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PEOPLES TRUST *Company*
The bank with a *heart*

Annual Report 2019

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Annual Report 2019

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25 Kingman Street
St. Albans, VT

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Enosburg Falls, VT

ESSEX TOWN CENTER
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St. Albans, VT

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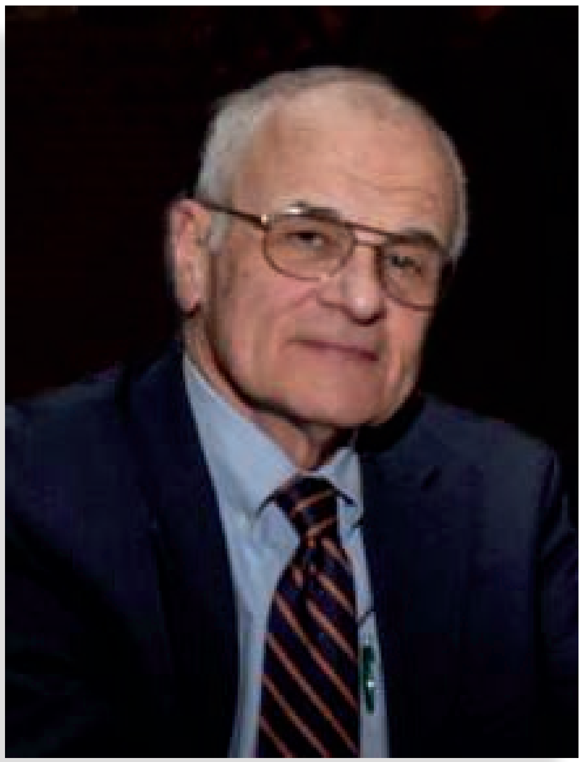

In fond remembrance of:

Marc J. Reynolds
Director
1944–2019

*Few were
so dedicated,
so loyal and
so protective
of the Peoples
Trust Company.
He will be
dearly missed.*

March 1, 2020

Dear Peoples Trust Company Shareholder,

Once again, I'm pleased to convey to you the results of the past year with this 2019 Peoples Trust Company Audited Financial Report. I begin this annual letter to the shareholders with a sense of pride and accomplishment. Not just for the strong financial performance of your bank this past year, but also for the work of our dedicated staff and the impact the bank has on our local community. While we experienced success and increased profitability in 2019, we also continued our investment in the future with ongoing technology implementations to improve the customer experience along with improving the bank's efficiency in delivering services. As a community bank, we are able to have the best of both worlds: we can be agile and embrace technology, but still have the small-town feel and personal interaction that our customers appreciate. Planning for the future and the long term success of your bank is of the utmost importance to us.

Here are a few of the financial highlights of the year ended December 31, 2019 compared to year ended December 31, 2018:

- *Net income increased by $306,190, or 16.5% to $2,161,551.*
- *Total assets increased by $823,767, or 0.3%, to $267,767,754.*
- *Net Loans in the owned loan portfolio decreased by $3,773,860, or 2.0% to $182,774,134.*
- *Net Loans in the serviced portfolio increased by $6,643,167, or 5.9% to $119,086,384.*
- *Book value per share increase by 7.6% to $59.17 per share as of December 31, 2019.*

Please find more detail in the accompanying pages of this report.

In terms of continuing to enhance shareholder value, the Board of Directors and I are pleased to announce that at the February 2020 Board meeting, Board members voted to increase the annual dividend payout to its shareholders from $0.85 per share to $0.95 per share. This is the fourth year in a row the bank has increased its dividend paid to shareholders. Additionally, by the time you receive this financial report, you will be well aware of the recent announcement of another formal share repurchase offering from Peoples Trust Company. The recent buyback offerings have been very successful with the bank retiring over 60,000 shares over the past five years. Your Board of Directors continue to impress me with their commitment to deliver tangible benefits to the shareholder base.

While it was a remarkable year in terms of how much we accomplished, the year was also unfortunately tragic with the sudden passing of long time former employee and Director Marc J. Reynolds on September 3, 2019. Marc started his career with the Peoples Trust Company in February of 1967 and he retired in 2009 as one of the longest serving employees in the company's history at 42 years, and one of the most successful achieving the status of Senior Executive Vice President, Treasurer and Board member. Not many people in the history of the bank have experienced and played such a vital role in the bank's growth: When Marc started at Peoples Trust Company, the Kingman Street location was the bank's only branch. He would participate in, and also lead the bank's branch expansion over the next few decades to the 6-branch locations Peoples Trust Company currently offers. He is responsible for designing some of the most beautiful bank buildings in Vermont and his attention to detail was simply second to none.

Few were so dedicated, so loyal and so protective of the Peoples Trust Company. He will be dearly missed.

I want to invite you all to attend the 133rd annual shareholder meeting on Tuesday, April 21st at 10:00am in the Board of Directors room at 25 Kingman Street, St. Albans, VT. In addition to reviewing the past years financial performance, we will be paying appropriate tribute to Marc Reynolds and Claire Manahan, who as noted in the 2019 Semi Annual report, passed away in early 2019. I hope that you will join us.

On behalf of the Board of Directors, all of our loyal staff and myself, I want to again thank you for your confidence and investment in the Peoples Trust Company.
Sincerely,

Thomas J. Gallagher

Thomas J. Gallagher
President/CEO
Peoples Trust Company

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PEOPLES TRUST COMPANY OF ST. ALBANS

FINANCIAL REPORT

DECEMBER 31, 2019

100
YEARS

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Peoples Trust Company of St. Albans
St. Albans, Vermont

We have audited the accompanying financial statements of Peoples Trust Company of St. Albans which comprise the balance sheets as of December 31, 2019 and 2018, and the related statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

A.M. PEISCH & COMPANY, LLP

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Suite 302
Colchester, VT 05446
(802) 654-7255

P.O. Box 460
Rutland, VT 05702
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(802) 527-0505

1020 Memorial Drive
St. Johnsbury, VT 05819
(802) 748-5654

24 Airport Road
Suite 402
West Lebanon, NH 03784
(603) 306-0100

INDEPENDENT AUDITOR'S REPORT

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Peoples Trust Company of St. Albans as of December 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

A. M. Peisch & Company LLP

Rutland, Vermont
February 10, 2020
VT Reg. No. 92-0000102

PEOPLES TRUST Company

The bank with a heart

BALANCE SHEETS
December 31, 2019 & 2018

ASSETS	2019	2018
Cash and cash equivalents	$ 4,887,225	$ 4,986,882
Interest bearing deposits with banks	9,301,610	9,011,651
Certificates of deposit	3,740,000	3,740,000
Securities available-for-sale	52,496,034	48,143,350
Securities held-to-maturity	-	827,567
Federal Home Loan Bank stock, at cost	220,700	392,300
Loans held for sale	517,291	162,678
Loans receivable, net	182,774,134	186,547,994
Premises and equipment, net	6,671,675	6,889,160
Accrued interest receivable	1,033,514	1,021,883
Bank owned life insurance	4,001,452	3,911,360
Other assets	2,124,119	1,309,162
Total assets	$ 267,767,754	$ 266,943,987

LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES		
Deposits:		
Demand deposits	$ 80,297,429	$ 73,830,501
Savings, NOW, and money market deposits	100,394,256	105,806,562
Time deposits $250,000 and over	7,897,942	7,016,541
Other time deposits	40,465,932	41,975,133
Total deposits	229,055,559	228,628,737
Repurchase agreements	3,182,657	4,734,098
Accrued interest payable and other liabilities	997,499	697,948
Total liabilities	233,235,715	234,060,783
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY		
Common stock - $0.50 par value; 2,000,000 shares authorized; 583,638 and 597,908 shares issued and outstanding in 2019 and 2018, respectively	291,819	298,954
Additional paid-in capital	8,381,685	8,381,685
Retained earnings	25,438,373	24,559,726
Accumulated other comprehensive income (loss)	420,162	(357,161)
Total shareholders' equity	34,532,039	32,883,204
Total liabilities and shareholders' equity	$ 267,767,754	$ 266,943,987

See notes to financial statements.

STATEMENTS OF INCOME
Years Ended December 31, 2019 & 2018

	2019	2018
Interest income:		
Interest and fees on loans	$ 9,532,442	$ 9,038,764
Interest and dividends on investment securities:		
U.S. government and federal agencies	410,464	412,078
CD's with banks	97,771	83,770
Other investments	747,378	853,399
Interest on federal funds sold and other interest bearing deposits	284,899	176,679
Total interest income	11,072,954	10,564,690
Interest expense:		
Interest on deposits	761,761	661,388
Interest on repurchase agreements	8,982	9,533
Total interest expense	770,743	670,921
Net interest income	10,302,211	9,893,769
Less provision for loan losses	-	-
Net interest income after provision for loans losses	10,302,211	9,893,769
Other income:		
Service charges on deposit accounts	797,491	832,907
Other service charges and fees	340,514	331,504
Interchange fees	840,644	834,822
Gain on sale of loans	349,889	149,470
Loss on sale of securities, net	-	(84,408)
Other income	376,449	385,235
Total other income	2,704,987	2,449,530
Other expenses:		
Salaries and employee benefits	6,335,966	6,102,019
Occupancy and equipment expense	1,108,955	1,104,930
Software maintenance	549,160	500,183
Loss on sale of fixed assets	10,935	1,986
Interchange expense	414,443	372,839
State franchise tax	263,680	253,733
Other expense	2,086,714	1,990,391
Total other expenses	10,769,853	10,326,081
Income before income taxes	2,237,345	2,017,218
Income tax expense	75,794	161,857
Net income	$ 2,161,551	$ 1,855,361
Earnings per common share	$ 3.64	$ 3.10

See notes to financial statements.

STATEMENTS OF COMPREHENSIVE INCOME

Years Ended December 31, 2019 & 2018

	2019	2018
Net income	$ 2,161,551	$ 1,855,361
Other comprehensive income (loss):		
Unrealized gain (loss) on securities:		
Unrealized holding gains (losses) arising during period	983,953	(496,127)
Tax effect	(206,630)	104,187
	777,323	(391,940)
Less: reclassification adjustment for losses (gains) included in income	-	84,408
Tax effect	-	(17,726)
	-	66,682
Other comprehensive income (loss), net of tax:	777,323	(325,258)
Comprehensive income	$ 2,938,874	$ 1,530,103

See notes to financial statements.

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Years Ended December 31, 2019 & 2018

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance, January 1, 2018	$ 298,954	$ 8,381,685	$ 23,152,796	$ (31,903)	$ 31,801,532
Net income	-	-	1,855,361	-	1,855,361
Other comprehensive loss	-	-	-	(325,258)	(325,258)
Cash dividends paid	-	-	(448,431)	-	(448,431)
Balance, December 31, 2018	298,954	8,381,685	24,559,726	(357,161)	32,883,204
Net income	-	-	2,161,551	-	2,161,551
Other comprehensive income	-	-	-	777,323	777,323
Stock buyback	(7,135)	-	(777,715)	-	(784,850)
Cash dividends paid	-	-	(505,189)	-	(505,189)
Balance, December 31, 2019	$ 291,819	$ 8,381,685	$ 25,438,373	$ 420,162	$ 34,532,039

See notes to financial statements.

STATEMENTS OF CASH FLOWS

Years Ended December 31, 2019 & 2018

CASH FLOWS FROM OPERATING ACTIVITIES	2019	2018
Net income	$ 2,161,551	$ 1,855,361
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	460,614	447,036
Net change in deferred taxes	(35,842)	(28,260)
Net change in taxes receivable	61,636	(133,597)
Gain on sale of loans	(349,889)	(149,470)
Loss on sale of fixed assets	10,935	1,986
Loss on sale of securities, net	-	84,408
Amortization, net	469,854	726,088
Increase in loans held for sale	(354,613)	(70,998)
Decrease in deferred loan fees	14,912	974
(Increase) decrease in accrued interest receivable	(11,631)	107,855
Increase in bank owned life insurance	(90,092)	(90,150)
(Increase) decrease in other assets	(935,693)	273,352
Increase in accrued expenses and other liabilities	187,863	113,563
Net cash provided by operating activities	1,589,605	3,138,148

CASH FLOWS FROM INVESTING ACTIVITIES		
(Increase) decrease in interest bearing deposits with banks	(289,959)	156,741
Proceeds from sales, maturities, and paydowns of securities available-for-sale	11,054,844	19,222,836
Purchase of securities available-for-sale	(14,893,429)	(6,478,274)
Proceeds from sales, maturities, and paydowns of certificates of deposit	-	242,147
Purchase of certificates of deposit	-	(1,500,000)
Proceeds from maturities of securities held-to-maturity	827,567	45,407
Net change in Federal Home Loan Bank stock	171,600	-
Loan originations, net of repayments	4,024,803	(18,149,064)
Recoveries of loans charged off	84,034	53,955
Purchase of premises and equipment	(254,064)	(518,218)
Net cash provided (used) by investing activities	725,396	(6,924,470)

See notes to financial statements.

STATEMENTS OF CASH FLOWS *continued*
Years Ended December 31, 2019 & 2018

CASH FLOWS FROM FINANCING ACTIVITIES	2019	2018
Net increase in demand, savings, NOW and money market	$ 1,054,622	$ 3,415,535
Net decrease in time deposits	(627,800)	(63,161)
Net (decrease) increase in repurchase agreements	(1,551,441)	298,419
Repurchase of stock	(784,850)	-
Dividends paid	(505,189)	(448,431)
Net cash (used) provided by financing activities	(2,414,658)	3,202,362
Net decrease in cash and cash equivalents	(99,657)	(583,960)
Cash and cash equivalents		
Beginning	4,986,882	5,570,842
Ending	$ 4,887,225	$ 4,986,882
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash payments for:		
Interest	$ 763,824	$ 669,023
Income taxes	$ 50,000	$ -
SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES		
Total change in unrealized loss on securities available-for-sale	$ 983,953	$ (411,719)

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

Note 1. Significant Accounting Policies

The accounting policies of Peoples Trust Company of St. Albans (the Bank) are in conformity with U. S. generally accepted accounting principles and general practices within the banking industry. The following is a description of the more significant policies.

Nature of operations

The Bank provides a variety of financial services to individuals, municipalities, commercial, and non-profit customers through its branches in northwestern Vermont, which is primarily a small business and agricultural area. The Bank's primary deposit products are checking and savings accounts and certificates of deposit. Its primary lending products are commercial, real estate, agricultural, and consumer loans.

Concentration of risk

The Bank's operations are affected by various risk factors, including interest-rate risk, credit risk, and risk from geographic concentration of lending activities. Management attempts to manage interest rate risk through various asset/liability management techniques designed to match maturities of assets and liabilities. Loan policies and administration are designed to provide assurance that loans will only be granted to credit-worthy borrowers, although credit losses are expected to occur because of subjective factors and factors beyond the control of the Bank. In addition, the Bank is a community bank and, as such, is mandated by the Community Reinvestment Act and other regulations to conduct most of its lending activities within the geographic area where it is located. Although the Bank has a diversified loan portfolio and economic conditions are stable, a substantial portion of its loan portfolio is secured by real estate and most of its lending activities are conducted in northern Vermont. As a result, the Bank and its borrowers may be especially vulnerable to the consequences of changes in the local economy and real estate market conditions. Note 3 discusses the types of investments the Bank invests in, and Note 5 discusses the type of lending the Bank engages in.

Use of estimates

In preparing financial statements in conformity with U. S. generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, accumulated depreciation based on estimated useful lives of assets, the valuation of foreclosed real estate, and deferred tax assets.

Presentation of cash flows

For purposes of presentation in the statements of cash flows, cash and cash equivalents include cash on hand and amounts due from banks (including cash items in process of clearing).

NOTES TO FINANCIAL STATEMENTS *continued*

Note 1. Significant Accounting Policies (Continued)

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 are classified as available-for-sale and recorded at fair value with unrealized gains and losses excluded from earnings and reported in other comprehensive income net of tax. Purchase premiums and discounts are recognized in interest income using methods approximating the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Declines in the fair value of individual held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary, result in write-downs of the individual securities to their fair value. The related write-downs are included 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 Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Federal Home Loan Bank stock

As a member of the Federal Home Loan Bank, the Bank is required to invest in $100 par value stock of the Federal Home Loan Bank. The stock is nonmarketable and is carried at cost. When redeemed, the Bank will receive from the Federal Home Loan Bank an amount equal to the par value of the stock.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding principal adjusted for any charge-offs, the allowance for loan losses and unearned fees. Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Sales are made primarily without recourse. Net unrealized losses are recognized through a valuation allowance by charges to income.

Loan interest income is accrued daily on the outstanding balances. Accrual of interest is discontinued when a loan is specifically determined to be impaired or when the loan is delinquent 90 days and management believes that, after considering collection efforts and other factors, the borrower's financial condition is such that collection of interest is doubtful. Any unpaid interest previously accrued on those loans is reversed from income. Interest income generally is not recognized on specific impaired loans unless the likelihood of further loss is remote. Interest payments received on such loans are generally applied as a reduction of the loan principal balance. Interest income on other nonaccrual loans is recognized only to the extent of interest payments received. 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 charged

Note 1. Significant Accounting Policies (Continued)

off when collection of principal is considered doubtful. Past due status is determined on a contractual basis.

Loan origination and commitment fees and certain direct loan origination costs are deferred and amortized as an adjustment of the related loan's yield using methods that approximate the interest method. The Bank is generally amortizing these amounts over the contractual life.

Allowance for loan losses

The allowance for loan losses is maintained at a level that, in management's judgment, is adequate to absorb credit losses inherent in the loan portfolio. The amount of the allowance is based on management's evaluation of the collectability of the loan portfolio, including the nature of the portfolio, credit concentrations, and trends in historical loss experience, specific impaired loans, and economic conditions. Allowances for impaired loans are generally determined based on collateral values or the present value of estimated cash flows. Although management uses available information to recognize losses on loans, because of uncertainties associated with local economic conditions, collateral values, and future cash flows on impaired loans, it is reasonably possible that a material change could occur in the allowance for loan losses in the near term. However, the amount of the change that is reasonably possible cannot be estimated. The allowance is increased by a provision for loan losses, which is charged to expense, and reduced by charge-offs, net of recoveries. Subsequent recoveries, if any, are credited to the allowance.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Impaired loans may also include loans which have been restructured. A troubled debt restructuring occurs when the Bank grants a concession to a borrower, for legal or economic reasons, that is experiencing financial difficulties. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Impairment is measured on a loan-by-loan basis, primarily for commercial 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 smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not generally identify individual consumer and residential loans for impairment disclosures, unless those loans are subject to restructuring agreements or are part of a larger impaired customer relationship.

Bank premises and equipment

Bank premises and equipment are stated at cost, less accumulated depreciation. Depreciation is computed on the straight-line and accelerated methods over the estimated useful lives of the related assets. The cost of assets sold or otherwise disposed of and the related allowance for depreciation is eliminated from the accounts and the resulting gains or losses are reflected in the income statement. Maintenance and repairs are charged to current expense as incurred and the cost of major renewals and betterments are capitalized.

NOTES TO FINANCIAL STATEMENTS *continued*

Note 1. Significant Accounting Policies (Continued)

Other real estate owned

Real estate properties acquired through or in lieu of loan foreclosure are initially recorded at the lower of the Bank's carrying amount or fair value less estimated selling cost at the date of foreclosure. Any write-downs based on the asset's fair value at the date of acquisition are charged to the allowance for loan losses. After foreclosure, these assets are carried at the lower of their new cost basis or fair value less cost 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 a property to the lower of its costs or fair value less cost to sell.

Mortgage servicing

The Bank recognizes, as separate assets, rights to service mortgage loans for others however those servicing rights are acquired. When the Bank acquires mortgage servicing rights through either the purchase or origination of mortgage loans (originated mortgage servicing rights) and sells or securitizes those loans with servicing rights retained, it allocates the total cost of the mortgage loans to the mortgage servicing rights and the loans (without the mortgage servicing rights) based on their relative fair values. To determine the fair value of the servicing rights created, the Bank uses the market prices under comparable servicing sale contracts. The cost of mortgage servicing rights is amortized in proportion to, and over the period of, estimated net servicing revenues. Impairment of mortgage servicing rights is assessed based on the fair value of those rights. Fair values are estimated using discounted cash flows based on a current market interest rate.

Pension plan

Pension costs relating to the Bank's defined contribution plan are charged to employee benefits expense and are funded as accrued.

Advertising costs

The Bank expenses advertising costs as incurred.

Income taxes

The Bank recognizes income taxes under the asset and liability method. Under this method, deferred tax assets and liabilities are established for the temporary differences between the accounting basis and the tax basis of the Bank's assets and liabilities at enacted tax rates expected to be in effect when the amounts related to such temporary differences are realized or settled. Adjustments to the Bank's deferred tax assets are recognized as deferred income tax expense or benefit based on management's judgments relating to the realizability of such assets. Historic rehabilitation, low income housing, and new markets tax credits are recognized as a reduction of income tax expense in the years they are earned.

Note 1. Significant Accounting Policies (Continued)

Generally accepted accounting standards prescribe a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return, and provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. Management reviews the inventory of tax positions taken at each reporting period to assess the more-likely-than-not recognition threshold. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold are derecognized in the first subsequent financial reporting period in which that threshold is no longer met.

Fair value measurements

Fair values of financial instruments are estimated using relevant market information and other assumptions. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates.

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

- Level 1 – Valuation is based on quoted prices in active markets for identical assets or liabilities that the Bank has the ability to access at the measurement date. Level one assets and liabilities generally include debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities;
- Level 2 – Valuation is based on inputs other than quoted prices included within level one that are observable for the asset or liability, 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 of the assets or liabilities. Level three 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.

Off-balance-sheet financial instruments

In the ordinary course of business the Bank is party to off-balance-sheet financial instruments consisting of commitments to extend credit, unused lines of credit, commercial letters of credit and standby letters of credit. Such financial instruments are recorded in the financial statements when they become payable.

Note 1. Significant Accounting Policies (Continued)

Earnings per common share

Earnings per common share are computed based on the weighted average number of shares of common stock outstanding during the period, retroactively adjusted for stock splits. The weighted average shares outstanding were 593,792 and 597,908 for the years ended December 31, 2019 and 2018, respectively.

Transfer and servicing 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 Bank, (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 Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Comprehensive income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income or in a separate statement. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities are reported net of the tax effect in the statement of comprehensive income.

Accounting Pronouncements

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses*. The standard requires financial assets to be measured at amortized cost basis to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that will be deducted from the amortized cost basis of the financial assets to present the net carrying value at the amount expected to be collected on the financial statements. The income statement will reflect the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. The measurement of expected credit losses is to be based on relevant information about past events, including historical experience, current conditions and reasonable and supportable forecasts that affect the collectability of the reported amount. An entity must use judgment in determining the relevant information and estimation methods that are appropriate in its circumstances. In addition, credit losses relating to available-for-sale debt securities should be recorded through an allowance for credit losses. The amount of this allowance for credit losses will be limited to the amount by which the fair value is below amortized cost. The standard is effective for reporting periods beginning after December 15, 2022, including interim periods within those fiscal years. The impact of this standard on the financial statements is yet to be determined.

NOTES TO FINANCIAL STATEMENTS *continued*

Note 2. Restrictions on Cash and Due From Banks

The Bank is required to maintain reserve and clearing balances in cash with Atlantic Community Bankers Bank. The totals of the reserve balances were approximately $783,000 and $776,000 at December 31, 2019 and 2018, respectively.

The nature of the Bank's business requires that it maintain amounts due from banks, which, at times, may exceed federally insured limits. No losses have been experienced on these accounts.

Note 3. Investment Securities

Securities available-for-sale (AFS) and held-to-maturity (HTM) consists of the following:

AFS	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2019				
U.S. Government and Federal Agencies	$ 33,738,670	$ 477,737	$ 95,326	$ 34,121,081
State and municipal securities	18,225,513	173,003	23,563	18,374,953
	$ 51,964,183	$ 650,740	$ 118,889	$ 52,496,034
December 31, 2018				
U.S. Government and Federal Agencies	$ 34,188,775	$ 61,128	$ 555,298	$ 33,694,605
State and municipal securities	14,406,677	74,688	32,620	14,448,745
	$ 48,595,452	$ 135,816	$ 587,918	$ 48,143,350
HTM				
December 31, 2019				
State and municipal securities	$ -	-	-	$ -
	$ -	-	-	$ -
December 31, 2018				
State and municipal securities	$ 827,567	-	-	$ 827,567
	$ 827,567	-	-	$ 827,567

NOTES TO FINANCIAL STATEMENTS *continued*

Note 3. Investment Securities (continued)

Included in the caption "Securities AFS: U. S. Government and Federal Agencies" are mortgage-backed securities as follows:

	Amortized Cost	Fair Value
December 31, 2019	$ 17,945,874	$ 18,043,723
December 31, 2018	$ 16,078,896	$ 15,782,018

Proceeds from the sale of securities available-for-sale were $-0- and $11,886,206 in 2019 and 2018, respectively.

Gross realized gains and gross realized losses on sales of investments available-for-sale were $-0- in 2019 and $15,834 and $100,242 in 2018.

The scheduled maturities of securities-available for sale and securities held-to-maturity at December 31, 2019 were as follows:

	Available-for-Sale Securities		Held-to-Maturity Securities	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due within one year	$ 2,262,577	$ 2,271,079	$ -	$ -
Due from one to five years	13,893,391	14,147,947	-	-
Due from five to ten years	5,260,072	5,320,317	-	-
Due in greater than ten years	12,602,269	12,712,968	-	-
Mortgage-backed securities	17,945,874	18,043,723	-	-
	$ 51,964,183	$ 52,496,034	$ -	$ -

Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

Assets, principally securities, with amortized cost of $9,761,827 and $12,654,790 and with fair values of $9,985,372 and $12,557,168 at December 31, 2019 and 2018, respectively, were pledged to secure public deposits and for other purposes required or permitted by law.

Note 3. Investment Securities (continued)

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

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
December 31, 2019						
U.S. Government and Federal Agencies	$ 3,200,481	$ (53,168)	$ 4,060,989	$ (42,158)	$ 7,261,470	$ (95,326)
State and municipal governments	3,832,691	(23,563)	-	-	3,832,691	(23,563)
Total	$ 7,033,172	$ (76,731)	$ 4,060,989	$ (42,158)	$ 11,094,161	$ (118,889)
December 31, 2018						
U.S. Government and Federal Agencies	$ 9,360,906	$ (72,834)	$ 17,734,596	$ (482,464)	$ 27,095,502	$ (555,298)
State and municipal governments	4,186,324	(4,131)	4,421,975	(28,489)	8,608,299	(32,620)
Total	$ 13,547,230	$ (76,965)	$ 22,156,571	$ (510,953)	$ 35,703,801	$ (587,918)

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (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 Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

At December 31, 2019, the ten debt securities and nine municipal bonds with unrealized losses have depreciated less than 2% from the Bank's amortized cost basis. These securities are guaranteed by the U. S. or State and municipal governments or other Federal Agencies. These unrealized losses relate principally to current interest rates for similar types of securities. In analyzing an issuer's financial condition, management considers whether the securities are issued by the Federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. As management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available-for-sale, no declines are deemed to be other-than-temporary.

NOTES TO FINANCIAL STATEMENTS *continued*

Note 4. Loan Servicing

Mortgage loans serviced for others are not included in the accompanying statements of financial condition. The unpaid principal balances of mortgage loans serviced for others were $119,086,384 and $112,443,217 at December 31, 2019 and 2018, respectively. The carrying amounts of mortgage service rights which approximate their fair value were $464,801 and $437,564 at December 31, 2019 and 2018, respectively. Mortgage service rights of $161,126 and $83,254 were capitalized in 2019 and 2018, respectively. Amortization of mortgage services rights was $133,889 and $142,815 in 2019 and 2018, respectively.

Note 5. Loans

The composition of net loans at December 31 is as follows:

	2019	2018
Residential real estate	$ 58,804,893	$ 63,150,464
Commercial real estate	81,999,233	84,079,070
Commercial	8,300,888	7,437,752
Agricultural real estate	20,580,320	19,379,455
Agricultural	1,414,711	1,673,432
Consumer	5,382,474	5,912,336
Municipal	8,553,376	7,192,023
Gross loans	185,035,895	188,824,532
Net deferred loan costs	(13,689)	1,223
Allowance for loan losses	(2,248,072)	(2,277,761)
Net loans	$ 182,774,134	$ 186,547,994

A summary of current, past due, and nonaccrual loans as of December 31, 2019 and 2018 were as follows:

December 31, 2019	Current	30-89 days	Over 90 days and accruing	Nonaccrual	Total
Residential real estate	$ 57,511,827	$ 598,671	$ -	$ 694,395	$ 58,804,893
Commercial real estate	79,110,204	423,082	-	2,465,947	81,999,233
Commercial	8,018,931	257,449	-	24,508	8,300,888
Agricultural real estate	20,453,884	-	-	126,436	20,580,320
Agricultural	1,414,711	-	-	-	1,414,711
Consumer	5,379,596	2,758	-	120	5,382,474
Municipal	8,553,376	-	-	-	8,553,376
Total	$ 180,442,529	$ 1,281,960	$ -	$ 3,311,406	$ 185,035,895

Note 5. Loans (continued)

December 31, 2018	Current	30-89 days	Over 90 days and accruing	Nonaccrual	Total
Residential real estate	$ 61,166,245	$ 1,198,847	$ -	$ 785,372	$ 63,150,464
Commercial real estate	82,001,347	930,649	-	1,147,074	84,079,070
Commercial	7,392,343	-	-	45,409	7,437,752
Agricultural real estate	19,253,019	-	-	126,436	19,379,455
Agricultural	1,620,847	52,585	-	-	1,673,432
Consumer	5,904,983	7,198	-	155	5,912,336
Municipal	7,192,023	-	-	-	7,192,023
Total	$ 184,530,807	$ 2,189,279	$ -	$ 2,104,446	$ 188,824,532

Note 6. Allowance for Loan Losses and Credit Quality

Changes in the Allowance for loan losses for the years ended December 31, 2019 and 2018 were as follows:

	Residential Real Estate	Commercial Real Estate	Commercial	Agricultural Real Estate	Agricultural, Consumer and Muncipal	Unallocated	Total
Balance December 31, 2018	$ 193,068	$ 1,409,033	$ 139,739	$ 237,275	$ 298,646	$ -	$ 2,277,761
Provision for loan losses	(16,707)	(64,937)	20,469	(1,664)	(46,591)	109,430	-
Recoveries of amounts charged off	15,000	3,830	433	5,270	59,502	-	84,035
	191,361	1,347,926	160,641	240,881	311,557	109,430	2,361,796
Amounts charged off	(5,085)	(57,285)	-	-	(51,354)	-	(113,724)
Balance December 31, 2019	$ 186,276	$ 1,290,641	$ 160,641	$ 240,881	$ 260,203	$ 109,430	$ 2,248,072
Balance December 31, 20173	$ 265,456	$ 1,486,453	$ 108,208	$ 227,959	$ 228,537	$ -	$ 2,316,613
Provision for loan losses	(29,399)	(77,748)	26,180	2,465	78,502	-	-
Recoveries of amounts charged off	1	328	5,351	6,851	41,424	-	53,955
	236,058	1,409,033	139,739	237,275	348,463	-	2,370,568
Amounts charged off	(42,990)	-	-	-	(49,817)	-	(92,807)
Balance December 31, 2018	$ 193,068	$ 1,409,033	$ 139,739	$ 237,275	$ 298,646	$ -	$ 2,277,761

Despite the above allocation, the Allowance for loan losses is general in nature and is available to absorb loss from any loan type.

Note 6. Allowance for Loan Losses and Credit Quality (Continued)

At December 31, 2019 and 2018, the allocation of the Allowance for loan losses summarized on the basis of the Bank's impairment methodology was as follows:

December 31, 2019	Residential Real Estate	Commercial Real Estate	Commercial	Agricultural Real Estate	Agricultural, Consumer and Municipal	Unallocated	Total
Individually evaluated for impairment	$ 13,736	$ 9,741	$ -	$ 52,288	$ 311	$ -	$ 76,076
Collectively evaluated for impairment	172,540	1,280,900	160,641	188,593	259,892	109,430	2,171,996
Allocated	$ 186,276	$ 1,290,641	$ 160,641	$ 240,881	$ 260,203	$ 109,430	$ 2,248,072
December 31, 2018							
Individually evaluated for impairment	$ 12,572	$ 46,243	$ -	$ 61,625	$ -	$ -	$ 120,440
Collectively evaluated for impairment	180,496	1,362,790	139,739	175,650	298,646	-	2,157,321
Allocated	$ 193,068	$ 1,409,033	$ 139,739	$ 237,275	$ 298,646	$ -	$ 2,277,761

The recorded investment in loans summarized on the basis of the Bank's impairment methodology as of December 31, 2019 and 2018 were as follows:

December 31, 2019	Residential Real Estate	Commercial Real Estate	Commercial	Agricultural Real Estate	Agricultural	Consumer and Municipal	Total
Individually evaluated for impairment	$ 928,089	$ 3,122,949	$ 24,508	$ 545,059	$ 128,290	$ -	$ 4,748,895
Collectively evaluated for impairment	57,876,804	78,876,284	8,276,380	20,035,261	1,286,421	13,935,850	180,287,000
Allocated	$ 58,804,893	$ 81,999,233	$ 8,300,888	$ 20,580,320	$ 1,414,711	$ 13,935,850	$ 185,035,895
December 31, 2018							
Individually evaluated for impairment	$ 1,112,689	$ 1,480,010	$ 45,409	$ 585,911	$ -	$ -	$ 3,224,019
Collectively evaluated for impairment	62,037,775	82,599,060	7,392,343	18,793,544	1,673,432	13,104,359	185,600,513
Allocated	$ 63,150,464	$ 84,079,070	$ 7,437,752	$ 19,379,455	$ 1,673,432	$ 13,104,359	$ 188,824,532

The following table summarizes the loan ratings applied to the Bank's loan types as of December 31, 2019 and 2018:

December 31, 2019	Residential Real Estate	Commercial Real Estate	Commercial	Agricultural Real Estate	Agricultural	Consumer and Municipal	Total
Satisfactory	$ 56,685,523	$ 75,377,402	$ 7,843,177	$ 13,594,857	$ 1,054,784	$ 13,931,914	$ 168,487,657
Watch	1,322,234	3,447,542	356,472	6,160,973	231,637	3,229	11,522,087
OAEM	-	-	-	-	-	-	-
Substandard	797,136	3,174,289	101,239	824,490	128,290	707	5,026,151
Doubtful	-	-	-	-	-	-	-
Total	$ 58,804,893	$ 81,999,233	$ 8,300,888	$ 20,580,320	$ 1,414,711	$ 13,935,850	$ 185,035,895

NOTES TO FINANCIAL STATEMENTS *continued*

Note 6. Allowance for Loan Losses and Credit Quality (Continued)

December 31, 2018	Residential Real Estate	Commercial Real Estate	Commercial	Agricultural Real Estate	Agricultural	Consumer and Municipal	Total
Satisfactory	$ 60,843,709	$ 74,169,114	$ 7,111,911	$ 12,409,568	$ 1,482,968	$ 13,099,429	$ 169,116,699
Watch	943,783	8,449,429	229,239	6,104,544	190,464	4,223	15,921,682
OAEM	-	-	-	-	-	-	-
Substandard	1,362,972	1,460,527	96,602	865,343	-	707	3,786,151
Doubtful	-	-	-	-	-	-	-
Total	$ 63,150,464	$ 84,079,070	$ 7,437,752	$ 19,379,455	$ 1,673,432	$ 13,104,359	$ 188,824,532

The following is an overview of the Bank’s loan rating system:

1-3 Rating – Satisfactory

Risk-rating grades “1” through “3” comprise those loans ranging from lower than average credit risk which indicates borrowers with high liquidity, excellent financial condition, strong management, favorable industry trends or loans secured by highly liquid assets through marginal credit risk, which while credit worthy, exhibit some characteristics which require special attention by the account officer.

4 Rating – Watch

These loans are characterized by adequate collateral but recent declining financial, reporting or management trends such as marginal cash flow, marginal profitability, etc.

5 Rating – Other Assets Especially Mentioned (OAEM)

Special mention assets have potential weaknesses that deserve management’s close attention and monitoring until resolved. OAEMs are not adversely classified and do not expose the Bank to sufficient risk to warrant adverse classification currently but might warrant adverse classification if correction of the weakness does not take place in the short term.

6 Rating – Substandard

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

7 Rating - Doubtful

An asset classified doubtful has all the weaknesses inherent in one classified substandard, with the added characteristic that weaknesses make collection or liquidation in full, on the basis of existing facts, conditions and values, highly questionable and improbable.

NOTES TO FINANCIAL STATEMENTS *continued*

Note 6. Allowance for Loan Losses and Credit Quality (Continued)

The following table provides information with respect to impaired loans as of and for the year ended December 31, 2019 and 2018, respectively:

	December 31, 2019			Year Ended December 31, 2019	
	Recorded Investment	Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Received
With an allowance recorded:					
Residential real estate	$ 235,867	$ 240,449	$ 13,736		
Commercial real estate	2,212,931	2,216,242	9,741		
Commercial	-	-	-		
Agricultural real estate	525,059	525,059	52,288		
Agricultural	128,290	128,290	311		
	3,102,147	3,110,040	76,076		
With no allowance recorded:					
Residential real estate	692,222	1,030,901	-		
Commercial real estate	910,018	1,763,019	-		
Commercial	24,508	101,239	-		
Agricultural real estate	20,000	20,000	-		
Agricultural	-	-	-		
	1,646,748	2,915,159	-		
Total:					
Residential real estate	928,089	1,271,350	13,736	$ 975,180	$ 19,576
Commercial real estate	3,122,949	3,979,261	9,741	2,394,051	36,075
Commercial	24,508	101,239	-	28,732	-
Agricultural real estate	545,059	545,059	52,288	565,998	39,376
Agricultural	128,290	128,290	311	96,886	-
Total	$ 4,748,895	$ 6,025,199	$ 76,076	$ 4,060,847	$ 95,027

Note 6. Allowance for Loan Losses and Credit Quality (Continued)

	December 31, 2018			Year Ended December 31, 2018	
	Recorded Investment	Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Received
With an allowance recorded:					
Residential real estate	$ 203,587	$ 217,417	$ 12,572		
Commercial real estate	573,832	590,901	46,243		
Commercial	-	-	-		
Agricultural real estate	585,911	585,911	61,625		
	1,363,330	1,394,229	120,440		
With no allowance recorded:					
Residential real estate	909,102	1,261,544	-		
Commercial real estate	906,178	1,634,605	-		
Commercial	45,409	96,602	-		
Agricultural real estate	-	-	-		
	1,860,689	2,992,751	-		
Total:					
Residential real estate	1,112,689	1,478,961	12,572	$ 1,384,357	$ 36,883
Commercial real estate	1,480,010	2,225,506	46,243	1,760,808	45,523
Commercial	45,409	96,602	-	53,636	-
Agricultural real estate	585,911	585,911	61,625	682,830	54,664
Total	$ 3,224,019	$ 4,386,980	$ 120,440	$ 3,881,631	$ 137,070

The following table provides information with respect to troubled debt restructurings (TDR) as of and for the year ended December 31, 2019 and 2018, respectively:

	Residential Real Estate	Commercial Real Estate	Commercial	Agricultural Real Estate	Total
Balance, December 31, 2018	$ 632,772	$ 631,115	$ 45,409	$ 585,911	$ 1,895,207
Additions	-	-	-	-	-
Charge-off's	-	-	-	-	-
Paydowns	(50,478)	(186,635)	(20,901)	(60,852)	(318,866)
Balance, December 31, 2019	$ 582,294	$ 444,480	$ 24,508	$ 525,059	$ 1,576,341

NOTES TO FINANCIAL STATEMENTS *continued*

Note 6. Allowance for Loan Losses and Credit Quality (Continued)

	Residential Real Estate	Commercial Real Estate	Commercial	Agricultural Real Estate	Total
Balance, December 31, 2017	$ 660,626	$ 803,940	$ 56,935	$ 641,639	$ 2,163,140
Additions	42,979	44,592	-	-	87,571
Charge-off's	-	-	-	-	-
Paydowns	(70,833)	(217,417)	(11,526)	(55,728)	(355,504)
Balance, December 31, 2018	$ 632,772	$ 631,115	$ 45,409	$ 585,911	$ 1,895,207

There were no new troubled debt restructurings during 2019.

During 2018, one residential real estate loan totaling $42,979 and one commercial loan totaling $44,592 were restructured. The Bank filed a "Lift the Stay Motion" after bankruptcy filings were discharged and the court ordered mediation. Both loans were modified based on the required mediation. On the residential loan interest and fees in the amount of the amount of $4,938 was capitalized. On the commercial loan interest and fees in the amount of $76,143 was capitalized. On both loans the interest rate was decreased and the term was extended. Both loans are considered adequately secured with no specific loss allocation.

At December 31, 2019 and 2018, the Bank was not committed to lend any additional funds to borrowers whose loans were nonperforming, impaired or restructured.

Note 7. Bank Premises and Equipment

The major classes of bank premises and equipment and the total accumulated depreciation at December 31 are as follows:

	2019	2018
Land and land improvements	$ 2,179,659	$ 2,179,659
Building and improvements	7,241,169	7,241,169
Furniture and equipment	4,058,447	4,045,722
	13,479,275	13,466,550
Less accumulated depreciation	6,807,600	6,577,390
	$ 6,671,675	$ 6,889,160

Depreciation included in occupancy and equipment expense amounted to $460,614 and $447,036 for the years ended December 31, 2019 and 2018, respectively.

Note 8. Other Real Estate Owned

At December 31, 2019 and 2018, the recorded investment of consumer mortgage loans secured by residential real estate properties for which formal foreclosure procedures are in process is $174,149 and $217,728, respectively.

Note 9. Deposits

The following is a maturity distribution of time deposits at December 31, 2019:

Maturing in 2020	$ 20,909,884
Maturing in 2021	11,993,334
Maturing in 2022	7,677,242
Maturing in 2023	5,864,419
Maturing in 2024 and thereafter	1,918,995
	$ 48,363,874

U.S. government and federal agency securities with a cost of $4,738,893 and $7,622,093 and a fair value of $4,865,817 and $7,616,238 were pledged to collateralize certain municipal deposits at December 31, 2019 and 2018, respectively.

Note 10. Repurchase Agreements

Securities sold under agreements to repurchase amounted to $3,182,657 and $4,734,098 as of December 31, 2019 and 2018, respectively. These agreements are collateralized by U.S. government and federal agency securities with a amortized cost of $5,022,934 and $5,032,697 and a fair value of $5,119,555 and $4,940,930 at December 31, 2019 and 2018, respectively. The securities underlying these agreements are held in safekeeping by the Bank.

The average daily balance of these repurchase agreements approximated $3,965,585 and 5,423,360 during 2019 and 2018, respectively. The maximum borrowings outstanding on these agreements at any month-end reporting period of the Bank were $5,128,800 and $8,547,263 in 2019 and 2018, respectively. The weighted average rate for repurchase agreements was 0.25% and 0.22% at December 31, 2019 and 2018, respectively.

Note 11. Borrowed Funds

The Bank maintains an unsecured $3,000,000 federal funds line of credit with Atlantic Community Bankers Bank which was unused at December 31, 2019 and 2018.

Note 12. Income Taxes

Income tax expense included in the Statements of Income for the years ended December 31 were as follows:

	2019	2018
Currently payable	$ 111,634	$ 133,597
Deferred	(35,840)	28,260
	$ 75,794	$ 161,857

Total income tax expense differed from the amounts computed by applying the U. S. Federal income tax rate of 21% for 2019 and 2018 to income before income taxes as a result of the following at December 31:

	2019	2018
Computed expected tax expense	$ 469,843	$ 423,616
Disallowed interest expense	2,969	3,294
Municipal income	(129,671)	(150,695)
Boli income	(18,919)	(18,931)
Tax credits	(287,677)	(119,366)
Other, net	39,249	23,939
	$ 75,794	$ 161,857

The deferred income tax provision consisted of the following items at December 31:

	2019	2018
Nonaccrual loan interest	$ (81,627)	$ 39,322
Depreciation	(1,143)	(1,311)
Bad debts	-	-
Deferred directors fees	(32,196)	(28,257)
Mortgage servicing rights	5,720	(12,508)
Limited partnerships	8,406	6,014
Other	65,000	25,000
	$ (35,840)	$ 28,260

NOTES TO FINANCIAL STATEMENTS *continued*

Note 12. Income Taxes (Continued)

The significant components of the net deferred tax asset consisted of the following items at December 31:

	2019	2018
Components of deferred tax assets:		
Bad debts	$ 243,277	$ 243,277
Off balance sheet accrual	6,154	6,154
Nonaccrual loan interest	230,398	148,771
Limited partnerships	11,495	19,901
Unrealized loss on securities available-for-sale	-	94,942
Deferred directors fees	75,017	42,821
Total deferred tax asset	566,341	555,866
Valuation allowance	-	-
Total deferred tax asset, net of valuation allowance	566,341	555,866
Components of deferred tax liability:		
Depreciation	(64,099)	(65,242)
Mortgage servicing rights	(97,608)	(91,888)
Unrealized gain on securities available-for-sale	(111,689)	-
Other	(110,000)	(45,000)
Total deferred tax liability	(383,396)	(202,130)
Net deferred tax asset	$ 182,945	$ 353,736

Net deferred tax asset is included in the caption "other assets" on the balance sheets at December 31, 2019 and 2018, respectively. The deferred tax asset valuation allowance did not change during 2019 and 2018.

Deferred tax assets are recognized subject to management's judgment that realization is more likely than not as GAAP allows for the recognition and measurement of deductible temporary differences to the extent that it is more likely than not that the deferred tax asset will be realized. Based on the temporary taxable items, historical taxable income and estimates of future taxable income, the Bank believes that it is more likely than not that the deferred tax assets at December 31, 2019 will be realized.

Based on management's evaluation, management has concluded that there were no significant uncertain tax positions requiring recognition in the Bank's financial statements at December 31, 2019. Although the Bank is not currently the subject of tax examination by the Internal Revenue Service (IRS), the Bank's tax years ended December 31, 2016 through 2019 are open to examination by the IRS under the applicable statute of limitations.

Note 12. Income Taxes (Continued)

The Bank may from time-to-time be assessed interest and/or penalties by federal or state tax jurisdictions, although any such assessments historically have been minimal and immaterial to the Bank's financial results. In the event that the Bank receives an assessment for interest and/or penalties, it will be classified in the financial statements as “Other expense”.

Note 13. Pension Plan

The Bank maintains a contributory 401(k) pension plan covering all employees who meet certain age and service requirements. Contributions to the plan are voluntary by the eligible participants up to certain limits. Employee contributions are matched dollar for dollar for every dollar contributed up to six percent of the participant's salary. Contributions to the plan by the Bank for the years ended December 31, 2019 and 2018 amounted to $241,159 and $226,184, respectively.

Note 14. Commitments and Contingencies

In the normal course of business, the Bank is involved in various legal proceedings. In the opinion of management, any liability resulting from such proceedings would not have a material adverse effect on the Bank's financial statements.

Note 15. Financial Instruments with Off-Balance-Sheet Risk

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 and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit, standby letters of credit, interest rate caps and floors written on adjustable rate loans, and commitments to sell loans. Such instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The contract or notional amounts of those instruments reflect the extent of involvement the Bank has in particular classes of financial 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, standby letters of credit, and commercial letters of credit is represented by the contractual notional amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. For interest rate caps and floors written on adjustable rate loans, the contract or notional amounts do not represent exposure to credit loss. The Bank controls the credit risk of their interest rate cap agreements through credit approvals, limits, and monitoring procedures. The Bank generally requires collateral or other security to support financial instruments with credit risk.

	Contract or Notional Amount	
	2019	**2018**
Financial instruments whose contract amount represent credit risk:		
Commitments to extend credit and available lines of credit	$ 37,213,000	$ 32,702,000
Stand by letters of credit and commercial letters of credit	$ 800,000	$ 1,875,000

NOTES TO FINANCIAL STATEMENTS *continued*

Note 15. Financial Instruments with Off-Balance-Sheet Risk (Continued)

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. At December 31, 2019, the Bank had binding loan commitments at fixed rates totaling $7,061,400 that are included in commitments to extend credit.

The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the customer. Collateral held varies but may include real estate, accounts receivable, inventory, property, plant, and equipment, and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers.

The Bank enters into a variety of interest rate contracts, including interest rate caps and floors written on adjustable rate loans in managing its interest rate exposure. Interest rate caps and floors on loans written by the Bank enable customers to transfer, modify or reduce their interest rate risk.

Note 16. Transactions with Related Parties

The Bank has had, and may be expected to have in the future, banking transactions in the ordinary course of business with directors, principal officers, their immediate families and affiliated companies in which they are principal shareholders (commonly referred to as related parties), all which have been, in the opinion of management, on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others.

Aggregate loan transactions with related parties as of December 31 were as follows:

	2019	2018
Balance, beginning	$ 6,473,806	$ 6,643,310
New loans	15,934	307,784
Repayments	(708,490)	(477,288)
Balance, ending	$ 5,781,250	$ 6,473,806

Deposit accounts with related parties approximated $4,223,258 and $3,854,394 at December 31, 2019 and 2018, respectively.

The Bank utilizes an appraisal company owned by a director for loan appraisal services. Appraisal fees are reimbursed to the Bank from the respective borrowers.

NOTES TO FINANCIAL STATEMENTS *continued*

Note 16. Transactions with Related Parties (Continued)

The Bank has instituted a split dollar deferred compensation plan for certain officers. The vehicle is funded through Bank Owned Life Insurance (BOLI). The BOLI had a balance of $4,001,452 and $3,911,360 as of December 31, 2019 and 2018, respectively. The accrued deferred compensation had a balance of $119,492 and $102,230 as of December 31, 2019 and 2018, respectively.

Amounts due officers and directors under non-qualified deferred compensation agreements were $357,226 and $203,828 at December 31, 2019 and 2018, respectively.

Note 17. Disclosures about Fair Value of Financial Instruments

Fair Value Measurement

The following methods and assumptions were used by the Bank in estimating its fair value disclosures for financial instruments, and for assets measured on recurring basis and non-recurring basis:

Cash and due from banks: The carrying amounts reported in the balance sheet for cash and due from banks, including certificates of deposit, approximate those assets' fair values.

Investment securities: Fair values for investment securities are based on quoted market prices, where available (level one valuation). If quoted market prices are not available, fair values are calculated based on a formula which uses matrices which interpolate prices according to observable inputs for similar items such as sector, credit spread, rating, maturity, and option premium (level two valuations).

Federal Home Loan Bank stock: The carrying amount of this stock approximates its fair value.

Loans and loans held for sale: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying amounts. The fair values of other loans (for example, fixed rate commercial real estate and rental property mortgage loans and commercial and industrial loans) are estimated using discounted cash flow analysis, based on interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Loan fair value estimates include judgments regarding future expected loss experience and risk characteristics. Collateral values are estimated using Level 2 inputs based on appraisals of similar properties obtained from a third party valuation service. Fair values for impaired loans are estimated using Level 3 inputs based on appraisals of similar properties obtained from a third party valuation service discounted by management based on historical losses for similar collateral and discounted cash flow analysis.

Other real estate owned: Other real estate owned is reported at the fair value of the underlying collateral. Collateral values are estimated using Level 3 inputs based on appraisals of similar properties obtained from a third party valuation service discounted by management based on updated information.

Note 17. Disclosures about Fair Value of Financial Instruments (Continued)

Deposits: The fair values disclosed for demand deposits (for example, checking and savings accounts) are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The fair values for 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 contractual maturities on such time deposits (Level 2).

Repurchase agreements and borrowed funds: For repurchase agreements and borrowed funds (including Federal funds purchased) that reprice frequently, fair values are based on carrying amounts. The fair values for other borrowings are estimated using a discounted cash flow calculation that applies interest rates currently being offered on such debt to a schedule of aggregated contractual maturities on such debt (Level 2).

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

Other liabilities: Commitments to extend credit were evaluated and fair value was estimated using the fees currently charged to enter into similar agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair market value for off balance sheet financial instruments was immaterial at December 31, 2019 and 2018.

The estimated fair values of the Company's financial instruments at December 31 are as follows:

	2019	
	Carrying Amount	Estimated Value
Financial assets:		
Cash and cash equivalents	$ 4,887,225	$ 4,887,225
Interest bearing deposits with banks	9,301,610	9,301,610
Certificates of deposit	3,740,000	3,740,000
Securities available-for-sale	52,496,034	52,496,034
Securities held-to-maturity	-	-
FHLB stock	220,700	220,700
Loans receivable and loans held-for-sale, net (Level 2)	178,618,606	175,070,384
Impaired loans (Level 3)	4,672,819	4,672,819
Accrued interest receivable	1,033,514	1,033,514
Financial liabilities:		
Deposits (Level 2)	229,055,559	229,997,045
Repurchase agreements (Level 2)	3,182,657	3,182,657
Accrued interest payable	25,766	25,766

NOTES TO FINANCIAL STATEMENTS *continued*

Note 17. Disclosures about Fair Value of Financial Instruments (Continued)

	2018	
	Carrying Amount	Estimated Value
Financial assets:		
Cash and cash equivalents	$ 4,986,882	$ 4,986,882
Interest bearing deposits with banks	9,011,651	9,011,651
Certificates of deposit	3,740,000	3,740,000
Securities available-for-sale	48,143,350	48,143,350
Securities held-to-maturity	827,567	827,567
FHLB Stock	392,300	392,300
Loans receivable and loans held-for-sale, net (Level 2)	183,607,093	176,002,903
Impaired loans (Level 3)	3,103,579	3,103,579
Accrued interest receivable	1,021,883	1,021,883
Financial liabilities:		
Deposits (Level 2)	228,628,737	229,086,597
Repurchase agreements (Level 2)	4,734,098	4,734,098
Accrued interest payable	18,847	18,847

The carrying amounts in the preceding table are included in the balance sheets under the applicable captions.

Fair values of assets and liabilities measured on a recurring basis at December 31, 2019 and 2018 are as follows:

	Fair Value	Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2019				
Loans held for sale	$ 517,291	$ -	$ 517,291	$ -
Investments - AFS				
U.S. Government and Federal Agencies	34,121,081	-	34,121,081	-
State and municipal securities	18,374,953	-	18,374,953	-
	$ 53,013,325	$ -	$ 53,013,325	$ -

NOTES TO FINANCIAL STATEMENTS *continued*

Note 17. Disclosures about Fair Value of Financial Instruments (Continued)

	Fair Value	Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2018				
Loans held for sale	$ 162,678	$ -	$ 162,678	$ -
Investments - AFS				
U.S. Government and Federal Agencies	33,694,605	-	33,694,605	-
State and municipal securities	14,448,745	-	14,448,745	-
	$ 48,306,028	$ -	$ 48,306,028	$ -

Fair values of assets and liabilities measured on a non-recurring basis at December 31, 2019 and 2018 are as follows:

	Fair Value	Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2019				
Impaired loans	$ 4,672,819	$ -	$ -	$ 4,672,819
	$ 4,672,819	$ -	$ -	$ 4,672,819
December 31, 2018				
Impaired loans	$ 3,103,579	$ -	$ -	$ 3,103,579
	$ 3,103,579	$ -	$ -	$ 3,103,579

There were $3,102,147 of impaired loans with a related allowance as of December 31, 2019. The residential real estate loans were evaluated using discounts of appraisals ranging from 13% to 40% along with discounted cash flow analysis. The commercial real estate and agricultural real estate loans were evaluated using discounts of appraisals and asset valuations ranging from 15% to 55% along with discounted cash flow analysis.

There were no transfers between levels for both recurring and non-recurring assets for the years ended December 31, 2019 and 2018.

Note 18. Regulatory Matters

The Bank is subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Under the Basel III rules, the Bank must hold a capital conservation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer is being phased in at the rate of 0.625% per year from 0.0% in 2015 to 2.50% on January 1, 2019. The capital conservation buffer for 2019 is 2.50% and for 2018 is 1.875%. The net unrealized gain or loss on available for sale securities is excluded in computing regulatory capital. Management believes as of December 31, 2019, the Bank met all capital adequacy requirements to which they are subject.

Prompt correction action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At year-end 2019 and 2018, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the institution's category.

The Bank's actual capital amounts (000's omitted) and ratios are also presented in the table.

	Actual		Minimums For Capital Adequacy Purposes		Minimums To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2019						
Total capital (to risk weighted assets)	$ 36,389	19.65%	$ 14,813	8.00%	$ 18,516	10.00%
Tier I (core) capital (to risk weighted assets)	$ 34,112	18.42%	$ 11,110	6.00%	$ 14,813	8.00%
Common Tier 1 (CET1) (to risk weighted assets)	$ 34,112	18.42%	$ 8,332	4.50%	$ 12,036	6.50%
Tier I (core) capital (to average assets)	$ 34,112	12.26%	$ 11,133	4.00%	$ 13,917	5.00%

Note 18. Regulatory Matters (Continued)

	Actual		Minimums For Capital Adequacy Purposes		Minimums To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of December 31, 2018						
Total capital (to risk weighted assets)	$ 35,548	19.08%	$ 14,906	8.00%	$ 18,633	10.00%
Tier I (core) capital (to risk weighted assets)	$ 33,241	17.84%	$ 11,180	6.00%	$ 14,906	8.00%
Common Tier 1 (CET1) (to risk weighted assets)	$ 33,241	17.84%	$ 8,385	4.50%	$ 12,111	6.50%
Tier I (core) capital (to average assets)	$ 33,241	12.27%	$ 10,835	4.00%	$ 13,544	5.00%

Note 19. Subsequent Events

The Company has evaluated subsequent events through February 10, 2020, the date which the financial statements were available to be issued.

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Retired Owner, Cioffi Real Estate

John T. Gallagher, *Member of Board of Directors of Peoples Trust Company of St. Albans since 1991*
Owner and President, Gallagher Inc.

Donald G. Poirier, *Secretary and Member of Board of Directors of Peoples Trust Company of St. Albans since 1996*
Retired Executive Vice President, Peoples Trust Company of St. Albans

Mark E. Lareau, *Member of Board of Directors of Peoples Trust Company of St. Albans since 2001*
Owner, Lareau Appraisal Service

Linda M. LeBlanc, *Member of Board of Directors of Peoples Trust Company of St. Albans since 2005*
Retired Senior Executive Officer/Chief Operations Officer of Peoples Trust Company of St. Albans

Leon J. Berthiaume, *Member of Board of Directors of Peoples Trust Company of St. Albans since 2008*
Senior Advisor for Dairy Farmers of America

Frank J. Cioffi, *Member of Board of Directors of Peoples Trust Company of St. Albans since 2009*
President, GBIC (Greater Burlington Industrial Corp.)

Thomas J. Gallagher, *Member of Board of Directors of Peoples Trust Company of St. Albans since 2011*
President/CEO of Peoples Trust Company of St. Albans

John P. Casavant, *Member of Board of Directors of Peoples Trust Company 2016*
Part owner and Vice President at NFP, Inc. (formerly Hackett, Valine and McDonald)

Board of Directors *continued*

David J. Handy, *Member of Board of Directors of Peoples Trust Company 2016*
Co-owner of Handy Buick, Cadillac, GMC, Inc.

Gordon A. Winters, *Member of Board of Directors of Peoples Trust Company 2016*
Owner, ACE Hardware stores in Milton, Jericho, St. Albans, Burlington VT and Champlain, NY

Executive Officers

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Aaron A. Reynolds *Senior Executive Vice President/CFO*

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