ANNUAL Report 2018

turning a new page. . .

Allegheny Bancshares Inc

Pendleton Community Bank

Your bank for generations...

INSIDE this Issue

OUR Mission

PCB, an Independent Community Bank,

is dedicated to **PROVIDING** products and services

that facilitate financial success of our customers,

ENCOURAGING professional success

for our team members,

and **STIMULATING** economic growth

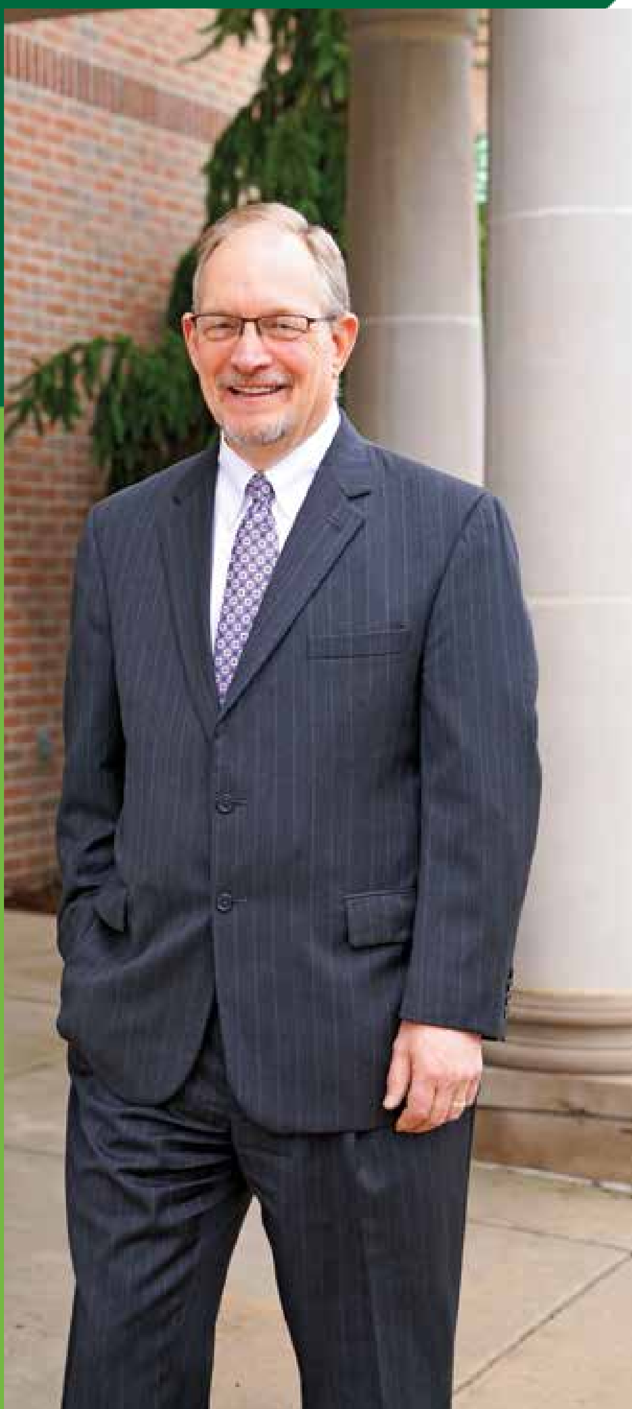
in our communities,

thereby enhancing the value

of “YourBank”.

Your bank for generations...

LETTER to Our Shareholders



DEAR SHAREHOLDER:

Turning the Page. . .

Not only are we turning the page to a new year, we are also excited to be turning the page on a new look and logo- one that we believe looks to the future, and one that honors and remains true to our heritage and deep roots. I know you will share in our excitement of the simple, vibrant look for our organization as we set the stage for not only 2019, but for years to come.

Before I turn to a discussion on 2018's performance, I'd like to focus on two events that are the focus of our "Tribute" section in this report, which impacted our organization in 2018 and early 2019. First, it was with mixed emotions that we announced Richard Phares' election to move to the position of Director Emeritus effective June 1, 2018. Richard's years of service spanned an amazing 49 years and during that time Richard helped direct and make PCB the superior organization we are today. In addition, the entire PCB family was deeply saddened with the passing of Director Emeritus John Heavner. John, who passed away January 23, 2019, tirelessly served as a Director of PCB from 1972 to 2006, when he elected to move to the position of Director Emeritus. John's absence will be evident to our organization and to all who knew him. I know you share in our appreciation of the role both individuals played in our success, as well as in the mourning of the passing of John Heavner.

Turning to 2018, I am excited to report that ABI, through contributions of PCB, had another year of record profitability. Year to date net income was $3,825,122 in comparison to 2017's level of $3,316,038. This growth in earnings ($509,084) represents an increase of 15.35% over last year's revenue. The year's net income provided a 16.41% increase in Earnings Per Share over 2017's level of $3.90 per share, Return on Average Assets of 1.27%, and Return of Equity (ROE) of 10.10%. This strong level of performance compares very favorably with state, national, and local peer group performance.

2018

This year's net income was accomplished by several factors. First, total assets grew by $18.7 million of which the $15.8 million in loan growth was funded by a 7.23% increase in total deposits. Second, continued focus on strategic balance sheet management provided a $556,744 (4.77%) increase in net interest income and supported a strong net interest margin. Finally, the Tax Cuts and Jobs Act provided a reduction in our tax expense; and, along with the aforementioned items, offset increases in operational expenses and investments in people, technology, and our physical facilities and footprint. Speaking of which, we are excited for the upcoming opening of our full-service facility in Wardensville, WV. We are convinced the success of the Wardensville Loan Production office will pave the way for a successful addition to our organization, and, collectively ensure that we will be able to be "your bank for generations".

In closing, as you continue to review this year's report, I trust you will share in my (our) excitement with this year's results and our new look. This year's superior performance would not have been possible without the coordinated and dedicated efforts of the Board of Directors, all of PCB's team members, and you the shareholder. To each, thank you for the part you played in our success and for the honor to lead this great company.

Best Regards,

William A. Loving, Jr., CLBB
President/CEO

Not only are we turning the page to a new year, we are also excited to be turning the page on a new look and logo- one that we believe looks to the future, and one that honors and remains true to our heritage and deep roots.

Your bank for generations...

OUR Board of Directors

"As we reflect on 2018, I would like to extend my sincerest appreciation to the BOARD OF DIRECTORS, OFFICERS, and TEAM MEMBERS who are committed to our MISSION – to enhance the value of "Your Bank". Without the continued support and direction of the Board of Directors and the dedication of our Officers and Staff, record setting outcomes like those highlighted in this annual report would not be possible."

– William A. Loving, Jr., CLBB, President/CEO

William A.
LOVING, JR. CLBB

President
CEO

Carole
HARTMAN

Chair
Farmer

John E.
GLOVER, DDS

Vice Chair
Dentist

Roger
CHAMP

Secretary
Contractor

William
BOSLEY, OD

Doctor of
Optometry

William
BEARD, JR.

Pocahontas County
Commissioner, Farmer

Laura
SIMPSON EVICK

Attorney

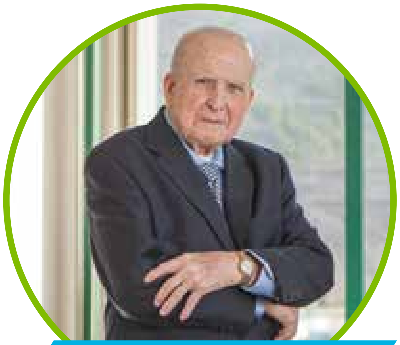
Chad
BRANSON

Associate Broker/
Old Dominion Realty

SPECIAL Tributes

RICHARD PHARES

A special thanks to Richard Phares for 49 years of service on the Board. Richard began serving on the Board of Directors of Pendleton Community Bank on November 13, 1969 and has tirelessly worked to support the goals and objectives of the bank. Richard retired from the Board of Directors and elected to become a Director Emeritus on June 1st, 2018. The Board of Directors want to express their deepest appreciation for the dedication and service Richard has demonstrated over the years.



Director from
1969 to 2018

JOHN HEAVNER

The Board of Directors would like to extend their deepest appreciation for the dedication and service of former Director, John Heavner, who passed away on January 23, 2019. The loss of our friend will be felt not just in banking, but in all walks of life. John tirelessly served with distinction and dedication and was instrumental in the success of this institution and the betterment of the community.

Born April 6, 1936 in Upper Tract, John D. Heavner, was the son of the late Walter Heavner and Anna Dyer Heavner. John was a Veteran, having served in the U.S. Army. A 1954 graduate of Franklin High School, John was a lifelong farmer. He had a passion for growing corn and was known for his "straight corn rows". In addition to being a member of our Board of Directors from 1972 through 2006 and a Director Emeritus until his death, he was also a member of Christ Central Church, and a charter member of both the South Branch Ruritan Club and the Upper Tract Volunteer Fire Dept.

Director from
1972 to 2006

Your bank for generations...

THE PCB Team

William A Loving, Jr., CLBB, President/CEO
L. Kirk Billingsley, CPA, SR. VP–Finance/CFO
Sheldon Arbaugh, SR. VP–West Virginia Area Executive
Josh Byers, SR. VP–Chief Credit Officer
Dan Withers, SR. VP–Virginia Area Executive
Jonah Pence, SR. VP-Virginia Area Executive
Cindy Rader, VP-Mortgage
Erin Sites, CPA, VP–Assistant CFO
Sylvia Smith, VP–Loan Operations
Amanda Smith, VP–Market Manager
Danielle Sisson, VP-Operations/Acting CIO
Kathy Parker, VP–Executive Assistant/Investor Relations/Ethics Officer
Mark Williams, VP-Director of Compliance
Bobby Williams, VP-Agricultural Lending
Tim Cash, VP-Business Development Officer
Tammy Smith, AVP–Electronic Branch Manager
Monika Eckard, CPA, AVP-Director of Human Resources/Affirmative Action Officer
Darla Jones, Collections Officer
Evelyn Simmons, Accounting Assistant/BSA Auditor
Brittany Mitters, Credit Analyst
Laura Roadcap, Internal Auditor
Lori Nelson-Roberson, Loan Review/Compliance Assistant
Natasha Simmons, BSA Assistant
Stephanie Butler, Assistant Operations Manager
Tammy Clutter, AVP-Assistant Loan Operations Manager
Clay Richardson, Public Relations Coordinator
Eric Hartman, Network Administrator
Holly Beachler
Brianna Bruns
Sarah Burns
Tammy Davis
Kim Fox
Renee Hedrick
Joy Hersey
Emily Hull
Debbie Propst
Samantha Puchany
Kitty Rexrode
Kimberly Reyes
Rachel Ruddle
Vicky Simmons
Judy Snyder
Lisa Sponaugle

FRANKLIN FINANCIAL CENTER
Dayne Davis, AVP-Financial Center Manager/Business Development Officer
Jessica Alt
Jessica Basagic, Universal Banker
Missy Bennett
Trish Flynn
Claire Heavner
Teresa Heavner, Universal Banker
Nancy Mallow
Nicole Marsh
Jamie Varner

HARRISONBURG WEST FINANCIAL CENTER
Katie Brill, AVP-Financial Center Manager
Patsy Campbell
Sheri Cave
Kathy Dove
Craig Orndorff, Universal Banker
Rachael Simmons
Sharon Stickley
Denise Streets

HARRISONBURG DOWNTOWN FINANCIAL CENTER
Katie Sinnett, Financial Center Manager
Melissa Elliott
Diana Hernandez
Sydney Moss
Susan Payne, Universal Banker
Teri Stearn
Joan Taylor
Stephanie Walker
Carly Watson
Peter Weaver III, Mortgage Banker

MARLINTON FINANCIAL CENTER
Selina King, AVP-Financial Center Manager
Hope Spencer, Assistant Financial Center Manager
Kendall Beverage, Business Development Officer / Security Officer
Lauren Dunbrack
Rebekah Friel
Steven Gravely
Ashley Moore

MOOREFIELD FINANCIAL CENTER
Melinda Biser, Financial Center Manager
Margaret Shriver, Universal Banker
Joey Vetter, AVP–Business Development Officer
Sarah Barnes
Beverly Berg
Madison Bennett
Dylan Chapman
Wendy Combs
Amanda McDonald
Nicole Ours
Marisol Requeno-Romero
Emily Roberson

PETERSBURG FINANCIAL CENTER
Christina Branham, Financial Center Manager
Nick Yoder, Universal Banker
Tony Calhoun
Richard Cardot
Lori Carr
Casey Goldizen
Donna Idleman
Misty Taylor

LOAN PRODUCTION OFFICE, WARDENSVILLE
Luke Kesner, AVP–LPO Manager/Business Development Officer
Brionna Childers
Ashley Delawder
Lana Watson

Your bank for generations...

FINANCIAL Highlights

	Years ended December 31,				
	2018	2017	2016	2015	2014
	(Dollars in thousands except per share data)				
RESULTS OF OPERATIONS					
Interest income	$ 13,896	$ 12,730	$ 12,238	$ 12,070	$ 11,730
Interest expense	(1,672)	(1,062)	(996)	(1,141)	(1,467)
Net Interest Income	12,224	11,668	11,242	10,929	10,263
Provisions for loan losses	(370)	(450)	(720)	(900)	(750)
Noninterest income	2,441	2,350	2,407	2,231	2,411
Noninterest expenses	(9,608)	(8,759)	(8,400)	(7,711)	(7,802)
Income taxes	(862)	(1,493)	(1,312)	(1,280)	(1,120)
Net Income	$ 3,825	$ 3,316	$ 3,217	$ 3,269	$ 3,002
PROFITABILITY RATIOS					
Return on Average Assets	1.27%	1.16%	1.17%	1.22%	1.13%
Return on Average Equity	10.10%	9.05%	8.93%	9.60%	9.33%
PER COMMON SHARE					
Net Income	$4.54	$3.90	$3.74	$3.80	$3.47
Cash Dividends Declared	2.00	1.88	1.80	1.78	1.70
Book Value	45.51	43.33	41.40	40.27	38.22
Last Reported Market Price	70.00	72.00	72.00	72.00	72.00
AT YEAR END					
Assets	$307,530	$288,858	$276,381	$269,459	$267,652
Deposits	263,655	245,880	236,542	230,171	226,062
Loans, Net	241,353	225,636	212,396	205,668	198,285
Long-term Debt	2,144	2,334	2,515	2,687	2,851
Stockholders' Equity	38,008	36,360	35,109	34,598	32,845
Equity to Assets Ratio	12.36%	12.59%	12.70%	12.84%	12.27%

FINANCIALS 2018

Allegheny Bancshares Inc

Pendleton Community Bank

Your bank for generations...

INDEX TO Financial Statements

Yount Hyde & Barbour
Certified Public Accountants and Consultants

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Stockholders
Allegheny Bancshares, Inc.
Franklin, West Virginia

Report on the Financial Statements
We have audited the accompanying consolidated financial statements of Allegheny Bancshares, Inc. and its subsidiary, which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity and cash flows for the years then ended and the related notes to the consolidated financial statements (collectively, 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 audit 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.

Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Allegheny Bancshares, Inc. and its 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.

Yount, Hyde & Barbour, P.C.

Roanoke, Virginia
February 22, 2019

CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2018 AND 2017

	2018	2017
ASSETS		
Cash and cash equivalents	$ 5,934,431	$ 7,406,252
Interest bearing deposits in banks	4,336,432	3,194,776
Investment securities available for sale, at fair value	37,148,157	35,274,045
Restricted equity securities	228,095	227,495
Loans receivable, net of allowance for loans losses of $2,685,984 in 2018 and $2,628,218 in 2017	241,353,392	225,635,938
Bank premises and equipment, net	5,549,609	5,482,120
Interest receivable	1,290,297	1,252,937
Goodwill	1,086,732	1,086,732
Bank owned life insurance	8,711,294	7,305,923
Other real estate owned, net of valuation allowance of $214,000 in 2018 and $221,250 in 2017	681,500	821,100
Other assets	1,210,166	1,170,615
Total Assets	$ 307,530,105	$ 288,857,933
LIABILITIES		
Deposits		
Noninterest bearing	$ 61,183,662	$ 58,632,011
Interest bearing		
Demand	46,863,803	47,486,746
Savings	71,942,711	56,742,425
Time deposits over $250,000	10,708,825	9,820,722
Other time deposits	72,955,800	73,197,788
Total Deposits	263,654,801	245,879,692
Securities sold under agreements to repurchase	1,013,491	1,869,924
Accrued expenses and other liabilities	2,709,759	2,414,085
Long-term debt	2,144,185	2,334,343
Total Liabilities	269,522,236	252,498,044
STOCKHOLDERS' EQUITY		
Common stock; $1 par value, 2,000,000 shares authorized, 784,554 shares issued in 2018 and 2017	784,554	784,554
Class A Common stock; $1 par value, 2,000,000 shares authorized, 108,872 shares issued in 2018 and 2017	108,872	108,872
Class B Common stock, $1 par value, 2,000,000 shares authorized, 6,574 shares issued in 2018 and 2017	6,574	6,574
Additional paid in capital	900,000	900,000
Retained earnings	39,980,775	37,837,683
Accumulated other comprehensive (loss) income	(12,999)	240,913
Common Treasury stock (at cost, 61,723 shares and 57,723 shares, respectively)	(3,567,787)	(3,327,787)
Class A Treasury stock (at cost, 3,185 shares and 3,165 shares, respectively)	(191,100)	(189,900)
Class B Treasury stock (at cost, 17 shares)	(1,020)	(1,020)
Total Stockholders' Equity	38,007,869	36,359,889
Total Liabilities and Stockholders' Equity	$ 307,530,105	$ 288,857,933

See accompanying notes to consolidated financial statements

ALLEGHENY BANCSHARES, INC.

CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	2018	2017
Interest Income:		
Loans and fees	$ 12,832,813	$ 11,742,821
Interest bearing deposits in banks	147,538	109,934
Investment securities – taxable	336,966	320,390
Investment securities – nontaxable	579,045	556,650
Total Interest Income	13,896,362	12,729,795
Interest Expense:		
Interest on deposits	1,537,760	929,799
Interest on borrowings	134,105	132,243
Total Interest Expense	1,671,865	1,062,042
Net Interest Income	12,224,497	11,667,753
Provision for loan losses	370,000	450,000
Net Interest Income After Provision for Loan Losses	11,854,497	11,217,753
Noninterest Income:		
Service charges, fees and commissions	1,195,420	1,218,413
Increase in cash value of bank owned life insurance	205,371	165,450
(Loss) Gain on sale of available for sale securities, net	(939)	9,475
Other income	1,040,842	956,325
Total Noninterest Income	2,440,694	2,349,663
Noninterest Expense:		
Salaries and benefits	5,055,581	4,609,049
Occupancy expenses	698,049	730,630
Equipment expenses	1,160,642	1,042,230
Director's fees	294,924	309,266
Losses on sale and writedowns of other real estate owned, net	99,281	47,076
Other expenses	2,299,517	2,020,732
Total Noninterest Expenses	9,607,994	8,758,983
Income before Income Taxes	4,687,197	4,808,433
Income Tax Expense	862,075	1,492,395
Net Income	$ 3,825,122	$ 3,316,038
Net Income per share of Common, basic and diluted	$ 4.54	$ 3.90
Net Income per share of Common Class A, basic and diluted	$ 4.77	$ 4.10
Net Income per share of Common Class B, basic and diluted	$ 5.00	$ 4.29
Cash dividends paid per share of Common	$ 2.00	$ 1.88
Cash dividends paid per share of Common Class A	$ 2.10	$ 1.97
Cash dividends paid per share of Common Class B	$ 2.20	$ 2.07
Weighted Average Shares Outstanding, Common	723,984	731,663
Weighted Average Shares Outstanding, Common Class A	105,699	105,849
Weighted Average Shares Outstanding, Common Class B	6,557	6,557

See accompanying notes to consolidated financial statements

ALLEGHENY BANCSHARES, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	2018	2017
Net Income	$ 3,825,122	$ 3,316,038
Other Comprehensive Income (Loss)		
Unrealized gains (losses) arising during the period on		
available for sale securities	(322,346)	108,400
Adjustments for income tax benefit (expense)	67,693	(36,856)
	(254,653)	71,544
Reclassification adjustment for net loss (gains) included in net income	939	(9,475)
Adjustment for income tax (benefit) expense	(198)	3,222
	741	(6,253)
Total other comprehensive income (loss)	(253,912)	65,291
Total comprehensive income	$ 3,571,210	$ 3,381,329

See accompanying notes to consolidated financial statements

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	2018	2017
Cash Flows from Operating Activities:		
Net Income	$ 3,825,122	$ 3,316,038
Adjustment to reconcile net income to net cash		
provided by operating activities:		
Provision for loan losses	370,000	450,000
Depreciation and amortization	540,104	539,956
Net amortization of securities	351,596	383,766
Loss (Gain) on sale of available for sale securities, net	939	(9,475)
Loss on sale of bank premises and equipment	- -	22,519
Deferred income tax expense	(153,393)	123,856
Increase in bank owned life insurance	(205,371)	(165,450)
Loss on sale and writedowns of other real estate owned	99,281	47,076
Net change in:		
Interest receivable	(37,360)	(88,667)
Other assets	104,837	(405,872)
Accrued expense and other liabilities	295,674	815,663
Net Cash Provided by Operating Activities	5,191,429	5,029,410
Cash Flows from Investing Activities:		
Net change in interest bearing deposits in banks	(1,141,656)	2,720,878
Proceeds from sales, calls and maturities of available		
for sale securities	2,168,747	4,946,950
Purchase of available for sale securities	(4,716,801)	(7,720,025)
Purchase of restricted investments	(154,600)	(2,900)
Purchase of bank owned life insurance	(1,200,000)	- -
Proceeds from redemption of restricted investments	154,000	7,700
Proceeds from sale of other real estate owned	116,819	345,699
Purchase of bank premises and equipment	(607,593)	(181,068)
Net changes in loans	(16,087,454)	(13,689,588)
Net Cash (Used in) Investing Activities	(21,468,538)	(13,572,354)
Cash Flows from Financing Activities:		
Net change in:		
Demand and savings deposits	17,128,994	12,105,947
Time deposits	646,115	(2,767,887)
Securities sold under agreements to repurchase	(856,433)	1,253,101
Curtailments of long-term borrowings	(190,158)	(180,884)
Purchase of treasury stock	(241,200)	(542,160)
Cash dividends paid	(1,682,030)	(1,588,258)
Net Cash Provided by Financing Activities	14,805,288	8,279,859
Cash and Cash Equivalents		
Net (decrease) in cash and cash equivalents	(1,471,821)	(263,085)
Cash and cash equivalents, January 1	7,406,252	7,669,337
Cash and cash equivalents, December 31	$ 5,934,431	$ 7,406,252
Supplemental Disclosure of Cash Paid During the Year for:		
Interest	$ 1,615,280	$ 1,052,214
Income taxes	$ 739,900	$ 1,534,259
Supplemental Schedule of Noncash Investing and Financing Activities:		
Other real estate acquired in settlement of loans	$ 76,500	$ 116,000
Unrealized (losses) gains on securities available for sale	$ (321,407)	$ 98,925
Reclassification of stranded tax effects from change in tax rate	$ - -	$ 39,644

See accompanying notes to consolidated financial statements

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	Total	Common Stock	Class A Common Stock	Class B Common Stock
Balance December 31, 2016	$ 35,108,978	$ 784,554	$ 108,872	$ 6,574
Net Income	3,316,038	- -	- -	- -
Other Comprehensive Income	65,291	- -	- -	- -
Reclassification of Stranded Tax Effects from Change in Tax Rate	- -	- -	- -	- -
Purchase of Treasury Stock	(542,160)	- -	- -	- -
Dividends Paid	(1,588,258)	- -	- -	- -
Balance December 31, 2017	$ 36,359,889	$ 784,554	$ 108,872	$ 6,574
Net Income	3,825,122	- -	- -	- -
Other Comprehensive Loss	(253,912)	- -	- -	- -
Purchase of Treasury Stock	(241,200)	- -	- -	- -
Dividends Paid	(1,682,030)	- -	- -	- -
Balance December 31, 2018	$ 38,007,869	$ 784,554	$ 108,872	$ 6,574

Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Common Treasury Stock	Class A Treasury Stock	Class B Treasury Stock
$ 900,000	$ 36,149,547	$ 135,978	$ (2,833,627)	$ (141,900)	$ (1,020)
- -	3,316,038	- -	- -	- -	- -
- -	- -	65,291	- -	- -	- -
- -	(39,644)	39,644	- -	- -	- -
- -	- -	- -	(494,160)	(48,000)	- -
- -	(1,588,258)	- -	- -	- -	- -
$ 900,000	$ 37,837,683	$ 240,913	$ (3,327,787)	$ (189,900)	$ (1,020)
- -	3,825,122	- -	- -	- -	- -
- -	- -	(253,912)	- -	- -	- -
- -	- -	- -	(240,000)	(1,200)	- -
- -	(1,682,030)	- -	- -	- -	- -
$ 900,000	$ 39,980,775	$ (12,999)	$ (3,567,787)	$ (191,100)	$ (1,020)

See accompanying notes to consolidated financial statements

Notes to Consolidated Financial Statements

Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Allegheny Bancshares ("Company") is a bank holding company and operates under a charter issued by the state of West Virginia. The Company owns all of the outstanding stock of Pendleton Community Bank ("Bank"), which operates under a charter issued by the State of West Virginia and provides commercial banking services to customers located primarily in Pendleton County, West Virginia and adjacent counties. As a state chartered bank, the Bank is subject to regulation by the Department of Banking for the State of West Virginia and the Federal Deposit Insurance Corporation. The Bank is engaged in the general commercial banking business offering a full range of banking services focused primarily towards serving individuals, small businesses, the agricultural industry, local government entities, and the professional community.

The Bank's primary trade area includes the West Virginia localities of Pendleton, Grant, Hardy and Pocahontas counties, including the towns of Franklin, Marlinton, Moorefield, and Petersburg. In Virginia, the Bank has two full service offices, one in downtown Harrisonburg, Virginia and one just outside the city of Harrisonburg. In addition, the Bank operates a loan production office in the town of Wardensville, West Virginia with plans to open a full service branch in Wardensville in the first half of 2019.

The accounting and reporting policies of the Company and its subsidiary conform to the U.S. generally accepted accounting principles and to accepted practice within the banking industry. A summary of significant accounting policies is as follows:

Classes of Commons Stock –The Company has three classes of common stock as follows: Common Stock, Class A Common Stock and Class B Common Stock. Common Stock has full voting rights on any and all matters that come before a vote of the Company's shareholders.

Class A Common Stock shareholders receive a 5% premium over the dividend paid on Common Stock, and Class A shareholders are only allowed to vote if shareholders are being asked to approve a merger, consolidation, conversion or sale of assets outside the normal course of business. Class A Common Stock will have a liquidation preference over Common Stock and Class B Common Stock.

Class B Common Stock shareholders receive a 10% premium over the dividend paid on Common Stock, and Class B shareholders are only allowed to vote if shareholders are being asked to approve a merger, consolidation, conversion or sale of assets outside the normal course of business. Class B Common Stock will have a liquidation preference over Common Stock, but after Class A Common Stock.

Consolidation Policy – The consolidated financial statements include Allegheny Bancshares, Inc. and Pendleton Community Bank. All significant intercompany balances and transactions have been eliminated.

Use of Estimates – The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses and the valuation of real estate in connection with foreclosures or in satisfaction of loans. In connection with the determination for the allowances for loan loss and foreclosed real estate, management obtains independent appraisals for significant properties.

While management uses available information to recognize loan losses, future additions to the allowance may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as a part of their routine examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examinations. Because of these factors, it is reasonably possible that the allowance for loan losses may change materially in the near term.

Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and Cash Equivalents – Cash and cash equivalents as used in the consolidated balance sheets and consolidated cash flow statements is defined as cash on hand and noninterest bearing funds at correspondent institutions.

Investment Securities – Investment securities which the Company intends to hold for indefinite periods of time, including investment securities used as part of the Company's asset/liability management strategy, are classified as available for sale. These investment securities are carried at fair value.

Interest and dividends on securities and amortization of premiums and accretion of discounts on securities are reported as interest income using the effective interest method. Gains and losses on the sale of investment securities are determined using the specific identification method.

Declines in the fair value of available-for-sale securities below their cost that are determined to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the intent of the Bank to sell the security, (2) whether it is more likely than not that the Bank will be required to sell the security before recovery of its amortized cost basis, and (3) whether the Bank expects to recover the security's entire amortized cost basis regardless of the Bank's intent to sell the security. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Loans – Loans are intended to be held until maturity and are shown on the consolidated balance sheets net of the allowance for loan losses. Interest is computed by using an effective interest method which generally results in level rates of return on principal. Interest income generally is not recognized on loans classified as nonaccrual loans. Payments received on such loans are applied as a reduction of the loan principal balance. Interest income on other impaired loans is recognized only to the extent of interest payments received. Loans will remain in nonaccrual status unless the loans are brought current per the loan contract and financial conditions have improved to a point that the likelihood of further loss is remote.

In the normal course of business, to meet the credit needs of its customers, the Company has made commitments to extend credit. These commitments represent a credit risk, which is not recognized in the Company's consolidated balance sheets. The Company uses the same credit policies in making commitments as it does for other loans. Commitments to extend credit are generally made for a period of one year or less and interest rates are determined when funds are disbursed. Collateral and other security for the loans are determined on a case-by-case basis. Since some of the commitments are expected to expire without being drawn upon, the contract or notional amounts do not necessarily represent future cash requirements. See Note 21 for lending commitments as of December 31, 2018 and 2017.

The accrual of interest on all loans is discontinued when in management's opinion the borrower may be unable to meet payments as they become due. These loans are considered nonaccrual loans, and all interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income.

Allowance for Loan Losses – The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the non-collectability 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.

During these evaluations, particular characteristics associated with a segment of the loan portfolio are also considered. These characteristics are detailed below:

Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

- Commercial loans not secured by real estate, carry risks associated with the successful operation of a business, and the repayments of these loans depend on the profitability and cash flows of the business. Additional risk relates to the value of collateral where depreciation occurs and the valuation is less precise.
- Loans secured by commercial real estate also carry risks associated with the success of the business and the ability to generate a positive cash flow sufficient to service debts. Real estate security diminishes risks only to the extent that a market exists for the subject collateral.
- Consumer loans carry risks associated with the continued credit-worthiness of the borrower and the value of the collateral, such as automobiles which may depreciate more rapidly than other assets. In addition, these loans may be unsecured. Consumer loans are more likely than real estate loans to be immediately affected in an adverse manner by job loss, divorce, illness or personal bankruptcy.
- Real estate secured construction loans carry risks that a project will not be completed as scheduled and budgeted and that the value of the collateral may, at any point, be less than the principal amount of the loan. Additional risks may occur if the general contractor is unable to finish the project as planned due to financial pressures unrelated to the project.
- Residential real estate loans carry risks associated with the continued credit-worthiness of the borrower and changes in the value of the collateral.
- Non profit and tax exempt loans are predominately loans made either to municipalities, or to emergency service organizations such as rescue squads or fire departments. These organizations rely on tax collections in the case of municipalities and often contributions for the rescue organizations. These loans are typically secured by equipment and sometimes real estate. The inherent risk is economic downturn that can hurt contributions or tax receipts.

The primary tool used in managing and controlling problem loans is a watch list report. The report is a listing of all loans or commitments that are either demonstrating signs of becoming problematic or currently considered problem loans. Changes to the report must have the concurrence of the Chief Credit Officer and the Chief Executive Officer.

Occurrence of any of the following criteria is a basis for adding a loan to the watch list report.
- Loans classified as substandard, doubtful or loss by bank examiners, external auditors or loan review based upon financial trends.
- Loans on nonaccrual status.
- Loans more than 90 days delinquent.
- Loans judgmentally selected by executive management or the Board of Directors, due to unexpected changes or events which could have a potentially adverse effect on the borrower’s ability to repay.

When a loan is added to the watch list report, the Chief Credit Officer and the Chief Executive Officer will assess the need for updated valuations. Upon receipt of current value updates, if necessary, these individuals along with the Chief Financial Officer will estimate the need for a specific loss to be allocated in the Bank’s loan loss allowance.

The following guidance has been given as an aid to loan officers in detecting problem loans.
- Financial Statement Analysis – As customer financial statements are received, they should be immediately analyzed to see if there are any significant changes in financial position or operating results.
- Delayed Financial Statements – If we are having problems getting financial statements from a customer, a problem may be developing.
- Delinquent Principal or Interest – Delinquencies are often the first indication of a problem. We carefully review each loan as soon as it becomes past due.
- Marital Difficulties – Marital difficulties often cause businesses financial stress and are a major cause of problem loans.
- Lack of Cooperation – It is in the borrower’s best interest to cooperate with the Bank. We suspect a problem if the customer becomes uncooperative.
- Other Red Flags – The following are additional red flags which could mean a problem situation is developing: more than two extension payments within the past 12 months, illness or death of a principal or key employee, overdrafts, unexpected renewals or unanticipated new borrowing, deteriorating financial ratios, irresponsible behavior on the part of a borrower or cancellation of insurance.

Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

The allowance consists of specific and general components. The specific component relates to loans that are classified as either doubtful or substandard or loans exceeding 90 days past due that exceed $100,000. For such loans, that are also classified as impaired, an allowance is established when the collateral value less estimated costs to sell, or observable market price (or discounted cash flows) of the impaired loan is lower than that carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors including current economic conditions and volume and mix of the existing loan portfolio.

The Bank utilizes a risk grading matrix to assign a risk grade to each of its loans. Credits are graded on a scale of 1 to 8. A description of the general characteristics of the 8 risk grades is as follows:

Risk Grades 1 through 4 (Pass): There are five different risk grades considered to be "Pass" grades. The first four grades are considered those performing credits that presently are considered lesser risk to the Bank. Credits in the Risk Grade 1 category are virtually risk-free and are well-collateralized by deposit accounts held by the Bank. The repayment program is well-defined and achievable and repayment sources are numerous. Risk Grade 2 is reserved for loans secured by readily marketable collateral, or loans within guidelines to borrowers with liquid financial statements with excellent sources of repayment, no significant identifiable risk of collection, and conformity in all respects to Bank policy guidelines, underwriting standards, and Federal and State regulations. A Risk Grade of 3 is reserved for the Bank's loans that are considered average credit risk, meet all the loan policy guidelines, and with no apparent weakness. These loans have no significant identifiable risk of collection. Generally, loans assigned this grade have documented historical cash flow that meets or exceeds required minimum Bank guidelines or that can be supplemented with verifiable cash flow from other sources as well as adequate secondary sources to liquidate debt. Finally, debts with a Risk Grade of 4 are loans considered to be slightly more than average credit risk. They meet the credit guidelines; however, they have certain characteristics which call into question the borrower's financial well-being. It may be elevated debt to income ratio, high loan to value ratio, balance sheet weakness or a cash flow weakness that is deemed to be temporary in nature. These are credits that may require more frequent monitoring.

Risk Grade 5 – Special Mention: The fifth and lowest pass grade is given to this level of risk. These loans have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in the deterioration of the repayment prospects for the asset or in the Bank's credit position at some future date. These loans are not adversely classified and do not expose the Bank to a sufficient risk to warrant adverse classification. Failure to properly monitor such loans or to correct deficiencies could result in greater credit risk in the future.

Risk Grade 6 – Substandard: A substandard loan is inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified as substandard must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt; they are characterized by the possibility that the institution may sustain some loss if the deficiencies are not corrected. Loans in this category are characterized by deterioration in the quality exhibited by any number of well-defined weaknesses requiring corrective action.

Such loans are no longer considered to be adequately protected due to the borrower's declining net worth, lack of earnings capacity, declining collateral margins, and/or unperfected collateral positions. A possibility of loss of a portion of the loan balance cannot be ruled out. The repayment ability of the borrower is marginal or weak, and the loan may have exhibited excessive overdue status or extensions and renewals.

Risk Grade 7 – Doubtful: Loans classified Doubtful have all the weaknesses inherent in loans classified Substandard, plus the added characteristic that the weaknesses make collection or liquidation in full on the basis of current existing facts, conditions, and values highly questionable and improbable. However, these loans are not yet rated as a loss because certain events may occur which would salvage the debt.

Note 1 ***SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):***

The ability of the borrower to service the debt is extremely weak, overdue status is constant, the debt has been placed on non-accrual status, and no definite repayment schedule exists. Doubtful is a temporary grade where a loss is expected but is presently not quantified with any degree of accuracy. Once the loss position is determined, the amount is charged off.

Risk Grade 8 – Loss: Loans classified Loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted.

All classes of loans are 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. 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 the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial real estate, residential real estate and construction loans by either the fair value of the collateral less estimated costs to sell, or present value of expected future cash flows discounted at the loan's effective interest rate.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer loans for impairment disclosures, unless such loans are in excess of $100,000.

In connection with the evaluation of the collectability of all classes of loans which are greater than 90 days past due as to principal or interest for nonaccrual status, any amounts not deemed well secured or otherwise collectible shall be recommended for charge-off at that time. Additionally, charge-off consideration shall be given to loans evaluated in connection with the Bank's loan review policy and procedures and loans identified for repossession or foreclosure or those that meet the criteria for classification as an in-substance foreclosure. In any event, it shall be the policy of the Bank to charge-off amounts deemed uncollectible in the periods when identified. All charge-off amounts are approved by the Board of Directors.

Troubled Debt Restructuring – In situations where, for economic or legal reasons related to a borrower's financial condition, management may grant a concession to the borrower that it would not otherwise consider. The related loan is classified as a troubled debt restructuring ("TDR"). Management strives to identify borrowers in financial difficulty early and work with them to modify their loan to more affordable terms before their loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. In cases where borrowers are granted new terms that provide for a reduction of either interest or principal, management measures any impairment on the restructuring as noted above for impaired loans.

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 Bank – put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (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 or the ability to unilaterally cause the holder to return specific assets.

Other Real Estate Owned – Asset acquired through, or in lieu of, loan foreclosures are held for sale and are initially recorded at fair value, less estimated costs to sell at the date of foreclosure, establishing a new cost basis. Physical possession of residential real estate collateralizing a consumer mortgage loan occurs when legal title is obtained upon completion of a foreclosure or when the borrower conveys all interest in the property to satisfy the loan through completion of a deed in lieu of foreclosure or through a similar loan agreement. Subsequent to foreclosure,

Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

management periodically performs valuations, and the assets are carried at the lower of carrying amount or fair value less estimated costs to sell. Revenue and expenses from operations and changes in valuation allowance are included in other operating expenses.

Bank Premises and Equipment – Land is carried at cost. Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is charged to income over the estimated useful lives of the assets principally on a straight-line method.

For buildings and improvements the estimated useful lives are between 10 and 50 years, the estimated lives for furniture and equipment are 5 to 10 years.

Bank Owned Life Insurance – The Company has purchased life insurance policies on certain key employees. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other amounts due that are probable at settlement.

***Goodwill* –** The Company follows FASB ASC 350-20*, Intangibles-Goodwill and Other* which gives the Company the option to qualitatively determine whether they can bypass the two-step goodwill impairment test. The Company continues to perform the two step process under ASC 350-20. Provisions within this statement require at least annual impairment review or more often if certain impairment conditions exist. The Goodwill resulted from a branch acquisition in 2009.

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

When tax returns are filed, it is highly certain that some positions taken would be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that would be ultimately sustained. The benefit of a tax position is recognized in the financial statements in the period which, based on all available evidence, management believes it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefits that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying consolidated balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination. Interest and penalties associated with the unrecognized tax benefits are classified as additional income taxes in the Consolidated Statements of Income. At December 31, 2018 and 2017, the Company has not identified and recorded any uncertain tax positions.

Net Income per Share – Basic earnings per common share represent income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share reflect additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. The Bank had no potential common shares during the calendar years 2018 and 2017. Earnings per common share is computed using the two-class method. The Class A Common shares carry a 5% dividend preference over common shares, and Class B shares carry a 10% dividend preference over Common shares.

Fair Value of Financial Instruments – Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully discussed in Note 19. Fair value estimates involve uncertainties and matters of significant judgment. Changes in assumption or in market conditions significantly affect the estimates.

Advertising – The Bank follows the policy of charging the costs of advertising to expense as incurred. Total advertising expense incurred for 2018 and 2017 was $255,624 and $256,884, respectively.

Note 1 SUMMARY OF 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, 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.

In February 2018, the FASB issued ASU 2018-02, *Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income ("AOCI").* The Company early adopted this new standard in the prior year. ASU 2018-01 requires reclassification from AOCI to retained earnings for stranded tax effects resulting from the impact of the newly enacted federal corporate income tax rate on items included in AOCI. The amount of this reclassification in 2017 was $39,644.

Recent Accounting Pronouncements

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." The amendments in ASU 2016-01, among other things: 1) Requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. 2) Requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e., securities or loans and receivables). 3) Eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost. The amendments within this ASU are effective for fiscal years beginning after December 15, 2018, and for interim periods within fiscal years beginning after December 15, 2019. The new guidance permits early adoption of the provision that exempts private companies and not-for-profit organizations from having to disclose fair value information about financial instruments measured at amortized cost. The Company is currently assessing the impact that ASU 2016-01 will have on its consolidated financial statements.

During February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." Among other things, in the amendments in ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (1) A lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) A right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, Revenue from Contracts with Customers. The amendments in this ASU are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early application is permitted. Lessees (for capital and operatingleases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The Company is currently assessing the impact that ASU 2016-02 will have on its consolidated financial statements.

During June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The amendments in this ASU, among other things, require the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. In November 2018, the FASB issued ASU No. 2018-19, "Codification Improvements to Topic 326, Financial Instruments – Credit Losses, which modified the effective date for the amendments in this ASU No. 2016-13 to fiscal years beginning after December 15, 2021, and interim periods within those fiscal years. The Company is currently assessing the impact that ASU 2016-13 will have on its consolidated financial statements.

During August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments", to address diversity in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 31, 2019. The amendments should be applied using a retrospective transition method to each period presented. If retrospective application is impractical for some of the issues addressed by the update, the amendments for those issues would be applied prospectively as of the earliest date practicable. Early adoption is permitted, including adoption in an interim period. The Company is currently assessing the impact that ASU 2016-15 will have on its consolidated financial statements.

During January 2017, the FASB issued ASU No. 2017-04, "Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment". The amendments in this ASU simplify how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. Instead, under the amendments in this ASU, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount, and recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The amendments in this ASU are effective for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2021. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Company does not expect the adoption of ASU 2017-04 to have a material impact on its consolidated financial statements.

During March 2017, the FASB issued ASU 2017-08, "Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities." The amendments in this ASU shorten the amortization period for certain callable debt securities purchased at a premium. Upon adoption of the standard, premiums on these qualifying callable debt securities will be amortized to the earliest call date. Discounts on purchased debt securities will continue to be accreted to maturity. The amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early adoption is permitted, including adoption in an interim period. Upon transition, entities should apply the guidance on a modified retrospective basis, with a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption and provide the disclosures required for a change in accounting principle. The Company is currently assessing the impact that ASU 2017-08 will have on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, "Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement." The amendments modify the disclosure requirements in Topic 820 to add disclosures regarding changes in unrealized gains and losses, the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements and the narrative description of measurement uncertainty. Certain disclosure requirements in Topic 820 are also removed or modified. The amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Certain of the amendments are to be applied prospectively while others are to be applied retrospectively. Early adoption is permitted. The Company does not expect the adoption of ASU 2018-13 to have a material impact on its consolidated financial statements.

The Company evaluated subsequent events that have occurred after the balance sheet date, but before the financial statements are issued. There are two types of subsequent events (1) recognized, or those that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements, and (2) nonrecognized, or those that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date.

Subsequent events have been considered through February 22, 2019, the date financial statements were available to be issued. Based on the evaluation, the Company did not identify any other recognized or non-recognized subsequent events that would have required adjustment to or disclosure to the audited financial statements.

Reclassifications – Some items in prior year financial statements were reclassified to conform to the current presentation. Reclassifications were insignificant and had no effect on prior year net income or stockholders' equity.

NOTE 2 RESTRICTIONS ON CASH:

The Company is required by the Federal Reserve to maintain a reserve balance based upon a percentage of deposits. The Company can meet this requirement through cash on hand, balances held with its correspondent bank, and cash held on reserve with Federal Reserve Bank. At December 31, 2018 and 2017, no balance was required to be on reserve with the Federal Reserve Bank.

NOTE 3 INVESTMENT SECURITIES:

The amortized cost and fair values of securities are as follows (in thousands):

December 31, 2018	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities available for sale:				
Mortgage backed obligations of federal agencies	$ 6,321	$ 4	$ 154	$ 6,171
Government sponsored enterprises	4,799	1	33	4,767
Obligations of states and political subdivisions	26,042	276	108	26,210
Total	$ 37,162	$ 281	$ 295	$ 37,148

December 31, 2017	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities available for sale:				
Mortgage backed obligations of federal agencies	$ 5,932	$ 1	$ 93	$ 5,840
Government sponsored enterprises	5,576	33	12	5,597
Obligations of states and political subdivisions	23,458	451	72	23,837
Total	$ 34,966	$ 485	$ 177	$ 35,274

For the years ended December 31, 2018 and 2017, proceeds from sales, calls and maturities of securities available for sale amounted to $2,168,747 and $4,946,950, respectively. Gross gains on sale of investment securities totaled $0 in 2018 and $10,924 in 2017. Gross losses on sale of securities totaled $939 in 2018 and $1,449 in 2017.

The following table shows the gross unrealized losses and fair value of the Company's investment securities with unrealized losses that are deemed to be temporarily impaired (in thousands), aggregated by investment category and length of time that individual securities have been in a continuous, unrealized loss position at December 31. The unrealized losses on the Company's investment securities were caused primarily by increase in interest rates, but the Company feels that no material impairment of value is due to deteriorating financial condition of the issuers. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. Because the Company has the ability and believes it is more likely than not that it

NOTE 3 INVESTMENT SECURITIES (CONTINUED):

will hold those investments until a recovery of fair value, which may be maturity, the Company feels that unrealized losses are temporary. The Company has 26 investments that have unrealized losses at December 31, 2018 and it considers them to be temporarily impaired.

	Less than 12 Months		12 Months or Greater	
December 31, 2018	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Description of Securities:				
Mortgage backed obligations of federal agencies	$ - -	$ - -	$ 5,141	$ 154
Government sponsored enterprises	998	4	2,722	29
Obligations of states and political subdivisions	2,333	20	2,785	88
Total	$ 3,331	$ 24	$ 10,648	$ 271

	Less than 12 Months		12 Months or Greater	
December 31, 2017	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Description of Securities:				
Mortgage backed obligations of federal agencies	$ 2,517	$ 21	$ 3,287	$ 72
Government sponsored enterprises	3,491	12	- -	- -
Obligations of states and political subdivisions	2,532	21	1,357	51
Total	$ 8,540	$ 54	$ 4,644	$ 123

A maturity schedule of securities in thousands as of December 31, 2018, by contractual maturity, is shown below. Actual maturities may differ because borrowers may have the right to call or prepay obligations.

	Amortized Cost	Fair Value
Due:		
In one year or less	$ 1,976	$ 1,966
After one year through five years	12,475	12,407
After five years through ten years	10,129	10,271
Over ten years	12,582	12,504
	$ 37,162	$ 37,148

The carrying value of securities pledged by the Company to secure deposits, repurchase agreements and for other purposes amounted to $27,606,151 and $26,801,611 at December 31, 2018 and 2017, respectively. The fair value of these pledged securities approximates the carrying value.

NOTE 4 RESTRICTED EQUITY SECURITIES:

Restricted equity securities are considered restricted due to lack of marketability. They consist of stock in the Federal Home Loan Bank (FHLB), stock in Federal Agricultural Mortgage Corporation (Farmer Mac) and stock in ICBA Reinsurance Company, LTD. Investment in the FHLB stock is determined by the level of the Bank's participation with FHLB's various products and is collateral against outstanding borrowings from that institution. The FHLB stock is carried at cost of $211,600 at December 31, 2018. The Farmer Mac stock and the ICBA Reinsurance Company stock is the level of stock required to participate in their programs. The Farmer Mac stock is carried at its cost of $14,000 and the ICBA Reinsurance Company stock is carried at its cost of $2,495 at December 31, 2018. Management evaluates these restricted securities for other-than-temporary impairment on an annual basis, and more often when conditions warrant.

NOTE 5 LOANS RECEIVABLE:

Loans receivable outstanding as of December 31, are summarized in thousands:

	2018	2017
Real Estate:		
Commercial:		
Construction and land development	$ 28,093	$ 25,959
Agriculuture	23,410	18,616
Other commercial	43,592	31,202
Residential:		
Construction	5,611	7,785
Consumer residential	100,171	103,926
Non Real Estate:		
Commercial and industrial	19,431	16,923
Consumer	11,522	11,414
Nonprofit and tax exempt loans	12,209	12,439
Total Loans	244,039	228,264
Less Allowance for Loan Losses	2,686	2,628
Loans Receivable	$ 241,353	$ 225,636

Demand deposit accounts that are overdrawn have been reclassified as a loan since they represent an amount owed to the Bank. The amount of overdrawn accounts included in the loan balance are $231,228 and $175,083 at December 31, 2018 and 2017, respectively, and are included in the non-real estate consumer loan balance above.

Substantially all of our 1-4 family mortgages as well as our multi-family residential mortgages are covered under a blanket lien with the Federal Home Loan Bank for borrowings.

Loans accounted for on a nonaccrual basis were $2,635,926 and $865,880 at December 31, 2018 and 2017 (1.08% and 0.38% of total loans), respectively. Accruing loans which are contractually past due 90 days or more as to principal or interest totaled $439,531 and $806,524 December 31, 2018 and 2017 (0.18% and 0.35% of total loans, respectively). Past due status is determined based on the contractual terms of the loan agreement.

The past due and nonaccrual status of loans as of year-end were as follows (in thousands):

December 31, 2018	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Nonaccrual Loans	Recorded Investment >90 Days and Accruing
Real Estate:								
Commercial:								
Construction and land development	$ 124	$ 1,730	$ 925	$ 2,779	25,314	$ 28,093	$ 2,636	$ 15
Agriculture	- -	- -	- -	- -	23,410	23,410	- -	- -
Other commercial	1,406	- -	- -	1,406	42,186	43,592	- -	- -
Residential:								
Construction	- -	- -	- -	- -	5,611	5,611	- -	- -
Consumer residential	697	916	408	2,021	98,150	100,171	- -	408
Non Real Estate:								
Commercial and industrial	12	- -	- -	12	19,419	19,431	- -	- -
Consumer	58	- -	17	75	11,447	11,522	- -	17
Non profit and tax exempt loans	239	- -	- -	239	11,970	12,209	- -	- -
Total	$ 2,536	$ 2,646	$ 1,350	$ 6,532	$ 237,507	$ 244,039	$ 2,636	$ 440

NOTE 5 LOANS RECEIVABLE (CONTINUED):

December 31, 2017	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Nonaccrual Loans	Recorded Investment >90 Days and Accruing
Real Estate:								
Commercial:								
Construction and land development	$ - -	$ - -	$ 656	$ 656	25,303	$ 25,959	$ 631	$ 25
Agriculture	139	- -	306	445	18,171	18,616	- -	306
Other commercial	2,020	390	28	2,438	28,764	31,202	- -	28
Residential:								
Construction	182	- -	- -	182	7,603	7,785	- -	- -
Consumer residential	1,467	512	622	2,601	101,325	103,926	206	438
Non Real Estate:								
Commercial and industrial	152	29	- -	181	16,742	16,923	- -	- -
Consumer	66	- -	18	84	11,330	11,414	29	10
Non profit and tax exempt loans	174	- -	- -	174	12,265	12,439	- -	- -
Total	$ 4,200	$ 931	$ 1,630	$ 6,761	$ 221,503	$ 228,264	$ 866	$ 807

Impaired loans, which include TDRs of $7,364,933 and $4,024,403 as of December 31, 2018 and 2017 respectively, were as follows:

December 31, 2018 With no related allowance: *(Dollars in Thousands)*	Recorded Investment in Loans	Unpaid Principal Balance	Related Allowance	Average Balance Total Loans	Interest Income Recognized
Commercial:					
Construction and land development	$ 1,864	$ 1,864	$ - -	$ 1,878	$ 66
Agriculture	328	328	- -	392	22
Other commercial	2,045	2,045	- -	2,091	125
Residential:					
Construction	- -	- -	- -	- -	- -
Consumer residential	1,836	1,836	- -	1,966	105
Non Real Estate:			- -		
Commercial and industrial	524	524	- -	508	29
Consumer	- -	- -	- -	- -	- -
Non profit and tax exempt loans	- -	- -	- -	13	- -
Total	$ 6,597	$ 6,597	$ - -	$ 6,848	$ 347

December 31, 2017 With no related allowance: *(Dollars in Thousands)*	Recorded Investment in Loans	Unpaid Principal Balance	Related Allowance	Average Balance Total Loans	Interest Income Recognized
Commercial:					
Construction and land development	$ 2,196	$ 2,196	$ - -	$ 611	$ 9
Agriculture	640	640	- -	698	42
Other commercial	2,245	2,245	- -	893	51
Residential:					
Construction	- -	- -	- -	- -	- -
Consumer residential	1,706	1,706	- -	1,584	69
Non Real Estate:			- -		
Commercial and industrial	270	270	- -	279	12
Consumer	- -	- -	- -	- -	- -
Non profit and tax exempt loans	- -	- -	- -	- -	- -
Total	$ 7,057	$ 7,057	$ - -	$ 4,065	$ 183

NOTE 5 LOANS RECEIVABLE (CONTINUED):

December 31, 2018 **With an allowance recorded:** *(Dollars in Thousands)*	**Recorded Investment in Loans**	**Unpaid Principal Balance**	**Related Allowance**	**Average Balance Total Loans**	**Interest Income Recognized**
Commercial:					
Construction and land development	$ 2,613	$ 2,613	$ 831	$ 2,538	$ 44
Agriculture	- -	- -	- -	130	- -
Other commercial	1,449	1,449	174	1,425	91
Residential:					
Construction	183	183	24	183	11
Consumer residential	861	861	382	745	44
Non Real Estate:					
Commercial and industrial	39	39	5	39	2
Consumer	82	82	82	84	6
Non profit and tax exempt loans	- -	- -	- -	- -	- -
Total	$ 5,227	$ 5,227	$ 1,498	$ 5,144	$ 198

December 31, 2017 **With an allowance recorded:** *(Dollars in Thousands)*	**Recorded Investment in Loans**	**Unpaid Principal Balance**	**Related Allowance**	**Average Balance Total Loans**	**Interest Income Recognized**
Commercial:					
Construction and land development	$ 2,342	$ 2,342	$ 845	$ 1,638	$ 69
Agriculture	- -	- -	- -	- -	- -
Other commercial	1,266	1,266	109	253	16
Residential:					
Construction	182	182	25	144	6
Consumer residential	970	970	373	831	36
Non Real Estate:					
Commercial and industrial	175	175	58	219	9
Consumer	- -	- -	- -	- -	- -
Non profit and tax exempt loans	- -	- -	- -	- -	- -
Total	$ 4,935	$ 4,935	$ 1,410	$ 3,085	$ 136

The recorded investment is defined as the principal balance, less principal payments and charge-offs.

Troubled Debt Restructurings

Included in certain loan categories in the impaired loans table above are troubled debt restructurings ("TDRs") that were classified as impaired. TDRs at December 31, 2018 are comprised of 19 loans totaling $7,364,933. A restructured loan is considered in default when it becomes 90 days past due. One of these 19 loans, which is a residential real estate loan in the amount of $111,934, was considered in default at December 31, 2018. One other of the 19 loans, a commercial construction and development loan in the amount of $1,725,203, while not technically in default at year end, was classified as nonaccrual during 2018. The remaining TDRs, were performing in accordance with their restructured terms, and are not on nonaccrual status. This compares with 17 loans totaling $4,024,403 in restructured loans at December 31, 2017. The amount of the valuation allowance related to total TDRs was $729,785 and $247,319 as of December 31, 2018 and December 31, 2017, respectively. There were no charge-offs of restructured loans during 2018 or 2017.

The 19 loans totaling $7,364,933 in TDRs at December 31, 2018 are represented by two commercial construction and development loans, one agricultural loan, four commercial real estate loans, eight consumer real estate loans, three commercial and industrial loans and one consumer loan.

NOTE 5 LOANS RECEIVABLE (CONTINUED):

During the year 2018, two loans that had previously been restructured went into default. During 2017, no restructured loans went into default. The following table shows these loans that subsequently defaulted during 2018 in thousands:

Class of Loan	Number of Contracts	For the Year Ended December 31, 2018 Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial Real Estate:			
Construction and land development	1	$ 1,725	$ 1,725
Agriculture	- -	- -	- -
Other commercial	- -	- -	- -
Residential Real Estate:			
Construction	- -	- -	- -
Consumer Residential	1	112	112
Non Real Estate:			
Commercial and industrial	- -	- -	- -
Consumer	- -	- -	- -
Non profit and tax exempt entities	- -	- -	- -
Total	2	$ 1,837	$ 1,837

During 2018 the bank restructured 5 loans that were considered to be troubled debt restructurings. These loans totaled $3,487,746 one of which was a commercial construction and development loan, two that were residential real estate loans, and two that were commercial real estate loans. These modifications included rate adjustments, revisions to the amortization schedule, and capitalizing interest, or any combination thereof. The following table presents by class of loan, information related to loans modified in a TDR during 2018 in thousands:

Class of Loan	Number of Contracts	For the Year Ended December 31, 2018 Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial Real Estate:			
Construction and land development	1	$ 561	$ 570
Agriculture	- -	- -	- -
Other commercial	2	2,663	2,690
Residential Real Estate:			
Construction	- -	- -	- -
Consumer Residential	2	227	228
Non Real Estate:			
Commercial and industrial	- -	- -	- -
Consumer	- -	- -	- -
Non profit and tax exempt entities	- -	- -	- -
Total	5	$ 3,451	$ 3,488

NOTE 5 LOANS RECEIVABLE (CONTINUED):

During 2017 the bank restructured 3 loans that were considered to be troubled debt restructurings. These loans totaled $218,375, one of which was a residential real estate loan, one commercial and industrial loan, and one consumer loan. These modifications included rate adjustments, revisions to the amortization schedule, and capitalizing interest, or any combination thereof. The following table presents by class of loan, information related to loans modified in a TDR during 2017 in thousands:

		For the Year Ended December 31, 2017	
Class of Loan	**Number of Contracts**	**Pre-Modification Outstanding Recorded Investment**	**Post-Modification Outstanding Recorded Investment**
Commercial Real Estate:			
Construction and land development	- -	$ - -	$ - -
Agriculture	- -	- -	- -
Other commercial	- -	- -	- -
Residential Real Estate:			
Construction	- -	- -	- -
Consumer Residential	1	89	89
Non Real Estate:			
Commercial and industrial	1	92	40
Consumer	1	89	89
Non profit and tax exempt entities	- -	- -	- -
Total	3	$ 270	$ 218

Management considers troubled debt restructurings and subsequent defaults in restructured loans in the determination of the adequacy of the Company's allowance for loan losses. When identified as a TDR, a loan is evaluated for potential loss based on the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the estimated fair value of the collateral, less any selling costs if the loan is collateral dependent. Loans identified as TDRs frequently are on non-accrual status at the time of the restructuring and, in some cases, partial charge-offs may have already been taken against the loan and a specific allowance may have already been established for the loan. As a result of any modification as a TDR, the specific reserve associated with the loan may be increased. Additionally, loans modified in a TDR are closely monitored for delinquency as an early indicator of possible future defaults. If loans modified in a TDR subsequently default, the Company evaluates the loan for possible further impairment. As a result, any specific allowance may be increased, adjustments may be made in the allocation of the total allowance balance, or partial charge-offs may be taken to further write-down the carrying value of the loan. Management exercises significant judgment in developing estimates for potential losses associated with TDRs.

NOTE 6 ALLOWANCE FOR LOAN LOSSES:

The following table presents, as of December 31, 2018 and 2017, the total allowance for loan losses, the allowance by impairment methodology (individually evaluated for impairment or collectively evaluated for impairment) the total loans and loans by impairment methodology (individually evaluated for impairment or collectively evaluated for impairment) in thousands:

December 31, 2018

	Real Estate Secured					Non Real Estate			
	Commercial			Residential					
	Construction and Land Development	Agricultural	Other Commercial	Construction	Consumer Residential	Commercial & Industrial	Consumer	Non Profit & Tax Exempt	Total
Beginning Balance	$ 1,052	$ 53	$ 618	$ 61	$ 667	$ 96	$ 47	$ 34	$ 2,628
Charge-offs	(156)	- -	- -	- -	(124)	(14)	(127)	- -	(421)
Recoveries	- -	38	- -	- -	1	- -	70	- -	109
Provision	429	(60)	(117)	(30)	93	(53)	130	(22)	370
Ending Balance	$ 1,325	$ 31	$ 501	$ 31	$ 637	$ 29	$ 120	$ 12	$ 2,686
Ending Balance individually valued for impairment	831	- -	174	24	382	5	82	- -	1,498
Ending balance collectively evaluated for impairment	494	31	327	7	255	24	38	12	1,188
Loans:									
Ending Balance individually evaluated for impairment	4,105	328	3,628	183	2,502	996	82	- -	11,824
Ending balance collectively evaluated for impairment	23,988	23,082	39,964	5,428	97,669	18,435	11,440	12,209	232,215
Total Loans	$ 28,093	$ 23,410	$ 43,592	$ 5,611	$ 100,171	$ 19,431	$ 11,522	$ 12,209	$ 244,039

December 31, 2017

	Real Estate Secured					Non Real Estate			
	Commercial			Residential					
	Construction and Land Development	Agricultural	Other Commercial	Construction	Consumer Residential	Commercial & Industrial	Consumer	Non Profit & Tax Exempt	Total
Beginning Balance	$ 72	$ 107	$ 1,180	$ 24	$ 709	$ 69	$ 50	$ 28	$ 2,239
Charge-offs	- -	- -	- -	- -	(33)	(16)	(136)	- -	(185)
Recoveries	8	40	- -	- -	4	- -	72	- -	124
Provision	972	(94)	(562)	37	(13)	43	61	6	450
Ending Balance	$ 1,052	$ 53	$ 618	$ 61	$ 667	$ 96	$ 47	$ 34	$ 2,628
Ending Balance individually valued for impairment	845	- -	109	25	373	58	- -	- -	1,410
Ending balance collectively evaluated for impairment	207	53	509	36	294	38	47	34	1,218
Loans:									
Ending Balance individually evaluated for impairment	4,538	640	3,511	182	2,676	446	- -	- -	11,993
Ending balance collectively evaluated for impairment	21,421	17,976	27,691	7,603	101,250	16,477	11,414	12,439	216,271
Total Loans	$ 25,959	$ 18,616	$ 31,202	$ 7,785	$ 103,926	$ 16,923	$ 11,414	$ 12,439	$ 228,264

NOTE 6 ALLOWANCE FOR LOAN LOSSES (CONTINUED):

Loans by credit quality indicators as of December 31, 2018 were as follows (in thousands):

	Pass	Special Mention	Substandard	Doubtful	Total
Commercial Real Estate:					
Construction and land development	23,547	$ 37	$ 4,509	$ - -	$ 28,093
Agriculture	22,945	428	37	- -	23,410
Other commercial	40,001	254	3,337	- -	43,592
Residential Real Estate:					
Construction	5,428	- -	183	- -	5,611
Consumer Residential	93,640	4,545	1,967	19	100,171
Non Real Estate:					
Commercial and industrial	18,532	576	316	7	19,431
Consumer	11,377	97	44	4	11,522
Non Profit and Tax Exempt Entities	12,209	- -	- -	- -	12,209
Total	$ 227,679	$ 5,937	$ 10,393	$ 30	$ 244,039

Loans by credit quality indicators as of December 31, 2017 were as follows (in thousands):

	Pass	Special Mention	Substandard	Doubtful	Total
Commercial Real Estate:					
Construction and land development	21,318	$ 1,710	$ 2,931	$ - -	$ 25,959
Agriculture	18,244	334	37	1	18,616
Other commercial	27,969	28	3,205	- -	31,202
Residential Real Estate:					
Construction	7,603	- -	182	- -	7,785
Consumer Residential	98,738	3,548	1,640	- -	103,926
Non Real Estate:					
Commercial and industrial	16,106	628	189	- -	16,923
Consumer	11,306	44	64	- -	11,414
Non Profit and Tax Exempt Entities	12,439	- -	- -	- -	12,439
Total	$ 213,723	$ 6,292	$ 8,248	$ 1	$ 228,264

NOTE 7 OTHER REAL ESTATE OWNED:

Changes in other real estate owned for 2018 were as follows (in thousands):

	Other Real Estate Owned	Valuation Allowance	Net
Balance at the beginning of the year	$ 1,042	$ (221)	$ 821
Additions	77	- -	77
Loss on sales and writedowns, net	(55)	(44)	(99)
Sales	(168)	51	(117)
Balance at the end of the year	$ 896	$ (214)	$ 682

Changes in other real estate owned for 2017 were as follows (in thousands):

	Other Real Estate Owned	Valuation Allowance	Net
Balance at the beginning of the year	$ 1,358	$ (260)	$ 1,098
Additions	116	- -	116
Loss on sales and writedowns, net	(33)	(14)	(47)
Sales	(399)	53	(346)
Balance at the end of the year	$ 1,042	$ (221)	$ 821

The major classifications of other real estate owned in the consolidated balance sheets at December 31, 2018 and December 31, 2017 were as follows (in thousands):

	December 31,	
	2018	2017
Commercial Real Estate:		
Construction and land development	$ 518	$ 551
Other commercial	116	191
Residential Real Estate:		
Residential	48	79
	$ 682	$ 821

NOTE 8 BANK PREMISES AND EQUIPMENT:

(In thousands)	December 31,	
	2018	2017
Bank buildings and improvements	$ 7,520	$ 7,201
Furniture and equipment	4,105	3,852
	11,625	11,053
Less accumulated depreciation	6,075	5,571
Bank premises and equipment	$ 5,550	$ 5,482

Depreciation expense on these premises and equipment totaled $540,104 and $539,956 for the years ended December 31, 2018 and 2017, respectively.

NOTE 9 GOODWILL:

The Company follows FASB ASC 350-20 *Goodwill and Other Intangible Assets,* which prescribes the accounting for goodwill and intangible assets subsequent to initial recognition. Provisions within ASC 350-20 require the Company to discontinue any amortization of goodwill and intangible assets with indefinite lives, and require at least annual impairment review or more often if certain impairment conditions exist. With the purchase in 2009 of two Citizens National Bank branches there was $1,086,732 of goodwill recorded. Goodwill was evaluated for impairment as of March 31, 2018 and it was determined that no impairment existed. No events have taken place since the date of the impairment testing that would suggest impairment exists at December 31, 2018.

NOTE 10 BANK OWNED LIFE INSURANCE:

The Bank, in an effort to attract and retain employees, offers a variety of benefits to full time employees. The costs of these benefits continue to grow faster than inflation. In order to offset some of these costs and to offer other benefits the Bank has invested in a Bank Owned Life Insurance (BOLI) contract. Earnings on these contracts are tax exempt.

NOTE 11 TIME DEPOSITS:

At December 31, 2018, the scheduled maturities of time deposits are as follows (in thousands):

2019	$ 34,875
2020	19,217
2021	12,192
2022	8,958
2023	7,811
Thereafter	612
Total	$ 83,665

NOTE 12 SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE:

Securities sold under agreements to repurchase generally mature within one day from the transaction date, unless classified as a term repurchase agreement. Securities sold under agreements to repurchase are reflected at the amount of cash received in connection with the transaction. The Company may be required to provide additional collateral based on the fair value of the underlying securities. The Company has a total of $1,767,459 and $1,802,645, at December 31, 2018 and 2017, respectively, in market value of securities pledged to secure these agreements. The weighted average interest rate on these agreements was 0.89% during 2018. The highest month end balance during 2018 was $1,625,674. For 2017, the highest month end balance was $1,889,924 and the average interest rate was 0.43%.

NOTE 13 LINES OF CREDIT:

The Bank has lines of credit with correspondent banks totaling $15,400,000. At December 31, 2018 and 2017 the Bank had no outstanding balances on these lines. These lines of credit are unsecured. The lenders may withdraw these lines at their discretion and without notice.

NOTE 14 LONG-TERM DEBT:

The Company has borrowings from the Federal Home Loan Bank of Pittsburgh (FHLB). The interest rates on all of the notes payable as of December 31, 2018 and December 31, 2017 were fixed at the time of the advance, and ranged from 4.58% to 5.61%. The FHLB notes are secured by FHLB Stock, as well as investment securities and mortgage loans. The weighted average interest rate is 5.29% at December 31, 2018. The Company has additional available borrowing capacity from the FHLB of $102,445,865.

Repayments of long-term debt are due monthly. Interest expense of $123,211 and $126,406 was incurred on these debts in 2018 and 2017, respectively. The maturities of long-term debt as of December 31, 2017 are as follows:

2019	$ 199,911
2020	210,167
2021	183,760
2022	180,308
2023	189,360
Thereafter	1,180,679
Total	$ 2,144,185

NOTE 15 DIVIDEND LIMITATIONS:

The principal source of funds of Allegheny Bancshares, Inc., is dividends paid by its subsidiary bank. The Code of West Virginia imposes certain restrictions on dividends paid by a state bank. A state bank cannot pay dividends (without the consent of state banking authorities) in excess of the total net profits of the current year and the combined retained profits of the previous two years. As of January 1, 2019, the Bank could pay dividends of up to $3,534,542 without permission of the authorities. Dividends paid by the Bank to the Company totaled $1,932,030 in 2018 and $1,788,258 in 2017.

NOTE 16 INCOME TAXES:

The current and deferred components of income tax expense are as follows (in thousands):

	2018	2017
Current component of income tax expense	$ 1,015	$ 1,368
Deferred income tax expense	$ (153)	$ 14
Deferred tax asset adjustment for enacted change in tax rate	- -	110
Income tax expense	$ 862	$ 1,492

Income Tax expense for 2017 includes a downward adjustment of net deferred tax assets in the amount of $110,000, recorded as a result of the enactment of the Tax Cuts and Jobs Act on December 22, 2017. The Act reduced the corporate Federal tax rate from 34% to 21% effective January 1, 2018.

A reconciliation between the provision for income taxes and the amount computed by multiplying income by the statutory federal income tax rate is as follows (in thousands):

	2018	2017
Income taxes computed at the applicable		
Federal income tax rate	$ 984	$ 1,635
Increase (decrease) resulting from:		
Tax exempt interest income	(270)	(382)
Non-deductible interest expense	8	8
State tax expense, net of federal taxes	135	118
Tax impact from enacted change in tax rate	- -	110
Other	5	3
Income tax expense	$ 862	$ 1,492

NOTE 16 INCOME TAXES (CONTINUED):

The net deferred tax asset arising from temporary differences in thousands as of December 31 is summarized as follows:

	2018	2017
Deferred Tax Asset:		
Provision for loan losses	$ 387	$ 344
Accrued expenses on long term benefits	406	346
Allowance for other real estate owned	52	54
Unrealized loss on securities available for sale	4	- -
Interest on nonaccrual loans	144	120
Total Assets	993	864
Deferred Tax Liabilities:		
Unrealized gain on securities available for sale	- -	64
Depreciation	327	371
Intangible amortization	172	155
Other	43	44
Total Liabilities	542	634
Net Deferred Tax Asset	$ 451	$ 230

NOTE 17 EMPLOYEE BENEFITS:

Defined Contribution Plan: The Bank has a defined contribution plan with 401(k) provisions that is funded with discretionary contributions by the bank that covers substantially all full time employees at the bank. There is a one year waiting period prior for admission to the plan. Contributions to the plan are based on a percentage of each employee's salary plus matching contributions. Investment of employee balances is done through the direction of each employee. Plan contributions by the employer are fully invested in the year of contribution. The amount of contributions by the Company into employees' accounts in the plan was $236,319 and $219,108 for the years ending December 31, 2018 and 2017, respectively.

Supplemental Retirement Agreement: The Bank has a non-qualified Supplemental Retirement Agreement (*"*SERP*"*) with the CEO, that provides for the payment of a monthly supplemental executive retirement benefit equal to annual payments of $105,051 for a 15 year period. Such benefit shall be payable for a period of fifteen years, or under certain circumstances prior to age 65. For each full calendar year the CEO completes with the Bank without separation of service, the CEO shall be credited with 8.33% of this benefit, toward 100% after 12 years. The SERP assumes a 6.25% discount rate. The Company has incurred an employee benefit expense of $126,934 and $114,761 during 2018 and 2017 respectively for this plan. At December 31, 2018 and 2017, the total amount accrued for this obligation was $870,266 and $743,332 respectively. The plan is unfunded. However, life insurance has been acquired on the life of the CEO in amounts sufficient to discharge the obligations of this agreement.

Director Deferred Fee Plan: The Bank adopted a Deferred Fee Plan (DFP) for its directors beginning February 13, 2013. This plan allows the directors to defer any or all of their director fees into this DFP where it will earn interest at a rate as set forth in the plan document. Currently this rate is 6%. In addition to the amounts contributed by the directors, the Bank can also contribute each year on behalf of the directors, the total expense for the bank including discretionary contributions and accrued interest on the deferred account balances totaled $58,842 and $51,197 for 2018 and 2017, respectively. Liability recorded under this plan at yearend totaled $626,779 for 2018 and $525,373 for 2017.

Survivor Income Plan: The Bank adopted a Survivor Income Agreement with certain key management employees in January 2008. The bank will provide death benefits to the employee's beneficiary in the amount ranging from $500,000 to $100,000 for pre separation of duty death benefit and an amount half of that for post separation of duty death benefit. There is a vesting schedule based upon employee reaching normal retirement age (age 62) combined with ten 10 years of service. Expense to the bank totaled $61,813 and $57,768 for 2018 and 2017 respectively. Liability recorded under this plan at yearend totaled $168,712 for 2018 and $149,086 for 2017.

NOTE 18 RELATED PARTY TRANSACTIONS:

During the year, officers, directors, principal stockholders and their affiliates (related parties) were customers of and had transactions with the Company in the ordinary course of business. In management's opinion, these transactions were made on substantially the same terms as those prevailing for other customers for comparable transactions and did not involve more than normal risks.

Deposits for officers and directors totaled $3,056,645 and $2,992,602 for year end 2018 and 2017, respectively.

Loan activity to related parties is as follows (in thousands):

	2018	2017
Beginning of Year	$ 5,775	$ 4,810
Additional borrowings	1,497	1,727
Repayments	(1,124)	(762)
End of Year	$ 6,148	$ 5,775

NOTE 19 FAIR VALUE:

FASB ASC 820-10, *Fair Value Measurements,* provides a definition of fair value for accounting purposes, establishes a framework for measuring fair value and expands related financial disclosures. Accounting standards specify a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. This statement establishes a hierarchy that prioritizes the use of fair value inputs used in valuation methodologies into the following three levels.

Level 1 – Valuation is based on quoted prices for identical instruments traded in active markets.
Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
Level 3 – Valuation is based upon significant inputs that reflect the reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

At December 31, 2018 and 2017, the Company had no liabilities subject to fair value. The following is a description of valuation methodologies used for assets recorded at fair values.

Securities available for sale: Securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, when available. If quoted prices are not available, fair values are measured using independent pricing models. Level 1 securities include those traded by dealers or brokers in an active market. The Company has no Level 1 securities at December 31, 2018 or 2017. For the Company, our Level 2 securities include securities issued by government sponsored entities, mortgage backed securities issued by government sponsored entities, municipal bonds and corporate debt securities. Securities classified as Level 3 include other equities that do not have an active market.

Impaired Loans: The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and a specific allowance for loan loss is established. Loans for which it is probable that payment of interest and principal will not be made when due in accordance with the contractual terms of the loan agreement are considered impaired. If a loan is considered impaired, an allowance for loan loss is established in accordance with FASB ASC 310-10 *Accounting by Creditors for Impairment of a Loan,* by utilizing market price (if available), or at the fair value of the loans' collateral less selling costs (if the loan is collateral dependent). The fair value is determined by the measurement of the fair value of the underlying collateral less estimated costs to sell.

NOTE 19 FAIR VALUE (CONTINUED)

Typically the collateral value is determined by applying a discount to an appraisal that was performed at or about the date of the loan. Due to the age of appraisals, the age of the related comparative property sales used for appraisals and the changing market conditions of real estate, he Company considers its impaired loans to be Level 3 assets which are measured on a nonrecurring basis.

Other Real Estate Owned: Certain assets such as other real estate owned (OREO) are measured at the lower of carrying value or fair value less estimated holding costs and cost to sell. We believe that the fair value component in its valuation follows the provisions of FASB ASC 820-10. Due to age of some appraisals, the age of the related comparative property sales used for appraisals and changing real estate market conditions, the Company considers its OREO to be Level 3 assets and is measured on a nonrecurring basis.

The following table presents the recorded amount of assets measured at fair value (in thousands of dollars):

	Level 1	Level 2	Level 3	Balance 2018
Assets recorded at fair value on a recurring basis:				
Mortgage backed obligations of federal agencies	$ - -	$ 6,171	$ - -	$ 6,171
Government sponsored enterprises	- -	4,767	- -	4,767
Obligations of states and political subdivisions	- -	26,210	- -	26,210
Total	$ - -	$ 37,148	$ - -	$ 37,148
Assets recorded at fair value on a nonrecurring basis:				
Impaired loans	$ - -	$ - -	$ 3,729	$ 3,729
Other real estate owned	- -	- -	682	682
Total	$ - -	$ - -	$ 4,411	$ 4,411

	Level 1	Level 2	Level 3	Balance 2017
Assets recorded at fair value on a recurring basis:				
Mortgage backed obligations of federal agencies	$ - -	$ 5,840	$ - -	$ 5,840
Government sponsored enterprises	- -	5,597	- -	5,597
Obligations of states and political subdivisions	- -	23,837	- -	23,837
Total	$ - -	$ 35,274	$ - -	$ 35,274
Assets recorded at fair value on a nonrecurring basis:				
Impaired loans	$ - -	$ - -	$ 3,525	$ 3,525
Other real estate owned	- -	- -	821	821
Total	$ - -	$ - -	$ 4,346	$ 4,346

Qualitative Information About Level 3 Fair Value Measurements for December 31, 2018
(in thousands)

	Fair Value	Valuation Technique(s)	Unobservable Input	Range (Weighted Average)
Assets				
Impaired Loans	$ 3,729	Discounted appraised value	Selling Cost	5%-10% (6%)
			Discount for lack of marketability and age of appraisal	10%-40% (14%)
Other Real Estate Owned	$ 682	Discounted appraised value	Selling Cost	5%-10% (6%)
			Discount for lack of marketability and age of appraisal	10%-60% (64%)

Qualitative Information About Level 3 Fair Value Measurements for December 31, 2017
(in thousands)

	Fair Value	Valuation Technique(s)	Unobservable Input	Range (Weighted Average)
Assets				
Impaired Loans	$ 3,525	Discounted appraised value	Selling Cost	5%-10% (6%)
			Discount for lack of marketability and age of appraisal	10%-40% (14%)
Other Real Estate Owned	$ 821	Discounted appraised value	Selling Cost	5%-10% (6%)
			Discount for lack of marketability and age of appraisal	10%-60% (64%)

NOTE 20 REGULATORY MATTERS:

Banks and bank holding companies are 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 judgements 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 Company 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. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital. Management believes as of December 31, 2018, the Company and Bank meet all capital adequacy requirements to which they are subject.

Prompt corrective 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 2018 and 2017, 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 and ratios, which are substantially the same as those of the Company on a consolidated basis, are presented below (in thousands).

	Actual		Minimum for Capital Adequacy Purposes		Minimum to be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of December 31, 2018						
Total Capital Risk Weighted Assets	$ 39,566	16.73%	$ 18,941	8.000%	$ 23,676	10.00%
Tier I Capital Risk Weighted Assets	36,880	15.60%	14,206	6.000%	18,941	8.00%
Tier I Common Equity	36,880	15.60%	10,654	4.500%	15,390	6.50%
Tier I Capital Average Assets	36,880	11.92%	12,391	4.000%	15,488	5.00%

	Actual		Minimum for Capital Adequacy Purposes		Minimum to be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of December 31, 2017						
Total Capital Risk Weighted Assets	$ 37,547	17.28%	$ 16,367	8.000%	$ 21,731	10.00%
Tier I Capital Risk Weighted Assets	34,919	16.07%	12,252	6.000%	17,384	8.00%
Tier I Common Equity	34,919	16.07%	9,189	4.500%	14,125	6.50%
Tier I Capital Average Assets	34,919	11.98%	11,185	4.000%	14,573	5.00%

NOTE 21 FINANCIAL INSTRUMENTS WITH OFF BALANCE SHEET RISK:

The Company makes commitments to extend credit in the normal course of business and issue standby letters of credit to meet the financing needs of their customers. The amount of the commitments represents the Company’s exposure to credit loss that is not included in the consolidated balance sheet.

The Company uses the same credit policies in making commitments and issuing letters of credit as used for the loans reflected on the consolidated balance sheet. Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer’s creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon the extension of credit, is based on management’s credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment, commercial and residential real estate.

NOTE 21 FINANCIAL INSTRUMENTS WITH OFF BALANCE SHEET RISK (CONTINUED):

As of December 31, 2018 and 2017, the Company had outstanding the following commitments (in thousands):

	2018	2017
Home equity lines of credit	$ 12,460	$ 11,919
Commitments to fund commercial real estate and construction	9,996	5,967
Other unused commitments	20,798	23,321
Performance standby letters of credit	592	540
	$ 43,846	$ 41,747

NOTE 22 CONCENTRATIONS:

The Bank operates as a community bank in the areas that it serves. As such, the loan portfolio consists of commercial, residential real estate and consumer loans to individuals and businesses located primarily in the areas surrounding our six offices. In addition, the collateral for our loans is secured primarily by real estate and personal property located in this same area.

NOTE 23 PARENT CORPORATION ONLY CONDENSED FINANCIAL STATEMENTS:

BALANCE SHEETS
DECEMBER 31, 2018 AND 2017

	December 31,	
	2018	2017
ASSETS		
Cash	$ 30,022	$ 67,699
Investment in subsidiary	37,960,037	36,261,951
Other assets	17,810	30,239
Total Assets	$ 38,007,869	$ 36,359,889
STOCKHOLDERS' EQUITY	38,007,869	36,359,889
Total Liabilities and Stockholders' Equity	$ 38,007,869	$ 36,359,889

NOTE 23 PARENT CORPORATION ONLY FINANCIAL STATEMENTS (CONTINUED):

STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	December 31, 2018	December 31, 2017
INCOME		
Dividends from subsidiary	$ 1,932,030	$ 1,788,258
Gain on sale of securities	- -	- -
Total Income	1,932,030	1,788,258
EXPENSES		
Professional fees	53,870	62,731
Annual shareholder meeting	18,246	18,165
Other expenses	4,600	4,407
Total Expenses	76,716	85,303
INCOME BEFORE INCOME TAX BENEFIT AND UNDISTRIBUTED INCOME OF SUBSIDIARY	1,855,314	1,702,955
Income tax benefit	17,810	30,539
UNDISTRIBUTED INCOME OF SUBSIDIARY	1,951,998	1,582,544
NET INCOME	$ 3,825,122	$ 3,316,038
COMPREHENSIVE INCOME	$ 3,571,953	$ 3,381,329

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	December 31, 2018	December 31, 2017
OPERATING ACTIVITIES		
Net income	$ 3,825,122	$ 3,316,038
Adjustments:		
Undistributed subsidiary income	(1,951,998)	(1,582,544)
Decrease (Increase) in other assets	12,429	263,226
Net Cash Provided by Operating Activities	1,885,553	1,996,720
FINANCING ACTIVITIES		
Purchase of treasury stock	(241,200)	(542,160)
Cash dividends paid	(1,682,030)	(1,588,258)
Net Cash (Used in) Financing Activities	(1,923,230)	(2,130,418)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(37,677)	(133,698)
Cash and equivalents, January 1	67,699	201,397
Cash and equivalents, December 31	$ 30,022	$ 67,699

ALLEGHENY BANCSHARES, INC.
ANNUAL DISCLOSURE STATEMENT

December 31, 2018

This **ANNUAL DISCLOSURE STATEMENT** is being provided by the management of the bank. The information is the representation of management and is correct in all material respects to the best of management's knowledge.

This statement has not been reviewed, or confirmed for accuracy or relevance, by the Federal Deposit Insurance Corporation.

W.A. "Bill" Loving, Jr., CLBB
President / CEO

Allegheny Bancshares, Inc.
PO Box 487
Franklin, WV 26807
PH: 304-358-2311
Fax: 304-358-7997

Your bank
for generations...