, the Corporation makes representations and warranties customary in the industry relating to, among other things, compliance with laws, regulations, and program standards and accuracy of information. If there is a breach of the representations and warranties by the Corporation, typically the Corporation corrects these flaws. If the flaws cannot be corrected, the Corporation may be required to repurchase these loans. As of December 31, 2018 and 2017, the Corporation recorded a liability of $50,000 for these potential contingencies.

Borrowing Facilities – The Corporation is a member of the Federal Home Loan Bank of Chicago (FHLBC). Through the membership, the Corporation maintains a collateral pledge agreement covering secured advances whereby the Corporation has agreed to keep on hand, free of all other pledges, liens, and encumbrances, specifically identified whole first mortgages on improved residential property not more than 90-days delinquent to secure advances from the FHLBC. All of the Bank's FHLBC common stock is also pledged as additional collateral for any outstanding advances. There were no advances outstanding at both December 31, 2018 and 2017. At December 31, 2018, the Corporation had the ability to borrow approximately $60,459,000 under its credit facilities with the FHLBC.

The Corporation has a line of credit with another financial institution for an amount up to $3,750,000. The line of credit is unsecured, matures in June 2020, and has a floating interest rate per annum reset monthly equal to the one month LIBOR plus 2.25% (4.60% at December 31, 2018). Interest is payable quarterly and all payments have been paid as agreed. There was $2,500,000 outstanding on the line of credit as of December 31, 2018. There was no balance outstanding on the line of credit as of December 31, 2017.

Note 11 – Restrictions on Dividends

Banking regulations place certain restrictions on dividends paid by the Bank to the Corporation. The total amount of dividends which may be paid at any date is generally limited to the retained earnings of the Bank. In addition, dividends paid by the Bank to the Corporation would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum capital requirements. At December 31, 2018, and as a result of recent dividend payments, the Bank is not allowed to pay dividends to the Corporation without prior regulatory approval.

Note 12 – Minimum Regulatory Capital Requirements

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

Note 12 – Minimum Regulatory Capital Requirements (Continued)

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of total, common and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2018 and 2017, that the Bank met all capital adequacy requirements to which it is subject.

As of December 31, 2018, the most recent notification from the Bank's primary regulator categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, common equity Tier 1 risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the following tables. There are no conditions or events since the notification that management believes have changed the Bank's category.

The Bank's actual capital amounts and ratios as of December 31, 2018 and 2017 are presented in the table.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
(Dollar Amounts In Thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2018						
Total capital to risk-weighted assets	$ 60,598	12.1%	$ 40,006	8.0%	$ 49,934	10.0%
Tier I capital to risk-weighted assets	$ 54,348	10.9%	$ 29,960	6.0%	$ 39,947	8.0%
Common equity tier I capital to risk-weighted assets	$ 54,348	10.9%	$ 22,470	4.5%	$ 32,457	6.5%
Tier I capital to average assets	$ 54,348	9.6%	$ 22,714	4.0%	$ 28,392	5.0%
As of December 31, 2017						
Total capital to risk-weighted assets	$ 60,949	13.6%	$ 35,842	8.0%	$ 44,802	10.0%
Tier I capital to risk-weighted assets	$ 55,338	12.4%	$ 26,881	6.0%	$ 35,842	8.0%
Common equity tier I capital to risk-weighted assets	$ 55,338	12.4%	$ 20,161	4.5%	$ 29,122	6.5%
Tier I capital to average assets	$ 55,338	10.1%	$ 21,938	4.0%	$ 27,422	5.0%

Note 13 – Fair Value of Financial Instruments

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

Note 13 – Fair Value of Financial Instruments (Continued)

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

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

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

Loans Held for Sale – Fair value of loans held for sale is based on commitments on hand from investors or prevailing market prices.

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

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

Securities Sold Under Agreements to Repurchase – The carrying amounts of borrowings under repurchase agreements maturing within 90 days approximate their fair values.

Junior Subordinated Debentures – The fair values of the Corporation's floating rate trust-preferred securities are generally presumed to approximate the recorded carrying amount. However, due to the current economic environment, the fair value was calculated using discounted cash flows at a market rate for comparable security types.

Borrowings Under Line of Credit – The carrying amount of variable rate borrowings under lines of credit approximate their fair values.

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

Interest Rate Swap – Fair values of interest rate swap contracts are based on amounts payable to or receivable from counterparties based on the contractual terms of the agreements.

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

Note 13 – Fair Value of Financial Instruments (Continued)

The estimated fair values and related carrying or notional amounts of the Corporation's financial instruments at December 31 are as follows (in thousands):

	December 31, 2018		December 31, 2017	
	Carrying Amounts	Estimated Fair Value	Carrying Amounts	Estimated Fair Value
Financial assets:				
Cash and cash equivalents	$ 45,541	$ 45,541	$ 24,103	$ 24,103
Investment securities - Available-for-sale	99,447	99,447	132,401	132,401
Other securities	1,148	1,148	1,108	1,108
Loans held for sale	1,006	1,025	1,225	1,225
Loans - Net	413,806	408,093	369,095	366,468
Accrued interest receivable	1,681	1,681	1,677	1,677
Financial liabilities:				
Deposits	$ (507,803)	$ (506,840)	$ (471,767)	$ (471,492)
Securities sold under agreements to repurchase	(4,417)	(4,408)	(6,948)	(6,937)
Junior subordinated debentures	(10,310)	(8,598)	(10,310)	(8,002)
Borrowings under line of credit	(2,500)	(2,500)	-	-
Accrued interest payable	(139)	(139)	(44)	(44)
Interest rate swap	(246)	(246)	-	-

Note 14 – Fair Value Measurements

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

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

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

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

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

Note 14 – Fair Value Measurements (Continued)

The following tables present information about the Corporation's assets and liabilities measured at fair value on a recurring basis at December 31, 2018 and 2017 and the valuation techniques used by the Corporation to determine those fair values.

	December 31, 2018			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2018
Assets				
Investment securities:				
U.S. government agencies	$ -	$ 22,047,917	$ -	$ 22,047,917
Mortgage-backed securities and collateralized mortgage obligations	-	2,394,993	-	2,394,993
State and municipal securities	-	61,032,212	-	61,032,212
Corporate debt securities	-	12,991,871	-	12,991,871
Community reinvestment fund	979,652	-	-	979,652
Total investment securities	$ 979,652	$ 98,466,993	$ -	$ 99,446,645
Liabilities				
Interest rate swap	$ -	$ 246,232	$ -	$ 246,232

	December 31, 2017			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2017
Assets				
Investment securities:				
U.S. government agencies	$ -	$ 49,979,071	$ -	$ 49,979,071
Mortgage-backed securities and collateralized mortgage obligations	-	2,784,198	-	2,784,198
State and municipal securities	-	61,417,991	-	61,417,991
Corporate debt securities	-	17,216,938	-	17,216,938
Community reinvestment fund	1,002,457	-	-	1,002,457
Total investment securities	$ 1,002,457	$ 131,398,198	$ -	$ 132,400,655

Note 14 – Fair Value Measurements (Continued)

The Corporation also has assets that under certain conditions are subject to measurement at fair value on a nonrecurring basis. These assets include other real estate owned and impaired loans. The Corporation has estimated the fair values of these assets based primarily on Level 3 inputs. Other real estate and impaired loans are generally valued using the fair value of collateral provided by third-party appraisals. These valuations include assumptions related to cash flow projections, discount rates, and recent comparable sales. The numerical range of unobservable inputs for these valuation assumptions is not meaningful.

The following tables present information about the Corporation's assets measured at fair value on a non-recurring basis at December 31, 2018 and 2017 and the valuation techniques used by the Corporation to determine those fair values.

	December 31, 2018			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2018
Other real estate owned	$ -	$ -	$ 513,625	$ 513,625
Impaired loans	-	-	3,847,994	3,847,994

	December 31, 2017			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2017
Other real estate owned	$ -	$ -	$ 240,000	$ 240,000
Impaired loans	-	-	4,558,129	4,558,129