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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

■ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended **December 31, 2021**

or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from ____________ to ____________

Commission file number **000-13222**

CITIZENS FINANCIAL SERVICES, INC.
(Exact name of registrant as specified in its charter)

Pennsylvania	**23-2265045**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

15 South Main Street, Mansfield, Pennsylvania	**16933**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code **(570) 662-2121**

Securities registered pursuant to Section 12(b) of the Act: **None**

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, par value $1.00 per share
(Title of class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

☐ Yes ■ No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

☐ Yes ■ No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

■ Yes ☐ No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

■ Yes ☐ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer", "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.:

Large accelerated filer ☐	Accelerated filer ☐
Non-accelerated filer ■	Smaller reporting company ■

Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended reporting transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) if the Exchange Act.

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report.

☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

☐ Yes ■ No

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter; $220,569,000 as of June 30, 2021.

As of March 1, 2022, there were 3,944,293 shares of the registrant's common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information required by Part III is incorporated by reference to the Registrant's Definitive Proxy Statement for the 2022 Annual Meeting of Shareholders.

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PART I

ITEM 1 – BUSINESS.

CITIZENS FINANCIAL SERVICES, INC.

Citizens Financial Services, Inc. (the “Company”), a Pennsylvania corporation, was incorporated on April 30, 1984 to be the holding company for First Citizens Community Bank (the “Bank”), a Pennsylvania-chartered bank and trust company. During 2020, CZFS Acquisition Company, LLC (CZFS) was formed as a wholly owned subsidiary of the Company, and subsequently the Company’s interest in the Bank was transferred to CZFS to facilitate the merger with MidCoast Community Bancorp, Inc. (MidCoast) and its wholly owned subsidiary, MidCoast Community Bank (“MC Bank”), which was completed on April 17, 2020. The Company is primarily engaged in the ownership and management of CZFS, its subsidiary, the Bank and the Bank’s wholly owned subsidiaries, First Citizens Insurance Agency, Inc. (“First Citizens Insurance”) and 1st Realty of PA LLC (“Realty”). Realty was formed in March of 2019 to manage and sell properties acquired by the Bank in the settlement of a bankruptcy filing with a commercial customer, as well as other properties the Bank obtains in foreclosure.

AVAILABLE INFORMATION

A copy of the Company’s annual report on Form 10-K, quarterly reports on Form 10-Q, current events reports on Form 8-K, and amendments to these reports, filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, are made available free of charge through the Company’s web site at www.firstcitizensbank.com as soon as reasonably practicable after such reports are filed with or furnished to the Securities and Exchange Commission. Copies of the reports the Company files electronically with the Securities and Exchange Commission are also available through the Securities and Exchange Commission’s website at www.sec.gov. Information on our website shall not be considered as incorporated by reference into this Form 10-K.

FIRST CITIZENS COMMUNITY BANK

The Bank is a full-service bank engaged in a broad range of banking activities and services for individual, business, governmental and institutional customers. These activities and services principally include checking, savings, and time deposit accounts; residential, commercial and agricultural real estate, commercial and industrial, state and political subdivision and consumer loans; and a variety of other specialized financial services. The Trust and Investment division of the Bank offers a full range of client investment, estate, mineral management and retirement services.

The Bank’s main office is located at 15 South Main Street, Mansfield (Tioga County), Pennsylvania. In addition to the main office in Mansfield, the Bank operates 29 full service offices and one limited branch office in its market areas. The Bank’s north central, Pennsylvania market area consists of the Pennsylvania Counties of Bradford, Clinton, Potter and Tioga in north central Pennsylvania. It also includes Allegany, Steuben, Chemung and Tioga Counties in Southern New York. The south central Pennsylvania market consists of Lebanon county and portions of Berks, Lancaster and Schuylkill Counties in Pennsylvania. The Central Pennsylvania market consists of our offices in Centre, Clinton and Union counties and the surrounding communities. Our Delaware market consists of Wilmington and Dover, Delaware and portions of Chester County, Pennsylvania and was due to the MidCoast acquisition, completed in April 2020, which added two offices in Wilmington, Delaware and one office in Dover, Delaware. In November of 2020, the Bank opened a full-service branch in Chester County, Pennsylvania. We have received regulatory approval to open a full service branch in Ephrata, Pennsylvania, which is expected to open in the second half of 2022.

The economy of the Bank’s market areas are diversified and include manufacturing industries, wholesale and retail trade, service industries, agricultural and the production of natural resources of gas and timber. We are dependent geographically upon the economic conditions in north central, central and south central Pennsylvania, the southern tier of New York and the cities and surrounding areas of Wilmington and Dover, Delaware.

COMPETITION

The banking industry in the Bank’s service areas are intensely competitive, with competitors including local community banks, larger regional banks, and financial service providers such as consumer finance companies, thrifts, investment firms, mutual funds, insurance companies, credit unions, mortgage banking firms, financial companies, financial affiliates of industrial companies, FinTech and internet entities, and government sponsored agencies, such as Freddie Mac, Fannie Mae and Farm Credit. Competitive pressures continue to increase in our service areas as entities seek both loan and deposit growth, as well as geographic expansion. The Bank is generally competitive with all competing financial institutions in its service areas with respect to interest rates paid on time and savings deposits, service charges on deposit accounts and interest rates charged on loans.

Additional information related to our business and competition is included in Part II, Item 7, "*Management's Discussion and Analysis of Financial Condition and Results of Operations.*"

HUMAN CAPITAL RESOURCES

At December 31, 2021, we had a total of 306 employees, including 22 part-time employees and of which approximately 75% are women. The full-time equivalent of our total employees at December 31, 2021 was 293. As a financial institution, approximately 48% of our employees are employed at our branch and loan production offices, and another 1.3% are employed at our customer care call center. The success of our business is highly dependent on our employees, who provide value to our customers and communities through their dedication to our mission. Our employees are not represented by any collective bargaining group. Management considers its employee relations to be good.

We encourage and support the growth and development of our associates and, wherever possible, seek to fill positions by promotion and transfer from within the organization. Continual learning and career development are advanced through internally developed training programs and specialty education within banking, using universities that offer Banking Management programs. We believe our ability to attract and retain employees is a key to our success. Accordingly, we strive to offer competitive salaries and employee benefits to all employees and monitor salaries in our market areas. At December 31, 2021, 24% of our current staff had been with us for fifteen years or more.

The safety, health and wellness of our employees is a top priority. The COVID-19 pandemic continues to present a unique challenge with regard to maintaining employee safety while continuing successful operations. All employees are asked not to come to work when they experience signs or symptoms of a possible COVID-19 illness and have been provided additional paid time off to cover compensation during such absences. On an ongoing basis, we further promote the health and wellness of our associates by strongly encouraging work-life balance and sponsoring various wellness programs, whereby associates are compensated for incorporating healthy habits into their daily routines.

SUPERVISION AND REGULATION

GENERAL

The Bank is subject to extensive regulation, examination and supervision by the Pennsylvania Department of Banking ("PDB") and, as a member of the Federal Reserve System, by the Board of Governors of the Federal Reserve System (the "FRB"). Federal and state banking laws and regulations govern, among other things, the scope of a bank's business, the investments a bank may make, the reserves against deposits a bank must maintain, terms of deposit accounts, loans a bank makes, the interest rates a bank charges and collateral a bank takes, the activities of a bank with respect to mergers and consolidations and the establishment of branches. The Company is registered as a bank holding company and is subject to supervision and regulation by the FRB under the Bank Holding Company Act of 1956, as amended (the "BHCA").

CARES ACT

In response to the COVID-19 pandemic, the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") was signed into law on March 27, 2020. Among other things, the CARES Act includes the following provisions impacting financial institutions like the Bank:

Community Bank Leverage Ratio (CBLR). The CARES Act directs the federal banking agencies to adopt interim final rules to lower the threshold under the CBLR from 9% to 8% and to provide a reasonable grace period for a community bank that falls below the threshold to regain compliance, in each case until the earlier of the termination date of the national emergency or

December 31, 2020. In April 2020, the federal bank regulatory agencies issued two interim final rules implementing this directive. One interim final rule provides that, as of the second quarter 2020, banking organizations with leverage ratios of 8% or greater (and that meet the other existing qualifying criteria) may elect to use the CBLR framework. It also establishes a two-quarter grace period for qualifying community banking organizations whose leverage ratios fall below the 8% CBLR requirement, so long as the banking organization maintains a leverage ratio of 7% or greater. The second interim final rule provides a transition from the temporary 8% CBLR requirement to a 9% CBLR requirement. It establishes a minimum CBLR of 8% for the second through fourth quarters of 2020, 8.5% for 2021, and 9% thereafter, and maintains a two-quarter grace period for qualifying community banking organizations whose leverage ratios fall no more than 100 basis points below the applicable CBLR requirement.

Temporary Troubled Debt Restructurings Relief. The CARES Act allows banks to elect to suspend requirements under accounting principles generally accepted in the United States of America ("GAAP") for loan modifications related to the COVID-19 pandemic (for loans that were not more than 30 days past due as of December 31, 2019) that would otherwise be categorized as a TDR, including impairment for accounting purposes, until the earlier of 60 days after the termination date of the national emergency or December 31, 2020. Federal banking agencies are required to defer to the determination of the banks making such suspension.

Small Business Administration Paycheck Protection Program. The CARES Act authorizes the SBA's Paycheck Protection Program ("PPP"). The PPP authorizes for small business loans to pay payroll and group health costs, salaries and commissions, mortgage and rent payments, utilities, and interest on other debt. The loans are provided through participating financial institutions, such as the Bank, that process loan applications and service the loans.

PENNSYLVANIA BANKING LAWS

The Pennsylvania Banking Code ("Banking Code") contains detailed provisions governing the organization, location of offices, rights and responsibilities of directors, officers, and employees, as well as corporate powers, savings and investment operations and other aspects of the Bank and its affairs. The Banking Code delegates extensive rule-making power and administrative discretion to the PDB so that the supervision and regulation of state chartered banks may be flexible and readily responsive to changes in economic conditions and in savings and lending practices.

Pennsylvania law also provides Pennsylvania state chartered institutions elective parity with the power of national banks, federal thrifts, and state-chartered institutions in other states as authorized by the FDIC, subject to a required notice to the PDB. The Federal Deposit Insurance Corporation Act ("FDIA"), however, prohibits state chartered banks from making new investments, loans, or becoming involved in activities as principal and equity investments which are not permitted for national banks unless (1) the FDIC determines the activity or investment does not pose a significant risk of loss to the Deposit Insurance Fund and (2) the bank meets all applicable capital requirements. Accordingly, the additional operating authority provided to the Bank by the Banking Code is restricted by the FDIA.

In April 2008, banking regulators in the States of New Jersey, New York, and Pennsylvania entered into a Memorandum of Understanding (the "Interstate MOU") to clarify their respective roles, as home and host state regulators, regarding interstate branching activity on a regional basis pursuant to the Riegle-Neal Amendments Act of 1997. The Interstate MOU establishes the regulatory responsibilities of the respective state banking regulators regarding bank regulatory examinations and is intended to reduce the regulatory burden on state chartered banks branching within the region by eliminating duplicative host state compliance exams. Under the Interstate MOU, the activities of branches we established in New York would be governed by Pennsylvania state law to the same extent that federal law governs the activities of the branch of an out-of-state national bank in such host states. Issues regarding whether a particular host state law is preempted are to be determined in the first instance by the PDB. In the event that the PDB and the applicable host state regulator disagree regarding whether a particular host state law is pre-empted, the PDB and the applicable host state regulator would use their reasonable best efforts to consider all points of view and to resolve the disagreement.

COMMUNITY REINVESTMENT ACT

The Community Reinvestment Act, ("CRA"), as implemented by FRB regulations, provides that the Bank has a continuing and affirmative obligation consistent with its safe and sound operation to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the CRA. The CRA requires the FRB, in connection with its examination of the Bank, to assess the institution's record of meeting the credit needs of its community and to take such record into account in its evaluation of certain corporate applications by such institution, such as mergers and branching. The Bank's most recent rating was "Satisfactory." Various consumer laws and regulations also affect the operations of the Bank. In addition to the impact of regulation, commercial banks are affected significantly by the actions of the FRB as it attempts to control the money supply and credit availability in order to influence the economy.

CURRENT CAPITAL REQUIREMENTS

Federal regulations require FDIC-insured depository institutions, including state-chartered, FRB-member banks, to meet several minimum capital standards. These capital standards were effective January 1, 2015, and result from a final rule implementing regulatory amendments based on recommendations of the Basel Committee on Banking Supervision and certain requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").

The capital standards require the maintenance of common equity Tier 1 capital, Tier 1 capital and total capital to risk-weighted assets of at least 4.5%, 6.0% and 8.0%, respectively, and a leverage ratio of at least 4% of Tier 1 capital. Common equity Tier 1 capital is generally defined as common stockholders' equity and retained earnings. Tier 1 capital is generally defined as common equity Tier 1 and Additional Tier 1 capital. Additional Tier 1 capital generally includes certain noncumulative perpetual preferred stock and related surplus and minority interests in equity accounts of consolidated subsidiaries. Total capital includes Tier 1 capital (common equity Tier 1 capital plus Additional Tier 1 capital) and Tier 2 capital. Tier 2 capital is comprised of capital instruments and related surplus meeting specified requirements, and may include cumulative preferred stock and long-term perpetual preferred stock, mandatory convertible securities, intermediate preferred stock and subordinated debt. Also included in Tier 2 capital is the allowance for loan and lease losses limited to a maximum of 1.25% of risk-weighted assets and, for institutions that have exercised an opt-out election regarding the treatment of Accumulated Other Comprehensive Income ("AOCI"), up to 45% of net unrealized gains on available-for-sale equity securities with readily determinable fair market values. The Company has exercised the AOCI opt-out option and therefore AOCI is not incorporated into common equity Tier 1 capital. Calculation of all types of regulatory capital is subject to deductions and adjustments specified in the regulations.

In determining the amount of risk-weighted assets for purposes of calculating risk-based capital ratios, assets, including certain off-balance sheet assets (e.g., recourse obligations, direct credit substitutes, residual interests) are multiplied by a risk weight factor assigned by the regulations based on the risks believed inherent in the type of asset. Higher levels of capital are required for asset categories believed to present greater risk. For example, a risk weight of 0% is assigned to cash and U.S. government securities, a risk weight of 50% is generally assigned to prudently underwritten first lien one- to four-family residential mortgages, a risk weight of 100% is assigned to commercial and consumer loans, a risk weight of 150% is assigned to certain past due loans and a risk weight of between 0% to 600% is assigned to permissible equity interests, depending on certain specified factors.

In addition to establishing the minimum regulatory capital requirements, the regulations limit capital distributions by the institution and certain discretionary bonus payments to management if an institution does not hold a "capital conservation buffer" consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets above the amount necessary to meet its minimum risk-based capital requirements. The capital conservation buffer requirement was phased in beginning January 1, 2016 at 0.625% of risk-weighted assets and increased each year until fully implemented at 2.5% on January 1, 2019.

The FRB has authority to establish individual minimum capital requirements in appropriate cases upon a determination that an institution's capital level is or may become inadequate in light of the particular risks or circumstances.

As permitted by applicable federal regulation, the Bank has opted to use the community bank leverage ratio (the "CBLR") framework for determining its capital adequacy, as discussed above. If a qualifying community bank fails to maintain the applicable minimum CBLR during the grace period, or if it is unable to restore compliance with the CBLR within the grace period, then it will revert to the Basel III capital framework and the normal Prompt Corrective Action capital categories will apply. At December 31, 2021, the Bank was considered “well-capitalized” under the CBLR framework, with a leverage ratio of 8.94%.

PROMPT CORRECTIVE ACTION RULES

Federal law establishes a system of prompt corrective action to resolve the problems of undercapitalized institutions. The law requires that certain supervisory actions be taken against undercapitalized institutions, the severity of which depends on the degree of undercapitalization. The FRB has adopted regulations to implement the prompt corrective action legislation as to state member banks. The regulations were amended to incorporate the previously mentioned increased regulatory capital standards that were effective January 1, 2015. An institution is deemed to be “well capitalized” if it has a total risk-based capital ratio of 10.0% or greater, a Tier 1 risk-based capital ratio of 8.0% or greater, a leverage ratio of 5.0% or greater and a common equity Tier 1 ratio of 6.5% or greater. An institution is “adequately capitalized” if it has a total risk-based capital ratio of 8.0% or greater, a Tier 1 risk-based capital ratio of 6.0% or greater, a leverage ratio of 4.0% or greater and a common equity Tier 1 ratio of 4.5% or greater. An institution is “undercapitalized” if it has a total risk-based capital ratio of less than 8.0%, a Tier 1 risk-based capital ratio of less than 6.0%, a leverage ratio of less than 4.0% or a common equity Tier 1 ratio of less than 4.5%. An institution is deemed to be “significantly undercapitalized” if it has a total risk-based capital ratio of less than 6.0%, a Tier 1 risk-based capital ratio of less than 4.0%, a leverage ratio of less than 3.0% or a common equity Tier 1 ratio of less than 3.0%. An institution is considered to be “critically undercapitalized” if it has a ratio of tangible equity (as defined in the regulations) to total assets that is equal to or less than 2.0%.

Subject to a narrow exception, a receiver or conservator must be appointed for an institution that is “critically undercapitalized” within specified time frames. The regulations also provide that a capital restoration plan must be filed with the FRB within 45 days of the date an institution is deemed to have received notice that it is “undercapitalized,” “significantly undercapitalized” or “critically undercapitalized.” Compliance with the capital restoration plan must be guaranteed by any parent holding company up to the lesser of 5% of the depository institution’s total assets when it was deemed to be undercapitalized or the amount necessary to achieve compliance with applicable capital requirements. In addition, numerous mandatory supervisory actions become immediately applicable to an undercapitalized institution including, but not limited to, increased monitoring by regulators and restrictions on growth, capital distributions and expansion. The FRB could also take any one of a number of discretionary supervisory actions, including the issuance of a capital directive and the replacement of senior executive officers and directors. Significantly and critically undercapitalized institutions are subject to additional mandatory and discretionary measures.

STANDARDS FOR SAFETY AND SOUNDNESS

The federal banking agencies have adopted Interagency Guidelines prescribing Standards for Safety and Soundness in various areas such as internal controls and information systems, internal audit, loan documentation and credit underwriting, interest rate exposure, asset growth and quality, earnings and compensation, fees and benefits. The guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. If the FRB determines that a state member bank fails to meet any standard prescribed by the guidelines, the FRB may require the institution to submit an acceptable plan to achieve compliance with the standard.

ENFORCEMENT

The PDB maintains enforcement authority over the Bank, including the power to issue cease and desist orders and civil money penalties and remove directors, officers or employees. The PDB also has the power to appoint a conservator or receiver for a bank upon insolvency, imminent insolvency, unsafe or unsound condition or certain other situations. The FRB has primary federal enforcement responsibility over FRB-member state banks and has authority to bring actions against the institution and all institution-affiliated parties, including shareholders, who knowingly or recklessly participate in wrongful actions likely to have an adverse effect on the bank. Formal enforcement action may range from the issuance of a capital directive or a cease and desist order, to removal of officers and/or directors. Civil penalties cover a wide range of violations and can amount to $25,000 per day, or even $1 million per day in especially egregious cases. The FDIC, as deposit insurer, has the authority to recommend to the FRB that enforcement action be taken with respect to a member bank. If the FRB does not take action, the FDIC has authority to take such action under certain circumstances. In general, regulatory enforcement actions occur with respect to situations involving unsafe or unsound practices or conditions, violations of law or regulation or breaches of fiduciary duty. Federal and Pennsylvania law also establish criminal penalties for certain violations.

REGULATORY RESTRICTIONS ON BANK DIVIDENDS

The Bank may not declare a dividend without approval of the FRB, unless the dividend to be declared by the Bank's Board of Directors does not exceed the total of: (i) the Bank's net profits for the current year to date, plus (ii) its retained net profits for the preceding two years, less any required transfers to surplus.

Under Pennsylvania law, the Bank may only declare and pay dividends from its accumulated net earnings. In addition, the Bank may not declare and pay dividends from the surplus funds that Pennsylvania law requires that it maintain. Under these policies and subject to the restrictions applicable to the Bank, the Bank could have declared, during 2021, without prior regulatory approval, aggregate dividends of approximately $20.6 million, plus net profits earned to the date of such dividend declaration.

BANK SECRECY ACT

Under the Bank Secrecy Act (BSA), banks and other financial institutions are required to retain records to assure that the details of financial transactions can be traced if investigators need to do so. Banks are also required to report most cash transactions in amounts exceeding $10,000 made by or on behalf of their customers. Failure to meet BSA requirements may expose the Bank to statutory penalties, and a negative compliance record may affect the willingness of regulating authorities to approve certain actions by the Bank requiring regulatory approval, including acquisition and opening new branches.

INSURANCE OF DEPOSIT ACCOUNTS

The Bank’s deposits are insured up to applicable limits by the Deposit Insurance Fund (DIF) of the FDIC. Under the FDIC’s risk-based assessment system, insured institutions are assigned to one of four risk categories based on supervisory evaluations, regulatory capital levels and certain other factors, with less risky institutions paying lower assessments. An institution’s assessment rate depends upon the category to which it is assigned, and certain adjustments specified by FDIC regulations.

As required by the Dodd-Frank Act, the FDIC has issued final rules implementing changes to the assessment rules. The rules change the assessment base used for calculating deposit insurance assessments from deposits to total assets, less tangible (Tier 1) capital. Since the new base is larger than the previous base, the FDIC also lowered assessment rates so that the rule would not significantly alter the total amount of revenue collected from the industry. The range of adjusted assessment rates is now 2.5 to 45 basis points of the new assessment base. The rule is expected to benefit smaller financial institutions, which typically rely more on deposits for funding, and shift more of the burden for supporting the insurance fund to larger institutions, which are thought to have greater access to nondeposit funding. No institution may pay a dividend if it is in default of its assessments. As a result of the Dodd-Frank Act, deposit insurance per account owner is $250,000 for all types of accounts.

The Dodd-Frank Act increased the minimum target DIF ratio from 1.15% to 1.35% of estimated insured deposits. The FDIC was required to seek to achieve the 1.35% ratio by September 30, 2020, and insured institutions with assets of $10 billion or more were supposed to fund the increase. On September 30, 2018, the 1.35% ratio was exceeded, reaching 1.36%. Insured institutions of less than $10 billion of assets received credits for the portion of their assessments that contributed to raising the reserve ratio between 1.15% and 1.35% effective when the fund rate achieves 1.38%. The fund rate achieved 1.40% as of June 30, 2019, and the FDIC first applied small bank credits on the September 30, 2019 assessment invoice (for the second quarter of 2019). The FDIC remitted the final small bank credits in 2020 as the ratio remained above 1.35%. The Dodd-Frank Act eliminated the 1.5% maximum fund ratio, instead leaving it to the discretion of the FDIC to establish a maximum fund ratio. The FDIC has exercised that discretion by establishing a long range fund ratio of 2%.

The FDIC has authority to increase insurance assessments. A significant increase in insurance premiums would likely have an adverse effect on the operating expenses and results of operations of the Bank. Management cannot predict what insurance assessment rates will be in the future.

Insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or regulatory condition imposed in writing. The management of the Bank does not know of any practice, condition or violation that might lead to termination of deposit insurance.

FEDERAL RESERVE SYSTEM

Under FRB regulations, the Bank is required to maintain reserves against its transaction accounts (primarily NOW and regular checking accounts). These reserve requirements are subject to annual adjustment by the FRB. For 2021, the Bank would have been required to maintain average daily reserves equal to 3% on aggregate transaction accounts of up to and including $640.6 million, plus 10% on the remainder, and the first $32.4 million of otherwise reservable balances will be exempt. In March 2020, the FRB reduced all reserve requirements to zero in response to the COVID-19 pandemic.

PROHIBITIONS AGAINST TYING ARRANGEMENTS

State-chartered banks are prohibited, subject to some exceptions, from extending credit to or offering any other service, or fixing or varying the consideration for such extension of credit or service, on the condition that the customer obtain some additional service from the institution or its affiliates or not obtain services of a competitor of the institution.

OTHER REGULATIONS

Interest and other charges collected or contracted for by the Bank are subject to state usury laws and federal laws concerning interest rates. The Bank's operations are also subject to federal and state laws applicable to credit transactions, such as the:

- Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers;
- Home Mortgage Disclosure Act, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
- Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed or other prohibited factors in extending credit;
- Fair Credit Reporting Act, governing the use and provision of information to credit reporting agencies;
- Fair Debt Collection Act, governing the manner in which consumer debts may be collected by collection agencies;
- Truth in Savings Act; and
- Rules and regulations of the various federal and state agencies charged with the responsibility of implementing such laws.

The Bank's operations also are subject to the:

- Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records;
- Electronic Funds Transfer Act and Regulation E promulgated thereunder, which govern automatic deposits to and withdrawals from deposit accounts and customers' rights and liabilities arising from the use of automated teller machines and other electronic banking services;
- Check Clearing for the 21st Century Act (also known as "Check 21"), which gives "substitute checks," such as digital check images and copies made from that image, the same legal standing as the original paper check;
- The USA PATRIOT Act, which requires banks operating to, among other things, establish broadened anti-money laundering compliance programs, due diligence policies and controls to ensure the detection and reporting of money laundering. Such required compliance programs are intended to supplement existing compliance requirements, also applicable to financial institutions, under the Bank Secrecy Act and the Office of Foreign Assets Control regulations; and
- The Gramm-Leach-Bliley Act, which places limitations on the sharing of consumer financial information by financial institutions with unaffiliated third parties. Specifically, the Gramm-Leach-Bliley Act requires all financial institutions offering financial products or services to retail customers to provide such customers with the financial institution's privacy policy

and provide such customers the opportunity to "opt out" of the sharing of certain personal financial information with unaffiliated third parties.

HOLDING COMPANY REGULATION

The Company, as a bank holding company, is subject to examination, supervision, regulation, and periodic reporting under the BHCA, as administered by the FRB. The Company is required to obtain the prior approval of the FRB to acquire all, or substantially all, of the assets of any bank or bank holding company. Prior FRB approval is also required for the Company to acquire direct or indirect ownership or control of any voting securities of any bank or bank holding company if it would, directly or indirectly, own or control more than 5% of any class of voting shares of the bank or bank holding company.

A bank holding company is generally prohibited from engaging in, or acquiring, direct or indirect control of more than 5% of the voting securities of any company engaged in nonbanking activities. One of the principal exceptions to this prohibition is for activities found by the FRB to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Some of the principal activities that the FRB has determined by regulation to be closely related to banking are: (i) making or servicing loans; (ii) performing certain data processing services; (iii) providing securities brokerage services; (iv) acting as fiduciary, investment or financial advisor; (v) leasing personal or real property under certain conditions; (vi) making investments in corporations or projects designed primarily to promote community welfare; and (vii) acquiring a savings association.

A bank holding company that meets specified conditions, including that its depository institutions subsidiaries are "well capitalized" and "well managed," can opt to become a "financial holding company." A "financial holding company" may engage in a broader array of financial activities than permitted a typical bank holding company. Such activities can include insurance underwriting and investment banking. The Company does not anticipate opting for "financial holding company" status at this time.

The Company is exempt from the FRB's consolidated capital adequacy guidelines for bank holding companies because the Company's consolidated assets are less than $3.0 billion. The FRB consolidated capital adequacy guidelines are at least as stringent as those required for the subsidiary depository institutions.

A bank holding company is generally required to give the FRB prior written notice of any purchase or redemption of then outstanding equity securities if the gross consideration for the purchase or redemption, when combined with the net consideration paid for all such purchases or redemptions during the preceding 12 months, is equal to 10% or more of the Company's consolidated net worth. The FRB may disapprove such a purchase or redemption if it determines that the proposal would constitute an unsafe and unsound practice, or would violate any law, regulation, FRB order or directive, or any condition imposed by, or written agreement with, the FRB. The FRB has adopted an exception to that approval requirement for well-capitalized bank holding companies that meet certain other conditions.

The FRB has issued a policy statement regarding the payment of dividends by bank holding companies. In general, the FRB's policies provide that dividends should be paid only out of current earnings and only if the prospective rate of earnings retention by the bank holding company appears consistent with the organization's capital needs, asset quality and overall financial condition. The FRB's policies also require that a bank holding company serve as a source of financial strength to its subsidiary banks by using available resources to provide capital funds during periods of financial stress or adversity and by maintaining the financial flexibility and capital-raising capacity to obtain additional resources for assisting its subsidiary banks where necessary. The Dodd-Frank Act codified the source of strength policy and requires the promulgation of implementing regulations. Under the prompt corrective action laws, the ability of a bank holding company to pay dividends may be restricted if a subsidiary bank becomes undercapitalized. These regulatory policies could affect the ability of the Company to pay dividends or otherwise engage in capital distributions.

The Federal Deposit Insurance Act makes depository institutions liable to the Federal Deposit Insurance Corporation for losses suffered or anticipated by the insurance fund in connection with the default of a commonly controlled depository institution or any assistance provided by the Federal Deposit Insurance Corporation to such an institution in danger of default. That law would have potential applicability if the Company ever held as a separate subsidiary a depository institution in addition to the Bank.

The status of the Company as a registered bank holding company under the Bank Holding Company Act will not exempt it from certain federal and state laws and regulations applicable to corporations generally, including, without limitation, certain provisions of the federal securities laws.

ACQUISITION OF THE HOLDING COMPANY

Under the Change in Bank Control Act (the "CIBCA"), a federal statute, a notice must be submitted to the FRB if any person (including a company), or group acting in concert, seeks to acquire 10% or more of the Company's shares of outstanding common stock, unless the FRB has found that the acquisition will not result in a change in control of the Company. Under the CIBCA, the FRB generally has 60 days within which to act on such notices, taking into consideration certain factors, including the financial and managerial resources of the acquirer, the convenience and needs of the communities served by the Company and the Bank, and the anti-trust effects of the acquisition. Under the BHCA, any company would be required to obtain prior approval from the FRB before it may obtain "control" of the Company within the meaning of the BHCA. Control generally is defined to mean the ownership or power to vote 25% or more of any class of voting securities of the Company or the ability to control in any manner the election of a majority of the Company's directors. An existing bank holding company would be required to obtain the FRB's prior approval under the BHCA before acquiring more than 5% of the Company's voting stock.

EFFECT OF GOVERNMENT MONETARY POLICIES

The earnings and growth of the banking industry are affected by the credit policies of monetary authorities, including the Federal Reserve System. An important function of the Federal Reserve System is to regulate the national supply of bank credit in order to control recessionary and inflationary pressures. Among the instruments of monetary policy used by the Federal Reserve to implement these objectives are open market activities in U.S. government securities, changes in the discount rate on member bank borrowings and changes in reserve requirements against member bank deposits. These operations are used in varying combinations to influence overall economic growth and indirectly, bank loans, securities, and deposits. These variables may also affect interest rates charged on loans or paid on deposits. The monetary policies of the Federal Reserve authorities have had a significant effect on the operating results of commercial banks in the past and are expected to continue to have such an effect in the future.

In view of the changing conditions in the national economy and in the money markets, as well as the effect of actions by monetary and fiscal authorities including the Federal Reserve System, no prediction can be made as to possible changes in interest rates, deposit levels, loan demand or their effect on the business and earnings of the Company and the Bank. Additional information is included under the caption "*Management's Discussion and Analysis of Financial Condition and Results of Operations*" appearing in this Annual Report on Form 10-K.

ITEM 1A – RISK FACTORS.

The following discussion sets forth the material risk factors that could affect the Company's consolidated financial condition and results of operations. Readers should not consider any descriptions of these factors to be a complete set of all potential risks that could affect the Company. Any risk factor discussed below could by itself, or combined with other factors, materially and adversely affect the Company's business, results of operations, financial condition, capital position, liquidity, competitive position or reputation, including by materially increasing expenses or decreasing revenues, which could result in material losses or a decrease in earnings.

RISKS RELATED TO THE COVID-19 PANDEMIC

The COVID-19 pandemic has impacted our business and financial results and that of many of our customers, and the ultimate impact will depend on future developments, which are highly uncertain, cannot be predicted and outside of our control, including the scope and duration of the pandemic and actions taken by governmental authorities in response to the pandemic.

The COVID-19 pandemic has created extensive disruptions to the global economy and to the lives of individuals throughout the world. Governments, businesses, and the public are taking unprecedented actions to contain the spread of COVID-19 and to mitigate its effects, including quarantines, travel bans, shelter-in-place orders, closures of businesses and schools, fiscal and monetary stimulus, and legislation designed to deliver financial aid and other relief. While the scope, duration, and full effects of

COVID-19 are not fully known, the pandemic and the efforts to contain it have disrupted global economic activity, adversely affected the functioning of financial markets, impacted market interest rates, increased economic and market uncertainty, and disrupted trade and supply chains. If these effects continue for a significantly longer term and result in further economic stress or a return to a recession, the effects of COVID-19 could have a material adverse impact on us in a number of ways as described in more detail below.

Credit Risk – Our risks of timely loan repayment and the value of collateral supporting the loans are affected by the strength of our borrowers' businesses. Concern about the spread of COVID-19 has caused and is likely to continue to cause business shutdowns, limitations on commercial activity and financial transactions, labor shortages, supply chain interruptions, increased unemployment and commercial property vacancy rates, reduced profitability and ability for property owners to make mortgage payments, and overall economic and financial market instability, all of which may cause our customers to be unable to make scheduled loan payments. Hotel and restaurant operators and others in the leisure, hospitality and travel industries and the agricultural industry, among other industries, have been particularly hurt by COVID-19. If the effects of COVID-19 result in widespread and sustained repayment shortfalls on loans in our portfolio, we could incur significant delinquencies, foreclosures and credit losses, particularly if the available collateral is insufficient to cover our credit exposure. The future effects of COVID-19 on economic activity could negatively affect the collateral values associated with our existing loans, the ability to liquidate the real estate collateral securing our residential and commercial real estate loans, our ability to maintain loan origination volume and to obtain additional financing, the future demand for or profitability of our lending and services, and the financial condition and credit risk of our customers. Further, in the event of delinquencies, regulatory changes and policies designed to protect borrowers may slow or prevent us from making our business decisions or may result in a delay in our taking certain remediation actions, such as foreclosure. In addition, we have unfunded commitments to extend credit to customers. During a challenging economic environment like now, our customers depend more on our credit commitments and increased borrowings under these commitments could adversely impact our liquidity. Furthermore, in an effort to support our communities during the pandemic, we participated in the Paycheck Protection Program under the CARES Act whereby loans to small businesses were made and those loans were subject to the regulatory requirements that would require forbearance of loan payments for a specified time or that would limit our ability to pursue all available remedies in the event of a loan default. If the borrower under the PPP loan fails to qualify for loan forgiveness, we are at the heightened risk of holding these loans at unfavorable interest rates as compared to the loans to customers that we would have otherwise extended credit.

Strategic Risk – Our success may be affected by a variety of external factors that may affect the price or marketability of our products and services, changes in interest rates that may increase our funding costs, reduced demand for our financial products due to economic conditions and the various response of governmental and nongovernmental authorities. The COVID-19 pandemic has significantly increased economic and demand uncertainty and has led to disruption and volatility in the global capital markets. Furthermore, governmental actions have been directed toward curtailing household and business activity to contain COVID-19. The future effects of COVID-19 on economic activity could negatively affect the future banking products we provide, including a decline in originating loans.

Operational Risk – Current and future restrictions on our workforce's access to our facilities could limit our ability to meet customer servicing expectations and have a material adverse effect on our operations. We rely on business processes and branch activity that largely depend on people and technology, including access to information technology systems as well as information, applications, payment systems and other services provided by third parties. In response to COVID-19, at times, we have modified our business practices with a portion of our employees working remotely from their homes to have our operations uninterrupted as much as possible. Further, technology in employees' homes may not be as robust as in our offices and could cause the networks, information systems, applications, and other tools available to employees to be more limited or less reliable than in our offices. The continuation of these work-from-home measures also introduces additional operational risk, including increased cybersecurity risk from phishing, malware, and other cybersecurity attacks, all of which could expose us to risks of data or financial loss and could seriously disrupt our operations and the operations of any impacted customers.

Moreover, we rely on many third parties in our business operations, including the appraisal of the real property collateral, vendors that supply essential services such as loan servicers, providers of financial information, systems and analytical tools and providers of electronic payment and settlement systems, and local and federal government agencies, offices, and courthouses. In light of the developing measures responding to the pandemic, many of these entities may limit the availability and access of their services. If the third-party service providers continue to have limited capacities for a prolonged period or if additional limitations or potential disruptions in these services materialize, it may negatively affect our operations.

Interest Rate Risk/Market Value Risk – Our net interest income, lending and investment activities, deposits and profitability could be negatively affected by volatility in interest rates caused by uncertainties stemming from COVID-19. In March 2020, the Federal Reserve lowered the target range for the federal funds rate to a range from 0% to 0.25%, citing concerns about the impact of COVID-19 on financial markets and market stress in the energy sector. A prolonged period of extremely volatile and unstable market conditions would likely increase our funding costs and negatively affect market risk mitigation strategies. Higher income volatility from changes in interest rates and spreads to benchmark indices could cause a loss of future net interest income and a decrease in prevailing fair market values of our investment securities and other assets. Fluctuations in interest rates will impact both the level of income and expense recorded on most of our assets and liabilities and the market value of all interest-earning assets and interest-bearing liabilities, which in turn could have a material adverse effect on our net income, operating results, or financial condition.

Because there have been no comparable recent global pandemics that resulted in similar global impact, we do not yet know the full extent of COVID-19's effects on our business, operations, or the global economy as a whole. Any future development will be highly uncertain and cannot be predicted, including the scope and duration of the pandemic, the effectiveness of our work-from-home arrangements, third party providers' ability to support our operations, and any actions taken by governmental authorities and other third parties in response to the pandemic. The uncertain future development of this crisis could materially and adversely affect our business, operations, operating results, financial condition, liquidity or capital levels.

RISKS RELATED TO CHANGES IN MARKET INTEREST RATES

Changing interest rates may decrease our earnings and asset values.

Our net interest income is the interest we earn on loans and investments less the interest we pay on our deposits and borrowings. Our net interest margin is the difference between the yield we earn on our assets and the interest rate we pay for deposits and our other sources of funding. Changes in interest rates—up or down—could adversely affect our net interest margin and, as a result, our net interest income. Although the yield we earn on our assets and our funding costs tend to move in the same direction in response to changes in interest rates, one can rise or fall faster than the other, causing our net interest margin to expand or contract. Our liabilities tend to be shorter in duration than our assets, so they may adjust faster in response to changes in interest rates. As a result, when interest rates rise, our funding costs may rise faster than the yield we earn on our assets, causing our net interest margin to contract until the asset yields catch up. Changes in the slope of the "yield curve"—or the spread between short-term and long-term interest rates—could also reduce our net interest margin. Normally, the yield curve is upward sloping, meaning short-term rates are lower than long-term rates. Because our liabilities tend to be shorter in duration than our assets, when the yield curve flattens or even inverts, we could experience pressure on our net interest margin as our cost of funds increases relative to the yield we can earn on our assets.

Changes in interest rates also affect the value of the Bank's interest-earning assets, and in particular the Bank's securities portfolio. Generally, the value of fixed-rate securities fluctuates inversely with changes in interest rates. Unrealized gains and losses on securities available for sale are reported as a separate component of shareholder equity, net of tax, while unrealized gains and losses on equity securities directly impact earnings. Decreases in the fair value of securities available for sale resulting from increases in interest rates could have an adverse effect on shareholders' equity or net income.

Impact of Inflation

The effects of price changes and inflation can vary substantially for most financial institutions. While management believes that inflation affects the growth of total assets, it believes that it is difficult to assess the overall impact. Management believes this to be the case due to the fact that generally neither the timing nor the magnitude of the inflationary changes in the CPI coincides with changes in interest rates. The price of one or more of the components of the CPI may fluctuate considerably and thereby influence the overall CPI without having a corresponding effect on interest rates or upon the cost of those goods and services normally purchased by us. In years of high inflation and high interest rates, intermediate and long-term interest rates tend to increase, thereby adversely impacting the market values of investment securities, mortgage loans and other long-term fixed rate loans. In addition, higher short-term interest rates caused by inflation tend to increase the cost of funds. In other years, the opposite may occur.

RISKS RELATED TO OUR LENDING ACTIVITIES

Activities related to the drilling for natural gas in the in the Marcellus and Utica Shale formations impacts certain customers of the Bank.

Our north central Pennsylvania market area is predominately centered in the Marcellus and Utica Shale natural gas exploration and drilling area, and as a result, the economy in north central Pennsylvania is influenced by the natural gas industry. Loan demand, deposit levels and the market value of local real estate are impacted by this activity. While the Company does not lend to the various entities directly engaged in exploration, drilling or production activities, many of our customers provide transportation and other services and products that support natural gas exploration and production activities. Therefore, our customers are impacted by changes in the market price for natural gas, as a significant downturn in this industry could impact the ability of our borrowers to repay their loans in accordance with their terms. Additionally, exploration and drilling activities may be affected by federal, state and local laws and regulations such as restrictions on production, permitting, changes in taxes and environmental protection. Regulatory and market pricing of natural gas could also impact and/or reduce demand for loans and deposit levels or loan collateral values. These factors could have a material adverse effect on our business, prospects, financial condition and results of operations.

Higher loan losses could require us to increase our allowance for loan losses through a charge to earnings.

When we loan money, we incur the risk that our borrowers do not repay their loans. We reserve for loan losses by establishing an allowance through a charge to earnings. The amount of this allowance is based on our assessment of loan losses inherent in our loan portfolio. The process for determining the amount of the allowance is critical to our financial results and condition. It requires subjective and complex judgments about the future, including forecasts of economic or market conditions that might impair the ability of our borrowers to repay their loans. We might underestimate the loan losses inherent in our loan portfolio and have loan losses in excess of the amount reserved. We might increase the allowance because of changing economic conditions. For example, in a rising interest rate environment, borrowers with adjustable-rate loans could see their payments increase. There may be a significant increase in the number of borrowers who are unable or unwilling to repay their loans, resulting in our charging off more loans and increasing our allowance. In addition, when real estate values decline, the potential severity of loss on a real estate-secured loan can increase significantly, especially in the case of loans with high combined loan-to-value ratios. A decline in the national economy and the local economies of the areas in which the loans are concentrated could result in an increase in loan delinquencies, foreclosures or repossessions resulting in increased charge-off amounts and the need for additional loan loss allowances in future periods. In addition, bank regulators may require us to make a provision for loan losses or otherwise recognize further loan charge-offs following their periodic review of our loan portfolio, our underwriting procedures, and our loan loss allowance. Any increase in our allowance for loan losses or loan charge-offs as required by such regulatory authorities could have a material adverse effect on our financial condition and results of operations.

Our allowance for loan losses amounted to $17.3 million, or 1.20% of total loans outstanding and 225.8% of nonperforming loans, at December 31, 2021. Our allowance for loan losses at December 31, 2021 may not be sufficient to cover future loan losses. A large loss could deplete the allowance and require increased provisions to replenish the allowance, which would decrease our earnings. In addition, at December 31, 2021 the top 40 relationships of the Bank had an outstanding balance of $393.8 million. These loans represent approximately 27.3% of our entire outstanding loan portfolio as of December 31, 2021 and the deterioration of one or more of these loans could result in a significant increase in our nonperforming loans and our provision for loan losses, which would negatively impact our results of operations.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments - Credit Losses: Measurement of Credit Losses on Financial Instruments*, which changes the impairment model for most financial assets. The underlying premise of the Update is that financial assets measured at amortized cost should be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. The allowance for credit losses should reflect management's current estimate of credit losses that are expected to occur over the remaining life of a financial asset. The income statement will be affected for the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. On October 16, 2019, the FASB voted to defer the effective date for ASC 326, *Financial Instruments – Credit Losses*, for smaller reporting companies to fiscal years beginning after December 15, 2022, and interim periods within those fiscal years. The implementation of this standard may result in significant changes to the balance in the allowance for loan losses and may result in significant costs being expended to implement.

Our emphasis on commercial real estate, agricultural real estate, construction and municipal lending may expose us to increased lending risks.

At December 31, 2021, we had $687.3 million in loans secured by commercial real estate, $312.0 million in agricultural real estate loans, $55.0 million in construction loans and $45.8 million in municipal loans. Commercial real estate loans, agricultural real estate, construction and municipal loans represented 47.7%, 21.6%, 3.8% and 3.1%, respectively, of our loan portfolio. At December 31, 2021, we had $13.5 million of reserves specifically allocated to these loan types. While commercial real estate, agricultural real estate, construction and municipal loans are generally more interest rate sensitive and carry higher yields than do residential mortgage loans, these types of loans generally expose a lender to greater risk of non-payment and loss than single-family residential mortgage loans because repayment of the loans often depends on the successful operation of the property, the income stream of the borrowers and, for construction loans, the accuracy of the estimate of the property's value at completion of construction and the estimated cost of construction. Such loans typically involve larger loan balances to single borrowers or groups of related borrowers compared to single-family residential mortgage loans. We monitor loan concentrations on an individual relationship and industry wide basis to monitor the amount of risk we have in our loan portfolio.

Agricultural loans are dependent for repayment on the successful operation and management of the farm property, the health of the agricultural industry broadly, and on the location of the borrower in particular, and other factors outside of the borrower's control.

At December 31, 2021, our agricultural loans, consisting primarily of agricultural real estate loans and other agricultural loans totaled $351.9 million, representing 24.4% of our total loan portfolio. The primary activities of our agricultural customers include dairy and beef farms, poultry and swine operations, crops and support businesses. Agricultural markets are highly sensitive to real and perceived changes in the supply and demand of agricultural products. Weaker prices could reduce the value of agricultural land in our local markets and thereby increase the risk of default by our borrowers or reduce the foreclosure value of agricultural land, animals and equipment that serves as collateral for certain of our loans. At December 31, 2021, the Company had a loan concentration to the dairy industry totaling $127,392,000, or 8.8% of total loans and 36.2% of total agricultural loans compared to 9.90% of total loans and 38.2% of total agricultural loans at December 31, 2020.

Our agricultural loans are dependent on the profitable operation and management of the farm property securing the loan and its cash flows. The success of a farm property may be affected by many factors outside the control of the borrower, including:

- The COVID-19 pandemic and its impact to supply and demand constraints
- adverse weather conditions (such as hail, drought and floods), restrictions on water supply or other conditions that prevent the planting or harvesting of a crop or limit crop yields;
- loss of crops or livestock due to disease or other factors;
- declines in the market prices or demand for agricultural products (both domestically and internationally), for any reason;
- increases in production costs (such as the costs of labor, rent, feed, fuel and fertilizer);
- the impact of domestic and international government policies and regulations (including changes in price supports, subsidies, government-sponsored crop insurance, minimum ethanol content requirements for gasoline, tariffs, trade barriers, trade agreements and health and environmental regulations);
- access to technology and the successful implementation of production technologies; and

- changes in the general economy that could affect the availability of off-farm sources of income and prices of real estate for borrowers.
- Disruptions in the supply chain and the processing of product and delivery to the final retail channel

Lower prices for agricultural products may cause farm revenues to decline and farm operators may be unable to reduce expenses as quickly as their revenues decline. In addition, many farms are dependent on a limited number of key individuals whose injury or death could significantly affect the successful operation of the farm. If the cash flow from a farming operation is diminished, the borrower's ability to repay the loan may be impaired. Consequently, agricultural loans may involve a greater degree of risk than residential mortgage lending, particularly in the case of loans that are unsecured or secured by rapidly depreciating assets such as farm equipment (some of which is highly specialized with a limited or no market for resale) or perishable assets such as livestock or crops. In such cases, any repossessed collateral for a defaulted agricultural operating loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation or because the assessed value of the collateral exceeds the eventual realization value.

Loan participations comprise a portion of our loan portfolio and a decline in loan participation volume could hurt profits and slow loan growth.

We have actively engaged in loan participations whereby we are invited to participate in loans, primarily commercial real estate and municipal loans, originated by another financial institution known as the lead lender. We have participated with other financial institutions in both our primary markets and out of market areas. We underwrite any loan we participate in as if we are originating the loan. The primary difference is that financial information is received from the participating financial institution and not the borrower. The loans we participate in totaled $58.3 million and $63.3 million at December 31, 2021 and 2020, respectively. As a percent of total loans, participation purchased loans were 4.0%, 4.5% and 5.6% as of December 31, 2021, 2020 and 2019. Our profits and loan growth could be significantly and adversely affected if the volume of loan participations would materially decrease, whether because loan demand declines, loan payoffs, lead lenders may come to perceive us as a potential competitor in their respective market areas, or otherwise.

Environmental liability associated with lending activities could result in losses.

In the course of our business, we may foreclose on and take title to properties securing our loans. If hazardous substances were discovered on any of these properties, we could be liable to governmental entities or third parties for the costs of remediation of the hazard, as well as for personal injury and property damage. Many environmental laws can impose liability regardless of whether we knew of, or were responsible for, the contamination. In addition, if we arrange for the disposal of hazardous or toxic substances at another site, we may be liable for the costs of cleaning up and removing those substances from the site even if we neither own nor operate the disposal site. Environmental laws may require us to incur substantial expenses and may materially limit use of properties we acquire through foreclosure, reduce their value or limit our ability to sell them in the event of a default on the loans they secure. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability.

RISKS RELATED TO OUR INVESTMENT SECURITIES

If we conclude that the decline in value of any of our investment securities is other than temporary, we are required to write down the value of that security through a charge to earnings.

We review our investment securities portfolio monthly and at each quarter-end reporting period to determine whether the fair value is below the current carrying value. When the fair value of any of our investment securities has declined below its carrying value, we are required to assess whether the decline is other than temporary. If we conclude that the decline is other than temporary, we are required to write down the value of that security through a charge to earnings. As of December 31, 2021, our investment portfolio included available for sale investment securities with an amortized cost of $412.0 million and a fair value of $412.4 million, which included unrealized losses on 138 securities totaling $3,997,000. Changes in the expected cash flows of these securities and/or prolonged price declines may result in our concluding in future periods that the impairment of these securities is other than temporary, which would require a charge to earnings to write down these securities to their fair value. Any charges for other-than-temporary impairment would not impact cash flow, tangible capital or liquidity.

RISKS RELATED TO OUR SECONDARY MORTGAGE OPERATIONS

Income from secondary mortgage market operations is volatile, and we may incur losses or charges with respect to our secondary mortgage market operations which would negatively affect our earnings.

We generally sell in the secondary market the longer term fixed-rate residential mortgage loans that we originate, earning non-interest income in the form of gains on sale. When interest rates rise, the demand for mortgage loans tends to fall and may reduce the number of loans available for sale. In addition to interest rate levels, weak or deteriorating economic conditions also tend to reduce loan demand. Although we sell loans in the secondary market without recourse, we are required to give customary representations and warranties to the buyers. If we breach those representations and warranties, the buyers can require us to repurchase the loans and we may incur a loss on the repurchase. Because we generally retain the servicing rights on the loans we sell in the secondary market, we are required to record a mortgage servicing right asset, which we test annually for impairment. The value of mortgage servicing rights tends to increase with rising interest rates, which occurred in 2021, and to decrease with falling interest rates, with activity increasing in falling rate environments. If we are required to take an impairment charge on our mortgage servicing rights our earnings would be adversely affected.

As a result of the acquisition in 2015, the Bank acquired a portfolio of loans sold to the FHLB, which were sold under the Mortgage Partnership Finance Program ("MPF"). While the Bank was not an active participant in the MPF program in 2021, we continue to evaluate the program to see if it would be beneficial to our customers and our performance. The MPF portfolio balance was $12,140,000 at December 31, 2021. The FHLB maintains a first-loss position for the MPF portfolio that totals $157,000. Should the FHLB exhaust its first-loss position, recourse to the Bank's credit enhancement would be up to the next $590,000 of losses. The Bank has not experienced any losses for the MPF portfolio.

RISKS RELATED TO OUR MARKET AREA

The Company's financial condition and results of operations are dependent on the economy in the Bank's market area.

The Bank's primary market area consists of the Pennsylvania Counties of Bradford, Clinton, Potter, and Tioga in north central Pennsylvania, Lebanon, Schuylkill, Berks and Lancaster in south central, Pennsylvania, Centre and Clinton in central Pennsylvania, and Allegany, Steuben, Chemung and Tioga Counties in southern New York. With the acquisition of MidCoast, we consider the cities and surrounding areas of Wilmington and Dover, Delaware, as well as Kennett Square, Pennsylvania in Chester County, as primary market areas. The majority of the Bank's loan and deposits come from households and businesses whose primary address is located in the Bank's primary market areas. Because of the Bank's concentration of business activities in its market area, the Company's financial condition and results of operations depend upon economic conditions in its market areas. Adverse economic conditions in our market areas could reduce our growth rate, affect the ability of our customers to repay their loans and generally affect our financial condition and results of operations. Conditions such as inflation, recession, unemployment, high interest rates and short money supply and other factors beyond our control may adversely affect our profitability. We are less able than a larger institution to spread the risks of unfavorable local economic conditions across a large number of diversified economies. Any sustained period of increased payment delinquencies, foreclosures or losses caused by adverse market or economic conditions in the States of Pennsylvania, New York and Delaware could adversely affect the value of our assets, revenues, results of operations and financial condition. Moreover, we cannot give any assurance we will benefit from any market growth or favorable economic conditions in our primary market areas if they do occur.

RISKS RELATED TO LAWS AND REGULATIONS

Regulation of the financial services industry is significant, and future legislation could increase our cost of doing business or harm our competitive position.

We are subject to extensive regulation, supervision and examination by the FRB and the PDB, our primary regulators, and by the FDIC, as insurer of our deposits. Such regulation and supervision governs the activities in which an institution and its holding company may engage and are intended primarily for the protection of the insurance fund and the depositors and borrowers of the Bank rather than for holders of our common stock. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on our operations, the classification of our assets and determination of the level of our allowance for loan losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, legislation or supervisory action, may have a material impact on our profitability and operations. Future legislative changes could require changes to business practices or force us to discontinue businesses and potentially expose us to additional costs, liabilities, enforcement action and reputational risk.

Our ability to pay dividends is limited by law.

Our ability to pay dividends to our shareholders largely depends on our receipt of dividends from the Bank. The amount of dividends that the Bank may pay to us is limited by federal and state laws and regulations. We also may decide to limit the payment of dividends even when we have the legal ability to pay them in order to retain earnings for use in our business.

Federal and state banking laws, our articles of incorporation and our by-laws may have an anti-takeover effect.

Federal law imposes restrictions, including regulatory approval requirements, on persons seeking to acquire control over us. Pennsylvania law also has provisions that may have an anti-takeover effect. These provisions may serve to entrench management or discourage a takeover attempt that shareholders consider to be in their best interest or in which they would receive a substantial premium over the current market price.

RISKS RELATED TO COMPETITION

Strong competition within the Bank's market areas could hurt profits and slow growth.

The Bank faces intense competition both in making loans and attracting deposits. This competition has made it more difficult for the Bank to make new loans and at times has forced the Bank to offer higher deposit rates. Price competition for loans and deposits might result in the Bank earning less on loans and paying more on deposits, which would reduce net interest income. Competition also makes it more difficult to increase the volume of our loan and deposit portfolios. As of June 30, 2021, which is the most recent date for which information is available, we held 34.2% of the FDIC insured deposits in Bradford, Potter and Tioga Counties, Pennsylvania, which was the second largest share of deposits out of eight financial institutions with offices in the area, and 6.0% of the FDIC insured deposits in Allegany County, New York, which was the third largest share of deposits out of three financial institutions with offices in this area. As of June 30, 2021, we held 7.6% of the FDIC insured deposits in Lebanon County, Pennsylvania, which was the fourth largest share out of the 14 financial institutions with offices in the County. As of June 30, 2021, we held 3.6% of the FDIC insured deposits in Clinton County, Pennsylvania, which was the eighth largest share out of the eight financial institutions with offices in the County. Our offices in Berks, Centre, Chester, Lancaster and Schuylkill Counties of Pennsylvania and our offices in Wilmington and Dover, Delaware all have less than 3% of the FDIC insured deposits of the corresponding County as of June 30, 2021. This data does not include deposits held by credit unions. Competition also makes it more difficult to hire employees and more expensive to retain experienced employees. Some of the institutions with which the Bank competes have substantially greater resources and lending limits than the Bank has and may offer services that the Bank does not provide. Management expects competition to increase in the future as a result of legislative, regulatory and technological changes (fintech) and the continuing trend of consolidation in the financial services industry. The Bank's profitability depends upon its continued ability to compete successfully in its market area.

RISKS RELATED TO OUR OPERATIONS

We rely on our management and other key personnel, and the loss of any of them may adversely affect our operations.

We are and will continue to be dependent upon the services of our executive management team. In addition, we will continue to depend on our ability to retain and recruit key commercial and agricultural loan officers. The unexpected loss of services of any key management personnel or commercial and agricultural loan officers could have an adverse effect on our business and financial condition because of their skills, knowledge of our market, years of industry experience and the difficulty of promptly finding qualified replacement personnel.

We are periodically subject to examination and scrutiny by a number of banking agencies and, depending upon the findings and determinations of these agencies, we may be required to make adjustments to our business that could adversely affect us.

Federal and state banking agencies periodically conduct examinations of our business, including compliance with applicable laws and regulations. If, as a result of an examination, a banking agency was to determine that the financial condition, capital resources, asset quality, asset concentration, earnings prospects, management, liquidity, sensitivity to market risk or other aspects of any of our operations has become unsatisfactory, or that we or our management is in violation of any law or regulation, it could take a number of different remedial actions as it deems appropriate. These actions include the power to enjoin “unsafe or unsound” practices, to require affirmative actions to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in our capital, to restrict our growth, to change the composition of our assets or liabilities, to assess civil monetary penalties against us and/or our officers or directors, to remove officers and directors and, if it is concluded that such conditions cannot be corrected or there is an imminent risk of loss to depositors, to terminate our deposit insurance. If we become subject to such regulatory actions, our business, results of operations and reputation may be negatively impacted.

We are subject to certain risks in connection with our use of technology.

Communications and information systems are essential to the conduct of our business, as we use such systems to manage our customer relationships, our general ledger, our deposits, our loans, and to deliver on-line and electronic banking services. Our operations rely on the secure processing, storage, and transmission of confidential and other information in our computer systems and networks. Although we take protective measures and endeavor to modify them as circumstances warrant, the security of our computer systems, software, and networks may be vulnerable to breaches, unauthorized access, misuse, computer viruses, or other malicious code and cyber attacks that could have a security impact.

In addition, breaches of security may occur through intentional or unintentional acts by those having authorized or unauthorized access to our confidential or other information or the confidential or other information of our customers, clients, or counterparties. If one or more of such events were to occur, the confidential and other information processed and stored in, and transmitted through, our computer systems and networks could potentially be jeopardized, or could otherwise cause interruptions or malfunctions in our operations or the operations of our customers, clients, or counterparties. This could cause us significant reputational damage or result in our experiencing significant losses from fraud or otherwise.

Furthermore, we may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures arising from operational and security risks. Also, we may be subject to litigation and financial losses that are either not insured against or not fully covered through any insurance we maintain.

We routinely transmit and receive personal, confidential, and proprietary information by e-mail and other electronic means. We have discussed and worked with our customers, clients, and counterparties to develop secure transmission capabilities, but we do not have, and may be unable to put in place, secure capabilities with all of these constituents, and we may not be able to ensure that these third parties have appropriate controls in place to protect the confidentiality of such information. Any interception, misuse, or mishandling of personal, confidential, or proprietary information being sent to or received from a customer, client, or counterparty could result in legal liability, regulatory action, and reputational harm, and could have a significant adverse effect on our competitive position, financial condition, and results of operations.

Our risk management framework may not be effective in mitigating risks and/or losses to us.

We have implemented a risk management framework to manage our risk exposure. This framework is comprised of various processes, systems and strategies, and is designed to manage the types of risk to which we are subject, including, among others, credit, market, liquidity, interest rate and compliance. Our framework also includes financial or other modeling methodologies which involve management assumptions and judgment. There is no assurance that our risk management framework will be effective under all circumstances or that it will adequately mitigate any risk or loss to us. If our framework is not effective, we could suffer unexpected losses and our business, financial condition, results of operations or prospects could be materially and adversely affected. We may also be subject to potentially adverse regulatory consequences.

RISKS RELATED TO LIBOR

Changes in the method pursuant to which benchmark rates, including LIBOR, are calculated and their potential discontinuance could adversely impact our business operations and financial results.

Many of our lending products, securities and derivatives utilize a benchmark rate to determine the applicable interest rate or payment amount. As the Company has grown and developed relationships with larger and more sophisticated borrowers, the benchmarks utilized by the Company have changed with an increased usage of LIBOR. In July 2017, the Chief Executive of the U.K. Financial Conduct Authority (“FCA”) announced that the FCA intends to stop persuading or compelling banks to submit rates for the calculation of LIBOR after 2021. This announcement indicates that the continuation of LIBOR cannot and will not be guaranteed after 2021. Instruments associated with LIBOR have been identified by the Company, and transition procedures to a revised benchmark are being developed.

The discontinuation of a benchmark rate, changes in a benchmark rate, or changes in market perceptions of the acceptability of a benchmark rate, including LIBOR, could, among other things, adversely affect the value of and return on certain of our financial instruments or products, result in changes to our risk exposures, or require renegotiation of previous transactions. In addition, any such discontinuation or changes, whether actual or anticipated, could result in market volatility, adverse tax or accounting effects, increased compliance, legal and operational costs, and risks associated with customer disclosures and contract negotiations. The transition to using a new rate could also expose us to risks associated with disputes with customers and other market participants in connection with interpreting and implementing fallback provisions.

Various regulators, industry bodies and other market participants in the U.S. are engaged in initiatives to develop, introduce and encourage the use of alternative rates to replace certain benchmarks. Despite progress made to date by regulators and industry participants, such as us, to prepare for the anticipated discontinuation of LIBOR, significant uncertainties still remain. Such uncertainties relate to, for example, whether replacement benchmark rates may become accepted alternatives to LIBOR for different types of transactions and financial instruments, how the terms of any transaction or financial instrument may be adjusted to account for differences between LIBOR and any alternative rate selected, how any replacement would be implemented across the industry, and the effect any changes in industry views or movement to alternative benchmarks would have on the markets for LIBOR-linked financial instruments.

RISKS RELATED TO OUR MERGER AND ACQUISITION ACTIVITY

Impairment of goodwill could require charges to earnings, which could result in a negative impact on our results of operations.

Our goodwill could become impaired in the future. If goodwill were to become impaired, it could limit the ability of the Bank to pay dividends to the Company, adversely impacting the Company’s liquidity and ability to pay dividends. The most significant assumptions affecting our goodwill impairment evaluation are variables including the market price of our Common Stock, projections of earnings, and the control premium above our current stock price that an acquirer would pay to obtain control of us. We are required to test goodwill for impairment at least annually or when impairment indicators are present. If an impairment determination is made in a future reporting period, our earnings and book value of goodwill will be reduced by the amount of the impairment. If an impairment loss is recorded, it will have little or no impact on the tangible book value of our Common Stock, or our regulatory capital levels, but such an impairment loss could significantly reduce the Bank’s earnings and thereby restrict the Bank's ability to make dividend payments to us without prior regulatory approval, because Federal Reserve policy states the bank holding company dividends should be paid from current earnings. At December 31, 2021, the book value of our goodwill was $31.4 million, all of which was recorded at the Bank.

We may fail to realize all of the anticipated benefits of entering new markets.

As a result of completed and proposed acquisitions and the hiring of additional agricultural and commercial lending teams, the Company enters new banking market areas. The success of entering these new markets depends upon, in part, the Company’s ability to realize the anticipated benefits and cost savings from combining the businesses of the Company and the acquisition, as well as organically growing loans and deposits. To realize these anticipated benefits and cost savings, the businesses and individuals must be successfully combined and operated. If the Company is not able to achieve these objectives, the anticipated benefits, including growth and cost savings related to the combined businesses, may not be realized at all or may take longer to realize than expected. If the Company fails to realize the anticipated benefits of the acquisitions and the new employee hiring's, the Company's results of operations could be adversely affected.

ITEM 1B – UNRESOLVED STAFF COMMENTS.

Not applicable.

ITEM 2 – PROPERTIES.

The headquarters of the Company and Bank are located at 15 South Main Street, Mansfield, Pennsylvania. The building contains the central offices of the Company and Bank. Our bank owns twenty three banking facilities and leases eleven other facilities.

The net book value of owned banking facilities and leasehold improvements totaled $16,323,000 as of December 31, 2021. The properties are adequate to meet the needs of the employees and customers. We have equipped all of our facilities with current technological improvements for data processing.

ITEM 3 - LEGAL PROCEEDINGS.

The Company is not involved in any pending legal proceedings other than routine legal proceedings occurring in the ordinary course of business. Such routine legal proceedings in the aggregate are believed by management to be immaterial to the Company's consolidated financial condition or results of operations.

ITEM 4 – MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5 - MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

The Company's stock is not listed on any stock exchange, but it is quoted on the OTC Pink Market under the trading symbol CZFS. Prices presented in the table below are bid prices between broker-dealers published by the OTC Pink Market and the Pink Sheets Electronic Quotation Service. The prices do not include retail markups or markdowns or any commission to the broker-dealer. The bid prices do not necessarily reflect prices in actual transactions. For 2021 and 2020, cash dividends were declared on a quarterly basis and are summarized in the table below:

	2021		**Dividends declared**	2020		Dividends declared
	High	**Low**	**per share**	High	Low	per share
First quarter	**$ 58.42**	**$ 53.96**	**$ 0.465**	$ 64.85	$ 37.62	$ 0.555
Second quarter	**62.50**	**58.42**	**0.465**	56.47	48.66	0.455
Third quarter	**64.00**	**61.10**	**0.470**	49.56	43.25	0.460
Fourth quarter	**61.50**	**59.00**	**0.470**	55.00	43.00	0.460

The Company has paid dividends since April 30, 1984, the effective date of our formation as a bank holding company. The Company's Board of Directors expects that comparable cash dividends will continue to be paid by the Company in the future; however, future dividends necessarily depend upon earnings, financial condition, appropriate legal restrictions and other factors in existence at the time the Board of Directors considers a dividend distribution. Cash available for dividend distributions to stockholders of the Company comes primarily from dividends paid to the Company by the Bank. Therefore, restrictions on the ability of the Bank to make dividend payments are directly applicable to the Company. Under the Pennsylvania Business Corporation Law of 1988, the Company may pay dividends only if, after payment, the Company would be able to pay debts as they become due in the usual course of our business and total assets will be greater than the sum of total liabilities. These regulatory policies could affect the ability of the Company to pay dividends or otherwise engage in capital distributions. Also see

"Supervision and Regulation – Regulatory Restrictions on Bank Dividends," "Supervision and Regulation – Holding Company Regulation," and "Note 15 – Regulatory Matters" to the consolidated financial statements.

As of March 1, 2022, the Company had 1,876 stockholders of record. The computation of stockholders of record excludes investors whose shares were held for them by a bank or broker at that date. The following table presents information regarding the Company's stock repurchases during the three months ended December 31, 2021:

Period	Total Number of Shares (or units Purchased)	Average Price Paid per Share (or Unit)	Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans of Programs	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs (1)
10/1/21 to 10/31/21	-	$0.00	-	**142,986**
11/1/21 to 11/30/21	2,634	$61.43	2,634	**140,352**
12/1/21 to 12/31/21	5,263	$60.46	5,263	**135,089**
Total	**7,897**	**$60.78**	**7,897**	**135,089**

(1) On April 21, 2020, the Company announced that the Board of Directors authorized the Company to repurchase up to an additional 150,000 shares at an aggregate purchase price not to exceed $12.0 million over a period of 36 months. The repurchases will be conducted through open-market purchases or privately negotiated transactions and will be made from time to time depending on market conditions and other factors. No time limit was placed on the duration of the share repurchase program. Any repurchased shares will be held as treasury stock and will be available for general corporate purposes.

ITEM 6 – [RESERVED]

ITEM 7 – MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

CAUTIONARY STATEMENT

We have made forward-looking statements in this document, and in documents that we incorporate by reference, that are subject to risks and uncertainties. Forward-looking statements include information concerning possible or assumed future results of operations of the Company, the Bank, First Citizens Insurance, Realty or the Company on a consolidated basis. When we use words such as "believes," "expects," "anticipates," or similar expressions, we are making forward-looking statements. Forward-looking statements may prove inaccurate. For a variety of reasons, actual results could differ materially from those contained in or implied by forward-looking statements:

- The scope, duration and severity of the COVID-19 pandemic and may have an adverse effect on our business and operations, our customers, including their ability to make timely loan payments, our service providers, and on the economy and financial markets more significant that we expect.
- Interest rates could change more rapidly or more significantly than we expect.
- The economy could change significantly in an unexpected way, which would cause the demand for new loans and the ability of borrowers to repay outstanding loans to change in ways that our models do not anticipate.
- The financial markets could suffer a significant disruption, which may have a negative effect on our financial condition and that of our borrowers, and on our ability to raise money by issuing new securities.
- It could take us longer than we anticipate implementing strategic initiatives, including expansions, designed to increase revenues or manage expenses, or we may be unable to implement those initiatives at all.
- Acquisitions and dispositions of assets could affect us in ways that management has not anticipated.
- We may become subject to new legal obligations or the resolution of litigation may have a negative effect on our financial condition or operating results.
- We may become subject to new and unanticipated accounting, tax, regulatory or compliance practices or requirements. Failure to comply with any one or more of these requirements could have an adverse effect on our operations.
- We could experience greater loan delinquencies than anticipated, adversely affecting our earnings and financial condition.
- We could experience greater losses than expected due to the ever increasing volume of information theft and fraudulent scams impacting our customers and the banking industry.
- We could lose the services of some or all of our key personnel, which would negatively impact our business because of their business development skills, financial expertise, lending experience, technical expertise and market area knowledge.
- The agricultural economy is subject to extreme swings in both the costs of resources and the prices received from the sale of products as a result of weather, government regulations, international trade agreements and consumer tastes, which could negatively impact certain of our customers.
- Loan concentrations in certain industries could negatively impact our results, if financial results or economic conditions deteriorate.
- A budget impasse in the Commonwealth of Pennsylvania could impact our asset values, liquidity and profitability as a result of either delayed or reduced funding to school districts and municipalities who are customers of the bank.
- Companies providing support services related to the exploration and drilling of the natural gas reserves in our market area may be affected by federal, state and local laws and regulations such as restrictions on production, permitting, changes in taxes and environmental protection, which could negatively impact our customers and, as a result, negatively impact our loan and deposit volume and loan quality. Additionally, the activities the companies providing support services related to the exploration and drilling of the natural gas reserves may be dependent on the market price of natural gas. As a result, decreases in the market price of natural gas could also negatively impact these companies, our customers.

Additional factors are discussed in this Annual Report on Form 10-K under *"Item 1A. Risk Factors."* These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Forward-looking statements speak only as of the date they are made and the Company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date of the forward-looking statements or to reflect the occurrence of unanticipated events. Accordingly, past results and trends should not be used by investors to anticipate future results or trends.

INTRODUCTION

The following is management’s discussion and analysis of the significant changes in financial condition, the results of operations, capital resources and liquidity presented in the accompanying consolidated financial statements for the Company. The Company’s consolidated financial condition and results of operations consist almost entirely of the Bank’s financial condition and results of operations. Management’s discussion and analysis should be read in conjunction with the audited consolidated financial statements and related notes. Except as noted, tabular information is presented in thousands of dollars.

The Company currently engages in the general business of banking throughout its service area of Bradford, Tioga, Clinton, Potter and Centre counties in north central Pennsylvania, Lebanon, Berks, Schuylkill and Lancaster counties in south central Pennsylvania and Allegany County in southern New York. We also have a limited branch office in Union county, Pennsylvania, which primarily serves agricultural customers in the central Pennsylvania market. We maintain our main office in Mansfield, Pennsylvania. Presently we operate 34 banking facilities, 31 of which operate as bank branches. In Pennsylvania, the Company has full service offices located in Mansfield, Blossburg, Ulysses, Genesee, Wellsboro, Troy, Sayre, Canton, Gillett, Millerton, LeRaysville, Towanda, Rome, the Mansfield Wal-Mart Super Center, Mill Hall, Schuylkill Haven, Friedensburg, Mt. Aetna, Fredericksburg, Mount Joy, Fivepointville, State College and two branches near the city of Lebanon, Pennsylvania. In November of 2020, we opened a full service branch in Kennett Square, Pennsylvania. We also have a limited branch office in Winfield, Pennsylvania. In New York, our office is in Wellsville. There are two branches in Wilmington Delaware, one branch in Dover Delaware, and a corporate administration building in Wilmington, Delaware, which were acquired as part of the MidCoast acquisition in April 2020.

Risk identification and management are essential elements for the successful management of the Company. In the normal course of business, the Company is subject to various types of risk, including interest rate, credit, liquidity, reputational and regulatory risk.

Interest rate risk is the sensitivity of net interest income and the market value of financial instruments to the direction and frequency of changes in interest rates. Interest rate risk results from various re-pricing frequencies and the maturity structure of the financial instruments owned by the Company. The Company uses its asset/liability and funds management policies to control and manage interest rate risk.

Credit risk represents the possibility that a customer may not perform in accordance with contractual terms. Credit risk results from loans with customers and the purchasing of securities. The Company’s primary credit risk is in the loan portfolio. The Company manages credit risk by adhering to an established credit policy and through a disciplined evaluation of the adequacy of the allowance for loan losses. Also, the investment policy limits the amount of credit risk that may be taken in the investment portfolio.

Liquidity risk represents the inability to generate or otherwise obtain funds at reasonable rates to satisfy commitments to borrowers and obligations to depositors. The Company has established guidelines within its asset/liability and funds management policy to manage liquidity risk. These guidelines include, among other things, contingent funding alternatives.

Reputational risk, or the risk to our business, earnings, liquidity, and capital from negative public opinion, could result from our actual or alleged conduct in a variety of areas, including legal and regulatory compliance, lending practices, corporate governance, litigation, ethical issues, or inadequate protection of customer information, which could include identify theft, or theft of customer information through third parties. We expend significant resources to comply with regulatory requirements. Failure to comply could result in reputational harm or significant legal or remedial costs. Damage to our reputation could adversely affect our ability to retain and attract new customers, and adversely impact our earnings and liquidity.

Regulatory risk represents the possibility that a change in law, regulations or regulatory policy may have a material effect on the business of the Company and its subsidiary. We cannot predict what legislation might be enacted or what regulations might be adopted, or if adopted, the effect thereof on our operations.

Readers should carefully review the risk factors described in other documents the Company files with the SEC, including the annual reports on Form 10-K, the quarterly reports on Form 10-Q and any current reports on Form 8-K filed by us.

SELECTED FINANCIAL DATA

The following table sets forth certain financial data as of and for each of the years in the five year period ended December 31, 2021:

(in thousands, except per share data)	2021	2020	2019	2018	2017
Interest and dividend income	$ 73,217	$ 70,296	$ 61,980	$ 56,758	$ 48,093
Interest expense	7,105	8,105	12,040	9,574	5,839
Net interest income	66,112	62,191	49,940	47,184	42,254
Provision for loan losses	1,550	2,400	1,675	1,925	2,540
Net interest income after provision for loan losses	64,562	59,791	48,265	45,259	39,714
Non-interest income	11,754	11,158	8,242	7,754	7,621
Investment securities gains (losses), net	551	264	144	(19)	1,035
Non-interest expenses	41,550	40,847	33,341	31,557	29,314
Income before provision for income taxes	35,317	30,366	23,310	21,437	19,056
Provision for income taxes	6,199	5,263	3,820	3,403	6,031
Net income	$ 29,118	$ 25,103	$ 19,490	$ 18,034	$ 13,025
Per share data:					
Net income - Basic (1)	$ 7.38	$ 6.53	$ 5.42	$ 4.99	$ 3.59
Net income - Diluted (1)	7.38	6.53	5.41	4.98	3.59
Cash dividends declared (1)	1.86	1.90	1.74	1.69	1.60
Stock dividend	1%	1%	1%	1%	5%
Book value (1) (2)	53.91	48.40	43.14	39.59	36.45
End of Period Balances:					
Total assets	$ 2,143,863	$1,891,674	$ 1,466,339	$1,430,712	$1,361,886
Available for sale securities	412,402	295,189	240,706	241,010	254,782
Loans	1,441,533	1,405,281	1,115,569	1,081,883	1,000,525
Allowance for loan losses	17,304	15,815	13,845	12,884	11,190
Total deposits	1,836,511	1,588,858	1,211,118	1,185,156	1,104,943
Total borrowings	73,977	88,838	85,117	91,194	114,664
Stockholders' equity	212,492	194,259	157,774	139,229	129,011
Key Ratios					
Return on assets (net income to average total assets)	1.45%	1.46%	1.34%	1.29%	1.03%
Return on equity (net income to average total equity)	14.26%	14.21%	13.00%	13.00%	10.04%
Equity to asset ratio (average equity to average total assets, excluding other comprehensive income)	10.20%	10.27%	10.31%	9.90%	10.31%
Net interest margin (tax equivalent) (3)	3.52%	3.92%	3.72%	3.66%	3.80%
Efficiency (4)	51.57%	53.62%	54.27%	55.04%	54.82%
Dividend payout ratio (dividends declared divided by net income)	25.36%	29.32%	32.40%	34.08%	44.97%
Tier 1 leverage (5)	9.31%	9.16%	9.77%	9.15%	9.18%
Common equity risk based capital (5)	12.03%	11.22%	12.11%	11.47%	11.27%
Tier 1 risk-based capital (5)	12.53%	11.75%	12.79%	12.18%	12.04%
Total risk-based capital (5)	14.35%	12.86%	14.04%	13.42%	13.21%
Nonperforming assets/total loans	0.61%	0.93%	1.38%	1.33%	1.18%
Nonperforming loans/total loans	0.53%	0.80%	1.08%	1.27%	1.07%
Allowance for loan losses/total loans	1.20%	1.13%	1.24%	1.19%	1.12%
Net (recoveries)charge-offs/average loans	0.00%	0.03%	0.06%	0.02%	0.03%

(1) Amounts were adjusted to reflect stock dividends.
(2) Calculation excludes accumulated other comprehensive income.
(3) Tax adjusted net interest income to average interest-earning assets. Tax adjusted net Interest income is a non-gaap measure and is reconciled to the GAAP equivalent measure on page 26 of this 10k.
(4) Bank non-interest expenses to tax adjusted net interest income and non-interest income, excluding security gains. Tax adjusted net Interest income is a non-gaap measure and is reconciled to the GAAP equivalent measure on page 30 of this 10k. The efficiency ratio calculated using non-tax effected net interest income was 52.21%, 54.50%, 55.36%, 56.26% and 57.68%, for the years ended 2021, 2020, 2019, 2018 and 2017, respectively.
(5) Ratio calculated on consolidated level

TRUST AND INVESTMENT SERVICES; OIL AND GAS SERVICES

Our Investment and Trust Division is committed to helping our customers meet their financial goals. The Trust Division offers professional trust administration, investment management services, estate planning and administration, custody of securities and individual retirement accounts. In addition to traditional trust and investment services offered, we assist our customers through various oil and gas specific leasing matters from lease negotiations to establishing a successful approach to personal wealth management. Assets held by the Bank in a fiduciary or agency capacity for its customers are not included in the consolidated financial statements since such items are not assets of the Bank. As of December 31, 2021 and 2020, assets owned and invested by customers of the Bank through the Bank's investment representatives totaled $282.1 million and $241.0 million, respectively. Additionally, as summarized in the table below, the Trust Department had assets under management as of December 31, 2021 and 2020 of $154.8 million and $150.3 million, respectively. During the year ended December 31, 2021, $1.3 million of new trust accounts were opened, $9.5 million of additional contributions to trust accounts, $9.6 million distributed from trust accounts, and $13.2 million of accounts were closed. As a result of market fluctuations, the fair value of the trust accounts increased approximately $16.6 million during the year ended December 31, 2021. The following table reflects trust accounts by investment type and structure:

(market values - in thousands)	**2021**	2020
INVESTMENTS:		
Bonds	**$ 8,640**	$ 11,777
Stock	**22,099**	30,867
Savings and Money Market Funds	**11,587**	13,427
Mutual Funds	**105,233**	86,141
Mineral interests	**2,959**	2,738
Mortgages	**856**	956
Real Estate	**2,099**	1,560
Miscellaneous	**942**	625
Cash	**425**	2,257
TOTAL	**$ 154,840**	$ 150,348
ACCOUNTS:		
Trusts	**46,953**	40,234
Guardianships	**443**	2,817
Employee Benefits	**62,149**	58,751
Investment Management	**45,293**	48,462
Custodial	**2**	84
TOTAL	**$ 154,840**	$ 150,348

Our financial consultants offer full service brokerage and financial planning services throughout the Bank's market areas. Appointments can be made at any Bank branch. Products such as mutual funds, annuities, health and life insurance are made available through our insurance subsidiary, First Citizens Insurance Agency, Inc.

RESULTS OF OPERATIONS

Net income for the year ended December 31, 2021 was $29,118,000, which represents an increase of $4,015,000, or 16.0%, when compared to 2020. Net income for the year ended December 31, 2020 was $25,103,000, which represents an increase of $5,613,000, or 28.8%, when compared to 2019. Basic earnings per share were $7.38, $6.53 and $5.42 for 2021, 2020 and 2019, respectively, while diluted earnings per share were $7.38, $6.53 and $5.41, for 2021, 2020 and 2019, respectively.

Net income is influenced by five key components: net interest income, provision for loan losses, non-interest income, non-interest expenses, and the provision for income taxes.

Net Interest Income

The most significant source of revenue is net interest income; the amount by which interest earned on interest-earning assets exceeds interest paid on interest-bearing liabilities. Factors that influence net interest income are changes in volume of interest-earning assets and interest-bearing liabilities as well as changes in the associated interest rates.

The following table sets forth the Company's average balances of, and the interest earned or incurred on, each principal category of assets, liabilities and stockholders' equity, the related rates, net interest income and rate "spread" created. The acquisition of MidCoast, which closed on April 17, 2020, impacted the average balances and rates for 2020 when compared to 2019:

Analysis of Average Balances and Interest Rates

(dollars in thousands)	**2021** Average Balance (1) $	**2021** Interest $	**2021** Average Rate %	2020 Average Balance (1) $	2020 Interest $	2020 Average Rate %	2019 Average Balance (1) $	2019 Interest $	2019 Average Rate %
ASSETS									
Short-term investments:									
Interest-bearing deposits at banks	**108,872**	**124**	**0.11**	41,330	37	0.09	9,693	23	0.24
Total short-term investments	**108,872**	**124**	**0.11**	41,330	37	0.09	9,693	23	0.24
Interest bearing time deposits at banks	**12,527**	**323**	**2.57**	14,139	364	2.57	15,085	384	2.55
Investment securities:									
Taxable	**252,470**	**4,198**	**1.66**	188,241	4,488	2.38	188,697	5,170	2.74
Tax-exempt (3)	**104,379**	**2,786**	**2.67**	80,131	2,366	2.95	58,637	1,889	3.22
Total investment securities	**356,849**	**6,984**	**1.96**	268,372	6,854	2.55	247,334	7,059	2.85
Loans:									
Residential mortgage loans	**203,062**	**9,867**	**4.86**	210,696	11,161	5.30	215,749	11,473	5.32
Construction loans	**56,315**	**2,292**	**4.07**	26,343	1,288	4.89	19,085	984	5.16
Commercial Loans	**739,000**	**36,215**	**4.90**	590,469	31,087	5.26	415,681	22,741	5.47
Agricultural Loans	**349,951**	**15,079**	**4.31**	357,201	16,022	4.49	344,586	15,879	4.61
Loans to state & political subdivisions	**52,804**	**1,871**	**3.54**	86,143	3,458	4.01	97,780	3,845	3.93
Other loans	**24,125**	**1,385**	**5.74**	20,986	1,185	5.65	9,684	740	7.64
Loans, net of discount (2)(3)(4)	**1,425,257**	**66,709**	**4.68**	1,291,838	64,201	4.97	1,102,565	55,662	5.05
Total interest-earning assets	**1,903,505**	**74,140**	**3.89**	1,615,679	71,456	4.42	1,374,677	63,128	4.59
Cash and due from banks	**6,525**			7,487			6,168		
Bank premises and equipment	**17,194**			17,286			16,074		
Other assets	**75,410**			79,305			57,038		
Total non-interest earning assets	**99,129**			104,078			79,280		
Total assets	**2,002,634**			1,719,757			1,453,957		
LIABILITIES AND STOCKHOLDERS' EQUITY									
Interest-bearing liabilities:									
NOW accounts	**457,189**	**1,387**	**0.30**	383,931	1,102	0.29	331,906	2,282	0.69
Savings accounts	**290,376**	**322**	**0.11**	241,429	476	0.20	218,240	814	0.37
Money market accounts	**257,937**	**684**	**0.27**	205,142	1,012	0.49	164,872	1,978	1.20
Certificates of deposit	**351,265**	**3,444**	**0.98**	345,397	4,261	1.23	277,946	4,145	1.49
Total interest-bearing deposits	**1,356,767**	**5,837**	**0.43**	1,175,899	6,851	0.58	992,964	9,219	0.93
Other borrowed funds	**84,621**	**1,268**	**1.50**	93,237	1,254	1.34	109,041	2,821	2.59
Total interest-bearing liabilities	**1,441,388**	**7,105**	**0.49**	1,269,136	8,105	0.64	1,102,005	12,040	1.09
Demand deposits	**341,604**			257,285			187,991		
Other liabilities	**15,420**			16,662			14,074		
Total non-interest-bearing liabilities	**357,024**			273,947			202,065		
Stockholders' equity	**204,222**			176,674			149,887		
Total liabilities & stockholders' equity	**2,002,634**			1,719,757			1,453,957		
Net interest income		**67,035**			63,351			51,088	
Net interest spread (5)			**3.40%**			3.78%			3.50%
Net interest income as a percentage of average interest-earning assets			**3.52%**			3.92%			3.72%
Ratio of interest-earning assets to interest-bearing liabilities			**1.32**			1.27			1.25

(1) Averages are based on daily averages.

(2) Includes loan origination and commitment fees.

(3) Tax exempt interest revenue is shown on a tax equivalent basis for proper comparison using a statutory federal income tax rate of 21% for 2021, 2020 and 2019.

(4) Income on non-accrual loans is accounted for on a cash basis, and the loan balances are included in interest-earning assets.

(5) Interest rate spread represents the difference between the average rate earned on interest-earning assets and the average rate paid on interest-bearing liabilities.

For purposes of the comparison, as well as the discussion that follows, this presentation facilitates performance comparisons between taxable and tax-free assets by increasing the tax-free income by an amount equivalent to the Federal income taxes that would have been paid if this income were taxable at the Federal statutory rate for the corresponding year. Accordingly, tax equivalent adjustments for investments and loans have been made accordingly to the previous table for the years ended December 31, 2021, 2020 and 2019, respectively (in thousands):

	2021	2020	2019
Interest and dividend income from investment securities, interest bearing time deposits and short-term investments (non-tax adjusted) (GAAP)	**$ 6,846**	$ 6,758	$ 7,069
Tax equivalent adjustment	**585**	497	397
Interest and dividend income from investment securities, interest bearing time deposits and short-term investments (tax equivalent basis) (Non-GAAP)	**$ 7,431**	$ 7,255	$ 7,466

	2021	2020	2019
Interest and fees on loans (non-tax adjusted) (GAAP)	**$ 66,371**	$ 63,538	$ 54,911
Tax equivalent adjustment	**338**	663	751
Interest and fees on loans (tax equivalent basis) (Non-GAAP)	**$ 66,709**	$ 64,201	$ 55,662

	2021	2020	2019
Total interest income	**$ 73,217**	$ 70,296	$ 61,980
Total interest expense	**7,105**	8,105	12,040
Net interest income (GAAP)	**66,112**	62,191	49,940
Total tax equivalent adjustment	**923**	1,160	1,148
Net interest income (tax equivalent basis) (Non-GAAP)	**$ 67,035**	$ 63,351	$ 51,088

The following table shows the tax-equivalent effect of changes in volume and rates on interest income and expense (in thousands):

Analysis of Changes in Net Interest Income on a Tax-Equivalent Basis

	2021 vs. 2020 (1)			2020 vs. 2019 (1)		
	Change in Volume	**Change in Rate**	**Total Change**	Change in Volume	Change in Rate	Total Change
Interest Income:						
Short-term investments:						
Interest-bearing deposits at banks	**$ 73**	**$ 14**	**$ 87**	$ 16	$ (2)	$ 14
Interest bearing time deposits at banks	**(41)**	**-**	**(41)**	(24)	4	(20)
Investment securities:						
Taxable	**1,287**	**(1,577)**	**(290)**	(13)	(669)	(682)
Tax-exempt	**615**	**(195)**	**420**	615	(138)	477
Total investment securities	**1,902**	**(1,772)**	**130**	602	(807)	(205)
Total investment income	**1,934**	**(1,758)**	**176**	594	(805)	(211)
Loans:						
Residential mortgage loans	**(394)**	**(900)**	**(1,294)**	(263)	(49)	(312)
Construction loans	**1,177**	**(173)**	**1,004**	353	(49)	304
Commercial Loans	**7,074**	**(1,946)**	**5,128**	9,164	(818)	8,346
Agricultural Loans	**(321)**	**(622)**	**(943)**	524	(381)	143
Loans to state & political subdivisions	**(1,218)**	**(369)**	**(1,587)**	(471)	84	(387)
Other loans	**180**	**20**	**200**	573	(128)	445
Total loans, net of discount	**6,498**	**(3,990)**	**2,508**	9,880	(1,341)	8,539
Total Interest Income	**8,432**	**(5,748)**	**2,684**	10,474	(2,146)	8,328
Interest Expense:						
Interest-bearing deposits:						
NOW accounts	**219**	**66**	**285**	444	(1,624)	(1,180)
Savings accounts	**133**	**(287)**	**(154)**	91	(429)	(338)
Money Market accounts	**410**	**(738)**	**(328)**	686	(1,652)	(966)
Certificates of deposit	**73**	**(890)**	**(817)**	416	(300)	116
Total interest-bearing deposits	**835**	**(1,849)**	**(1,014)**	1,637	(4,005)	(2,368)
Other borrowed funds	**(60)**	**74**	**14**	(360)	(1,207)	(1,567)
Total interest expense	**775**	**(1,775)**	**(1,000)**	1,277	(5,212)	(3,935)
Net interest income	**$ 7,657**	**$ (3,973)**	**$ 3,684**	$ 9,197	$ 3,066	$ 12,263

(1) The portion of the total change attributable to both volume and rate changes during the year has been allocated to volume and rate components based upon the absolute dollar amount of the change in each component prior to allocation.

2021 vs. 2020

Tax equivalent net interest income for 2021 was $67,035,000 compared to $63,351,000 for 2020, an increase of $3,684,000 or 5.8%. Total interest income increased $2,684,000, as loan interest income increased $2,508,000, and total investment income increased $176,000. Interest expense decreased $1,000,000 from 2020.

Total tax equivalent interest income from investment securities increased $130,000 in 2021 from 2020. The average balance of investment securities increased $88.5 million, which had an effect of increasing interest income by $1,902,000 due to volume. The majority of the increase in volume was in tax-exempt securities, which experienced an increase in the average balance of $64.2 million. The average tax-effected yield on our investment portfolio decreased from 2.55% in 2020 to 1.96% in 2021. The decrease in the tax-effected yield is attributable to purchases made in a lower rate environment. As a result of the yield on investment securities decreasing 59 basis points (bps) to 1.96%, interest income on investment securities decreased $1,772,000, with the decrease primarily related to taxable securities. The investment strategy for 2021 has been to utilize cashflows from the investment portfolio and deposit inflows to purchase U.S. treasury securities, mortgage backed securities issued by government sponsored entities and obligations of state and political securities. The increase in the investment portfolio was in response to the deposit inflows that occurred in 2021. We continually monitor interest rate trading ranges and try to focus purchases to times when rates are in the top of the trading range. The Bank believes its investment strategy has appropriately mitigated its interest rate risk exposure for various rate environments, while providing sufficient cashflows to meet liquidity needs.

In total, loan interest income increased $2,508,000 in 2021 from 2020. The average balance of our loan portfolio increased by $133.4 million in 2021 compared to 2020, which resulted in an increase in interest income of $6,498,000 due to volume. The increase in the average balance of loans was driven by the MidCoast acquisition from 2020, which was outstanding for the entire year and loan growth that occurred primarily in the Delaware market. The average tax-effected yield on our loan portfolio decreased 29 basis points to 4.68% in 2021, resulting in a decrease in loan interest income of $3,990,000. The decrease in the tax-effected yield was due to the lower rate environment promoted by the Federal Reserve in response to the COVID-19 pandemic.

- Interest income on residential mortgage loans decreased $1,294,000. The average balance of residential mortgage loans decreased $7.6 million, resulting in a decrease of $394,000 due to volume. The decrease in loans is due to loans being refinanced and sold on the secondary market. The change due to rate was a decrease of $900,000 as the average yield on residential mortgages decreased from 5.30% in 2020 to 4.86% in 2021 as a result of the lower rate environment during the year as a result of COVID-19 pandemic.

- The average balance of construction loans increased $30.0 million from 2020 to 2021 as a result of projects in our south central Pennsylvania market and Delaware market, which resulted in an increase of $1,177,000 in interest income. The average yield on construction loans decreased from 4.89% to 4.07%, which correlated to a $173,000 decrease in interest income.

- Interest income on commercial loans increased $5,128,000 from 2020 to 2021. The increase in the average balance of commercial loans of $148.5 million is attributable to the MidCoast acquisition and growth in the Delaware market. The increase in the average balance of these loans resulted in an increase in interest income due to volume of $7,074,000. Our lenders have been able to attract and retain loan relationships in their markets by providing excellent customer service and having attractive products. We believe our lenders are adept at customizing and structuring loans to customers that meet their needs and satisfy our commitment to credit quality. In many cases, the Bank works with the Small Business Administration (SBA) guaranteed loan programs to offset credit risk and to further promote economic growth in our market area. The average yield on commercial loans decreased 36 basis points to 4.90% in 2021, resulting in a decrease in interest income due to rate of $1,946,000.

- Interest income on agricultural loans decreased $943,000 from 2020 to 2021. The decrease in the average balance of agricultural loans of $7.3 million is primarily attributable to the south central Pennsylvania market. The decrease in the average balance of these loans resulted in a decrease in interest income due to volume of $321,000. The average yield on agricultural loans decreased from 4.49% in 2020 to 4.31% in 2021 due to a general decrease in rates, resulting in a decrease in interest income due to rate of $622,000. We believe our lenders are adept at customizing, understanding and have the expertise to structure loans for customers that meet their needs and satisfy our commitment to credit quality. In many cases, the Bank works with the United States Department of Agriculture's (USDA) guaranteed loan programs to offset credit risk and to further promote economic growth in our market area.

- The average balance of loans to state and political subdivisions decreased $33.3 million from 2020 to 2021 which had a negative impact of $1,218,000 on total interest income due to volume was due to customers refinancing through the municipal bond market. The average tax equivalent yield on loans to state and political subdivisions decreased from 4.01% in 2020 to 3.54% in 2021, decreasing interest income by $369,000.

- The average balance of other loans increased $3.1 million as a result of an increase in outstanding student loans. This resulted in an increase of $180,000 on total interest income due to volume. The average tax equivalent yield on other loans increased from 5.65% in 2020 to 5.74% in 2021, increasing interest income by $20,000 in other loans

Total interest expense decreased $1,000,000 in 2021 compared to 2020. The majority of the decrease was due to a decrease in the average rate paid on interest bearing deposits of 15 basis points to 0.43%. This decrease resulted in a decrease in interest expense of $1,849,000. The decrease in rates was driven by the Federal Reserve's response to the COVID-19 pandemic. The average rate on certificates of deposit decreased from 1.23% to 0.98% resulting in a decrease in interest expense of $890,000. The average rate on money markets decreased from 0.49% to 0.27% resulting in a decrease in interest expense of $738,000. The average rate paid on savings accounts decreased 9 bps and resulted in a decrease in interest expense of $287,000. The average rate paid on other borrowed funds increased from 1.34% to 1.50% resulting in an increase in interest expense of $74,000 and was due to interest expense on debt issued in 2021.

Average interest-bearing liabilities increased $172.3 million in 2021, with average interest-bearing deposits increasing $180.9 million and average other borrowings decreasing $8.6 million. As a result of the increase in average deposits, interest expense increased $835,000 as result of the change in volume. Increases in average deposits, which were primarily driven by organic growth across all markets of the Bank, included NOW accounts of $73.3 million, savings accounts of $48.9 million, money market accounts of $52.8 million and certificates of deposits of $5.9 million The combined impact to interest expense of these increases was $835,000. The average balance of other borrowed funds decreased $8.6 million, which corresponds to a decrease in interest expense of $60,000.

Our tax equivalent net interest margin for 2021 was 3.52% compared to 3.92% for 2020, with the change attributable to the yield of interest-earning assets decreasing more than the cost from interest-bearing liabilities during 2021. Interest rates rose in 2021 in response to shifting expectations for fiscal policy and an enduring pandemic that continued to hamper economic activity, strengthening and prolonging unusually strong inflationary pressures and altering the expected path of monetary policy. The moves up for interest rates, however, unfolded across the maturity spectrum at different times during the year. Longer yields peaked at the end of the first quarter, propelled higher by the rollout of vaccines and expectations for more stimulative fiscal policy. Federal Reserve officials abandoned in the second half of the year their belief that higher inflation would prove transitory and had shifted to a notably more aggressive posture by year's end. The central bank's official forecast from March 2021 for rates to remain near zero for the next several years gave way to a call by December to raise the federal funds target rate range by 1.50% by the end of 2023. Federal funds futures contracts, which began the year flat across the forecast horizon, reflected a presumption for three 25-basis point rate hikes in 2022 and two more in 2023. The 2-year Treasury yield traded within a range of 0.10% to 0.19% from January 1 through the Federal Reserve's June 15 meeting, was bounded between 0.17% and 0.27% from mid-June to the September 22 meeting, but climbed steeply in the fourth quarter to 0.73% by year's end. Along a similar timeline, the 5-year Treasury yield rose from a low of 0.35% in early January to 1.26% by the end of the year. Despite historic inflation readings in the second half of the year, concerns that the abrupt policy shift by the Federal Reserve to fight inflation raised the risk of a policy error that could disrupt the recovery kept longer yields in check. The 10-year yield failed to eclipse its March high and finished the year at 1.51%. The timing differences of rate changes across the curve had a noticeable and informative impact on the shape of the curve throughout the year. The spread between the 2-year and 10-year Treasury yields expanded from 0.79% on January 1, 2021 to a peak of 1.58% on March 31, 2021. Stepping lower in stages for the remainder of the year, the spread tightened back to 0.77% by the end of 2021.

2020 vs. 2019

Tax equivalent net interest income for 2020 was $63,351,000 compared to $51,088,000 for 2019, an increase of $12,263,000 or 24.0%. Total interest income increased $8,328,000, as loan interest income increased $8,539,000, and total investment income decreased $211,000. Interest expense decreased $3,935,000 in 2020 from 2019.

Total tax equivalent interest income from investment securities decreased $205,000 in 2020 from 2019. The average balance of investment securities increased $21.0 million, which had an effect of increasing interest income by $602,000 due to volume. The majority of the increase in volume was in tax-exempt securities, which experienced an increase in the average balance of $21.5 million. The average tax-effected yield on our investment portfolio decreased from 2.85% in 2019 to 2.55% in 2020. The decrease in the tax-effected yield is attributable to purchases made in a lower rate environment and calls in the third quarter of 2019 of securities purchased at a discount. As a result of the yield on investment securities decreasing 30 basis points (bps) to 2.55%, interest income on investment securities decreased $807,000, with the decrease primarily related to taxable securities. The increase in the investment portfolio was in response to growth in deposits that exceeded organic loan opportunities in 2019. The Covid-19 pandemic did provide opportunities for the Company to purchase high quality municipal securities and mortgage backed securities with relatively high spreads in the first and second quarters of 2020. Purchases in the second half of 2020 were reflective of tighter spreads and lower yields due government stimulus and its impact on bond markets and deposit levels.

In total, loan interest income increased $8,539,000 in 2020 from 2019. The average balance of our loan portfolio increased by $189.3 million in 2020 compared to 2019, which resulted in an increase in interest income of $9,880,000 due to volume. The increase in the average balance of loans was driven by the MidCoast acquisition in the first quarter of 2020 and the PPP program authorized by the SBA in response to the COVID-19 pandemic. Organic growth in the first three quarters of 2020, excluding the PPP program was limited, but did increase in the fourth quarter of 2020, primarily in our Delaware market. The average tax-effected yield on our loan portfolio decreased 8 basis points to 4.97% in 2020, resulting in a decrease in loan interest income of $1,341,000. The decrease in the tax-effected yield was due to the lower rate environment promoted by the Federal Reserve in 2020 in response to the COVID-19 pandemic.

- Interest income on residential mortgage loans decreased $312,000. The average balance of residential mortgage loans decreased $5.1 million, resulting in a decrease of $263,000 due to volume. The decrease in loans is due to loans being refinanced and sold on the secondary market. The change due to rate was a decrease of $49,000 as the average yield on residential mortgages decreased from 5.32% in 2019 to 5.30% in 2020 as a result of the lower rate environment during the year as a result of COVID-19 pandemic.

- The average balance of construction loans increased $7.3 million from 2019 to 2020 as a result of the acquisition and projects in our south central Pennsylvania market, which resulted in an increase of $353,000 in interest income. The average yield on construction loans decreased from 5.16% to 4.89%, which correlated to a $49,000 decrease in interest income.

- Interest income on commercial loans increased $8,346,000 from 2019 to 2020. The increase in the average balance of commercial loans of $174.8 million is attributable to the MidCoast acquisition and PPP loans originated in the second and third quarters of 2020. The increase in the average balance of these loans resulted in an increase in interest income due to volume of $9,164,000. The average yield on commercial loans decreased 21 basis points to 5.26% in 2020, resulting in a decrease in interest income due to rate of $818,000.

- Interest income on agricultural loans increased $143,000 from 2019 to 2020. The increase in the average balance of agricultural loans of $12.6 million is primarily attributable to the central and south central markets as well as the acquisition. The increase in the average balance of these loans resulted in an increase in interest income due to volume of $524,000. The average yield on agricultural loans decreased from 4.61% in 2019 to 4.49% in 2020 due to a general decrease in rates, resulting in a decrease in interest income due to rate of $381,000.

- The average balance of loans to state and political subdivisions decreased $11.6 million from 2019 to 2020 which had a negative impact of $471,000 on total interest income due to volume. The average tax equivalent yield on loans to state and political subdivisions increased from 3.93% in 2019 to 4.01% in 2020, increasing interest income by $84,000.

- The average balance of other loans increased $11.3 million as a result of an increase in outstanding student loans. This resulted in an increase of $573,000 on total interest income due to volume. The average tax equivalent yield on other loans decreased from 7.64% in 2019 to 5.65% in 2020 as a result of the growth in student loans, decreasing interest income by $128,000 in student loans

Total interest expense decreased $3,935,000 in 2020 compared to 2019. The majority of the decrease was due to a decrease in the average rate paid on interest bearing liabilities of 45 basis points to 0.64%. This decrease resulted in a decrease in interest expense of $5,212,000. The decrease in rates was driven by the Federal Reserve decreasing rates in the second half of 2019 as a result of a slowing economy and in the first quarter of 2020 in response to the COVID-19 pandemic. The average rate on certificates of deposit decreased from 1.49% to 1.23% resulting in a decrease in interest expense of $300,000. The average rate paid on other borrowed funds decreased from 2.59% to 1.34% resulting in a decrease in interest expense of $1,207,000. The average rate paid on money market accounts decreased from 1.20% to 0.49% resulting in a decrease in interest expense of $1,652,000. The average rate paid on NOW accounts decreased from 0.69% in 2019 to 0.29% in 2020 resulting in a decrease in interest expense of $1,624,000. The average rate paid on savings accounts decreased 17 bps and resulted in a decrease in interest expense of $429,000.

Average interest-bearing liabilities increased $167.1 million in 2020, with average interest-bearing deposits increasing $182.9 million and average other borrowings decreasing $15.8 million. As a result of the increase in average deposits, interest expense increased $1,277,000 as result of the change in volume. Increases in average deposits, which were primarily driven by the MidCoast acquisition, included NOW accounts of $52.0 million, savings accounts of $23.2 million, money market accounts of $40.3 million and certificates of deposits of $67.5 million The combined impact to interest expense of these increases was $1,637,000. The average balance of other borrowed funds decreased $15.8 million, which corresponds to a decrease in interest expense of $360,000.

Our tax equivalent net interest margin for 2020 was 3.92% compared to 3.72% for 2019, with the change attributable to the cost of interest-bearing liabilities decreasing more than income from interest earning assets during 2020.

PROVISION FOR LOAN LOSSES

For the year ended December 31, 2021, we recorded a provision for loan losses of $1,550,000. The provision for 2021 was $850,000, or 35.4%, lower than the provision in 2020. The decrease in the provision for loan losses was primarily the result of the impact the COVID-19 pandemic had on the economy in 2020 and limited organic growth in 2021 compared to 2020. (see also “Financial Condition – Allowance for Loan Losses and Credit Quality Risk”).

For the year ended December 31, 2020, we recorded a provision for loan losses of $2,400,000. The provision for 2020 was $725,000, or 43.3%, higher than the provision in 2019. The increase in the provision for loan losses was primarily the result of the COVID-19 pandemic and its impact on our economy as well as organic growth attributable to the Delaware market primarily in the fourth quarter of 2020 (see also “Financial Condition – Allowance for Loan Losses and Credit Quality Risk”).

NON-INTEREST INCOME

The following table reflects non-interest income by major category for the years ended December 31 (dollars in thousands):

	2021	2020	2019
Service charges	**4,755**	$ 4,221	$ 4,687
Trust	**865**	803	750
Brokerage and insurance	**1,625**	1,297	1,141
Equity security gains (losses), net	**339**	(41)	120
Available for sale security gains, net	**212**	305	24
Gains on loans sold	**1,283**	2,168	473
Earnings on bank owned life insurance	**1,828**	695	623
Other	**1,398**	1,974	568
Total	**$ 12,305**	$ 11,422	$ 8,386

	2021/2020 Change		2020/2019 Change	
	Amount	**%**	Amount	%
Service charges	**$ 534**	**12.7**	$ (466)	(9.9)
Trust	**62**	**7.7**	53	7.1
Brokerage and insurance	**328**	**25.3**	156	13.7
Equity security gains (losses), net	**380**	**(926.8)**	(161)	(134.2)
Available for sale security gains (losses), net	**(93)**	**(30.5)**	281	1,170.8
Gains on loans sold	**(885)**	**(40.8)**	1,695	358.4
Earnings on bank owned life insurance	**1,133**	**163.0**	72	11.6
Other	**(576)**	**(29.2)**	1,406	247.5
Total	**$ 883**	**7.7**	$ 3,036	36.2

2021 vs. 2020

Non-interest income increased $883,000 in 2021 from 2020, or 7.7%. We experienced a $212,000 net gain on available for sale securities in 2021 compared to net gains totaling $305,000 in 2020. During 2021, we sold $17.2 million of US treasury securities for a pre-tax gain of $177,000 and $12.0 million of US Agency securities for a pre-tax gain of $35,000 to take advantage of market conditions at the time of the sales. During 2020, we sold 19 mortgage backed securities for a net gain of $305,000 to lock in gains that benefitted from the Federal Reserve investment purchase program in response to the COVID-19 pandemic. During 2021, net equity security gains amounted to $339,000 as a result of market gains experienced in 2021 compared to losses of $41,000 last year associated with the Covid-19 pandemic.

Gains on loans sold decreased $885,000 compared to last year. The decrease in gains on loans sold is attributable to a $20.2 million, or 26.6% decrease in the proceeds from the sale of residential mortgages loans. The increase in service charges of $534,000 for 2021 is attributable to the Bank’s response to the COVID-19 pandemic in 2020 and an increase in customer spending in 2021 compared to 2020 which was impacted by mandatory stay at home orders as customers ate out less and spent less on discretionary items. The decrease in other income is due to fees on offering derivative contracts for certain customers, that provided the customer with fixed rate loans, which generated fee income of $494,000 in 2021 compared to $1,373,000 in 2020. The increase in earnings on bank owned life insurance is due to two former employees of the Company passing during the first quarter of 2021, which generated a death benefit payable to the Company of $1,155,000. The increase in brokerage and insurance commissions was attributable to growth in our south central and north central, Pennsylvania markets.

2020 vs. 2019

Non-interest income increased $3,036,000 in 2020 from 2019, or 36.2%. We experienced a $305,000 net gain on available for sale securities in 2020 compared to net gains totaling $24,000 in 2019. During 2020, we sold 19 mortgage backed securities for a net gain of $305,000 to lock in gains that benefitted from the Federal Reserve investment purchase program in response to the COVID-19 pandemic. During 2019, we sold 3 agency securities for a net gain of $1,000 and 4 US Treasury securities for a gain of $23,000 to fund loan growth and to restructure the investment portfolio to improve performance in the current rate environment. During 2020, net equity security losses amounted to $41,000 as a result of market losses associated with the Covid-19 pandemic compared to gains of $120,000 in 2019.

Gains on loans sold increased $1,695,000 compared to 2019. The increase in gains on loans sold was attributable to a $54.0 million, or 248.1% increase in the proceeds from the sale of residential mortgages loans as a result of the low rate environment, which has significantly increased residential refinancings. The decrease in service charges of $466,000 for 2020 is attributable to the Bank’s response to the COVID-19 pandemic and a decrease in customer spending as a result of mandatory stay at home orders as customers ate out less and spent less on discretionary items. The increase in other income is due to fees on offering derivative contracts for certain customers, that provided the customer with fixed rate loans, which generated fee income of $1,373,000 in 2020. The increase in brokerage and insurance commissions was primarily attributable to growth in our south central market.

Non-interest Expenses

The following tables reflect the breakdown of non-interest expense by major category for the years ended December 31 (dollars in thousands):

	2021	2020	2019
Salaries and employee benefits	**25,902**	$ 24,190	$ 20,456
Occupancy	**2,966**	2,557	2,174
Furniture and equipment	**519**	757	674
Professional fees	**1,526**	1,517	1,423
FDIC insurance	**522**	476	75
Pennsylvania shares tax	**880**	868	808
Amortization of intangibles	**192**	216	259
Merger and acquisition	**-**	2,179	466
ORE expenses	**439**	451	376
Software expenses	**1,321**	1,155	948
Other	**7,283**	6,481	5,682
Total	**$ 41,550**	$ 40,847	$ 33,341

	2021/2020 Change		2020/2019 Change	
	Amount	**%**	Amount	%
Salaries and employee benefits	**$ 1,712**	**7.1**	$ 3,734	18.3
Occupancy	**409**	**16.0**	383	17.6
Furniture and equipment	**(238)**	**(31.4)**	83	12.3
Professional fees	**9**	**0.6**	94	6.6
FDIC insurance	**46**	**9.7**	401	534.7
Pennsylvania shares tax	**12**	**1.4**	60	7.4
Amortization of intangibles	**(24)**	**(11.1)**	(43)	(16.6)
Merger and acquisition	**(2,179)**	**(100.0)**	1,713	367.6
ORE expenses	**(12)**	**(2.7)**	75	19.9
Software expenses	**166**	**14.4**	207	21.8
Other	**802**	**12.4**	799	14.1
Total	**$ 703**	**1.7**	$ 7,506	22.5

2021 vs. 2020

Non-interest expenses for 2021 totaled $41,550,000, which represents an increase of $703,000, compared to 2020 expenses of $40,847,000. Salaries and employee benefits increased $1,712,000 or 7.1%. The increase was due to merit increases effective at the beginning of 2021, additional headcount as part of the MidCoast acquisition and servicing the Delaware market and increased profit sharing expenses due to increased profitability of the Company. Employee commissions related to brokerage and insurance commissions increased due to the increased sales in 2021 compared to 2020.

The increase in occupancy expenses is due to the additional branches acquired as part of the MidCoast acquisition and the Kennett Square branch as they are included for a full year in 2021. The decrease in merger and acquisition costs was due to costs associated with the MidCoast acquisition that closed in April 2020. The decrease in furniture and fixtures is due to a decrease in non-capitalized items that were purchased in 2020 to support the acquisition. The increase in other expenses is due to charitable contributions made in our south central Pennsylvania and Delaware markets the Delaware franchise tax due to the performance of the Delaware market, advertising and promotions associated with the Delaware markets.

2020 vs. 2019

Non-interest expenses for 2020 totaled $40,847,000, which represents an increase of $7,506,000, compared to 2019 expenses of $33,341,000. The primary cause of the total increase was the MidCoast acquisition costs, as well as the additional salaries and benefits costs of the acquired employees. Salary and benefit costs increased $3,734,000, or 18.3%. Base salaries and related payroll taxes increased $3,081,000 as a result of merit increases and additional headcount associated with the acquisition. Full time equivalent staffing was 281 and 259 for 2020 and 2019, respectively. Profit sharing expenses increased $829,000 compared to 2019, as a result of the employee mix and increased profitability, which resulted in higher bonuses to employees.

The increase in occupancy and furniture and equipment expenses was due to the additional branches acquired as part of the MidCoast acquisition. The increase in merger and acquisition expenses was due to costs associated with the MidCoast acquisition that closed in April 2020. The increase in FDIC insurance in 2020 was due to credits received from the FDIC in 2019 as the Deposit Insurance Fund exceeded 1.38% as well as organic and acquisition growth that occurred in 2020. The increase in software expenses is due to new systems implemented in the second half of 2020 for our tellers and image capture and review. The largest drivers of the increase in other expenses was the termination of a pension plan in 2019 for a gain that was acquired as of the FNB acquisition in 2015, ATM and data processing expenses as a result of fraud prevention, contributions in response to the COVID-19 pandemic, supplies for the additional branches and the Delaware franchise fee. The increase in ORE expenses is the result of net losses on the disposal of ORE properties in 2020 compared to a net gain in 2019.

Provision for Income Taxes

The provision for income taxes was $6,199,000, $5,263,000 and $3,820,000 for 2021, 2020 and 2019, respectively. The effective tax rates for 2021, 2020 and 2019 were 17.6%, 17.3% and 16.4%, respectively.

The increase in income tax expense of $936,000 in 2021 was due to the increase of $4,951,000 in income before the provision for income taxes, which accounts for an increase in tax expense of $1,040,000 at a 21% tax rate.

The increase in income tax expense of $1,443,000 in 2020 was due to the increase of $7,056,000 in income before the provision for income taxes, which accounts for an increase in tax expense of $1,482,000 at a 21% tax rate.

We are involved in five limited partnership agreements that operate low-income housing projects in our market areas, one of which we entered into during 2021. During 2021, 2020 and 2019, we recognized tax credits related to one of the five partnerships. The 2021 partnership started in 2021 and credits are expected to be available in 2022. Tax credits associated with three of the partnerships were fully utilized by December 2016. We anticipate recognizing an aggregate of $3.1 million of tax credits over the next twelve years.

FINANCIAL CONDITION

The following table presents ending balances (dollars in millions), the dollar amount of change and the percentage change during the past two years:

	2021 Balance	**Increase**	**% Change**	2020 Balance
Total assets	**$ 2,143.9**	**$ 252.2**	**13.3**	$ 1,891.7
Total investments	**412.4**	**117.2**	**39.7**	295.2
Total loans, net	**1,424.2**	**34.7**	**2.5**	1,389.5
Total deposits	**1,836.2**	**247.3**	**15.6**	1,588.9
Total borrowings	**74.0**	**(14.8)**	**(16.7)**	88.8
Total stockholders' equity	**212.5**	**18.2**	**9.4**	194.3

Cash and Cash Equivalents

Cash and cash equivalents totaled $172.8 million at December 31, 2021 compared to $68.7 million at December 31, 2020. Management actively measures and evaluates its liquidity through our Asset – Liability committee and believes its liquidity needs are satisfied by the current balance of cash and cash equivalents, readily available access to traditional funding sources, Federal Home Loan Bank financing, federal funds lines with correspondent banks, brokered certificates of deposit and the portion of the investment and loan portfolios that mature within one year. Management expects that these sources of funds will permit us to meet cash obligations and off-balance sheet commitments as they come due.

Investments

The following table shows the year-end composition of the investment portfolio, at fair value, for the two years ended December 31 (dollars in thousands):

	2021 Amount	% of Total	2020 Amount	% of Total
Available-for-sale:				
U. S. Agency securities	**$ 73,945**	**17.8**	$ 81,416	27.4
U.S. Treasuries	**115,347**	**27.8**	28,043	9.4
Obligations of state & political subdivisions	**112,021**	**27.0**	102,972	34.7
Corporate obligations	**10,333**	**2.5**	6,509	2.2
Mortgage-backed securities	**100,756**	**24.3**	76,249	25.7
Equity securities (a)	**2,270**	**0.6**	1,931	0.6
Total	**$ 414,672**	**100.0**	$ 297,120	100.0

(a) As of January 1, 2018, the Company adopted ASU 2016-01 resulting in the reclassification of equity securities from available for sale securities to equity securities in the Consolidated Balance Sheet.

2021

The Company's investment portfolio increased during 2021 by $117.6 million. This growth was fueled by increases in deposits that were driven by customers held more cash and government stimulus efforts that occurred during 2021. During 2021, we purchased $108.4 million of U.S. Treasuries, $20.6 million of U.S. agencies, $56.6 million of mortgage backed securities, $18.6 million of state and local obligations and $7.0 million of corporate obligations, which helped to offset the $28.8 million of principal repayments and $26.7 million of calls and maturities that occurred during the year. We also sold $29.2 million of bonds at a net gain of $212,000. The fair value of our investment portfolio decreased approximately $7.3 million in 2021 due to interest rate fluctuations, net of equity market gains. Excluding our short term investments consisting of monies held primarily at the Federal Reserve, the effective yield on our investment portfolio for 2021 was 1.96% compared to 2.55% for 2020 on a tax equivalent basis.

Interest rates rose during 2021 in response to shifting expectations for fiscal policy and an enduring pandemic that continued to hamper economic activity, strengthening and prolonging unusually strong inflationary pressures and altering the expected path of monetary policy. The upper movement in interest rates, however, unfolded across the maturity spectrum at different times during the year. Longer yields peaked at the end of the first quarter, propelled higher by the rollout of vaccines and expectations for more stimulative fiscal policy. The central bank's official forecast from March 2021 for rates to remain near zero for the next several years gave way to a call by December to raise the federal funds target rate range by 1.50% by the end of 2023. Federal funds futures contracts, which began the year flat across the forecast horizon, reflected a presumption for three 25-basis point rate hikes in 2022 and two more in 2023. The 2-year Treasury yield traded within a range of 0.10% to 0.19% from January 1 through the Federal Reserve's June 15 meeting, was bounded between 0.17% and 0.27% from mid-June to the September 22 meeting, but climbed steeply in the fourth quarter to 0.73% by year's end. Along a similar timeline, the 5-year Treasury yield rose from a low of 0.35% in early January to 1.26% by the end of the year. Despite historic inflation readings in the second half of the year, concerns that the abrupt policy shift by the Federal Reserve to fight inflation raised the risk of a policy error that could disrupt the recovery kept longer yields in check. The 10-year yield failed to eclipse its March high and finished the year at 1.51%. The timing differences of rate changes across the curve had a noticeable and informative impact on the shape of the curve throughout the year. The spread between the 2-year and 10-year Treasury yields expanded from 0.79% on January 1, 2021 to a peak of 1.58% on March 31, 2021. Stepping lower in stages for the remainder of the year, the spread tightened back to 0.77% by the end of 2021. The investment strategy for 2021 has been to utilize cashflows from the investment portfolio and deposit inflows to purchase US treasury securities, mortgage backed securities in government sponsored entities and obligations of state and political securities, as well as US agency securities. The increase in the investment portfolio was in response to growth in deposits that exceeds organic loan opportunities. We continually monitor interest rate trading ranges and try to focus purchases to times when rates are in the top third of the trading range. The Company believes its investment strategy has appropriately mitigated its interest rate risk exposure if rates rise while providing sufficient cashflows for the Company's liquidity needs.

At December 31, 2021, the Company did not own any securities, other than government-sponsored and government-guaranteed mortgage-backed securities, that had an aggregate book value in excess of 10% of its consolidated stockholders' equity at that date.

The expected principal repayments at amortized cost and average weighted yields for the investment portfolio (excluding equity securities) as of December 31, 2021, are shown below (dollars in thousands). Expected principal repayments, which include prepayment speed assumptions for mortgage-backed securities, are significantly different than the contractual maturities detailed in Note 4 of the consolidated financial statements. Yields on tax-exempt securities are presented on a fully taxable equivalent basis, assuming a 21% tax rate, which was the rate in effect at December 31, 2021.

	One Year or Less		After One Year to Five years		After Five Years to Ten Years		After Ten Years		Total	
	Amortized Cost	Yield %	Amortized Cost	Yield %	Amortized Cost	Yield %	Amortized Cost	Yield %	Amortized Cost	Yield %
Available-for-sale securities:										
U.S. agency securities	$ 22,706	1.5	$ 35,145	2.1	$ 15,952	1.3	$ -	-	$ 73,803	1.7
U.S. treasuries	8,491	2.1	64,808	0.8	43,444	1.1	-	-	116,743	1.0
Obligations of state & political subdivisions	8,173	2.9	53,597	2.1	47,597	1.9	-	-	109,367	2.0
Corporate obligations	-	-	10,378	3.6	-	-	-	-	10,378	3.6
Mortgage-backed securities	24,439	1.0	35,965	1.5	31,142	1.4	10,181	1.4	101,727	1.3
Total available-for-sale	$ 63,809	1.6	$ 199,893	1.6	$ 138,135	1.4	$ 10,181	1.4	$ 412,018	1.6

At December 31, 2021, approximately 64.0% of the amortized cost of debt securities is expected to mature, call or pre-pay within five years or less. The Company expects that earnings from operations, the levels of cash held at the Federal Reserve and other correspondent banks, the high liquidity level of the available-for-sale securities, growth of deposits and the availability of borrowings from the Federal Home Loan Bank and other third party banks will be sufficient to meet future liquidity needs.

Loans Held for Sale

Loans held for sale decreased $10.1 million to $4.6 million as of December 31, 2021 from December 31, 2020. The decrease in loans held for sale was due to the amount of refinancings occurring due to the low rate environment in the fourth quarter of 2020 compared to 2021.

Loans

The Bank's lending efforts have historically focused on north central Pennsylvania and southern New York. With the acquisition of FNB and the opening of offices in Lancaster County, this focus has grown to include Lebanon, Schuylkill, Berks and Lancaster County markets of south central, Pennsylvania. We have a limited branch office in Union County that is staffed by a lending team to primarily support agricultural opportunities and offices in State College and Mill Hall to support commercial opportunities in central Pennsylvania, especially Centre and Clinton Counties. In April 2020, we completed the MidCoast acquisition, which expanded our markets into the State of Delaware with activity centered around the cities of Wilmington and Dover, Delaware. In November of 2020, we opened a branch in Kennett Square, Pennsylvania, to further serve customers obtained as part of the MidCoast acquisition, as well as to expand operations into Chester County, Pennsylvania.

We originate loans primarily through direct loans to our existing customer base, with new customers generated through the strong relationships that our lending teams have with their customers, as well as by referrals from real estate brokers, building contractors, attorneys, accountants, corporate and advisory board members, existing customers and the Bank's website. The Bank offers a variety of loans, although historically most of our lending has focused on real estate loans including residential, commercial, agricultural, and construction loans. As of December 31, 2021, approximately 87.1% of our loan portfolio consisted of real estate loans. All lending is governed by a lending policy that is developed and administered by management and approved by the Board of Directors.

The Bank primarily offers fixed rate residential mortgage loans with terms of up to 25 years and adjustable rate mortgage loans (with amortization schedules up to 30 years) with interest rates and payments that adjust based on one, three, five and 15 year fixed periods. Loan to value ratios are usually 80% or less with exceptions for individuals with excellent credit and low debt to income and/or high net worth. Adjustable rate mortgages are tied to a margin above the comparable Federal Home Loan Bank of Pittsburgh borrowing rate. Home equity loans are written with terms of up to 15 years at fixed rates. Home equity lines of credit are variable rate loans tied to the Prime Rate generally with a ten year draw period followed by a ten year repayment period. Home equity loans are typically written with a maximum 80% loan to value.

Commercial real estate loan terms are generally 20 years or less, with one to five year adjustable interest rates. The adjustable rates are typically tied to a margin above the comparable Federal Home Loan Bank of Pittsburgh borrowing rate with a typical loan to value ratio of 80% or less. During 2021 and 2020, the Bank offered certain customers derivative contracts that allowed the customer to obtain a fixed interest rate for a period up to 10 years. Where feasible, the Bank participates in the United States Department of Agriculture's (USDA) and Small Business Administration (SBA) guaranteed loan programs to offset credit risk and to further promote economic growth in our market area.

Agriculture is an important industry throughout our market areas. Therefore, the Bank has not only developed an agriculture lending team with significant experience that has a thorough understanding of this industry, but also continually looks for additional employees with a thorough understanding of agriculture. We have an agricultural loan policy to assist in underwriting agricultural loans. Agricultural loans are made to a diversified customer base that include dairy, swine and poultry farmers and their support businesses. Agricultural loans focus on character, cash flow and collateral, while also considering the particular risks of the industry. Loan terms are generally 20 years or less, with one to five year adjustable interest rates. The adjustable rates are typically tied to a margin above the comparable Federal Home Loan Bank of Pittsburgh borrowing rate with a typical loan to value of less than 80%. We evaluate the financial strength of the integrators we have exposure to with our poultry and swine agricultural customers. The Bank is a preferred lender under the USDA's Farm Service Agency (FSA) and participates in the FSA guaranteed loan program.

The Bank, as part of its commitment to the communities it serves, is an active lender for projects by our local municipalities and school districts. These loans range from short term bridge financing to 20 year term loans for specific projects. These loans are typically written at rates that adjust at least every five years. Due to the size of certain municipal loans, we have developed participation lending relationships with other community banks that allow us to meet regulatory compliance issues, while meeting the needs of the customer. At December 31, 2021, the aggregate balance of our participation loans, in which a portion was sold to other lender's totaled $157.5 million, of which $90.9 million was sold.

Activity associated with exploration for natural gas in 2021 was slightly higher than 2020. Certain entities drilled new wells and created new pad sites and pipelines, while other companies only maintained their existing wells. Natural gas prices increased during 2021, but still experienced significant volatility in 2021. While the Bank has loaned to companies that service the exploration activities, the Bank did not originate any loans to companies performing the actual drilling and exploration activities. Loans made by the Company were to service industry customers which included trucking companies, stone quarries and other support businesses. We also originated loans to businesses and individuals for restaurants, hotels and apartment rentals that were developed and expanded to meet the housing and living needs of the gas workers. Due to our understanding of the industry and its cyclical nature, the loans made for natural gas-related activities were originated in a prudent and cautious manner and were subject to specific policies and procedures for lending to these entities, which included lower loan to value thresholds, shortened amortization periods, and expansion of our monitoring of loan concentrations associated with this activity.

The following table shows the year-end composition of the loan portfolio for the five years ended December 31 (dollars in thousands):

	2021		2020	
	Amount	**%**	Amount	%
Real estate:				
Residential	**$ 201,097**	**14.0**	$ 201,911	14.4
Commercial	**687,338**	**47.7**	596,255	42.4
Agricultural	**312,011**	**21.6**	315,158	22.4
Construction	**55,036**	**3.8**	35,404	2.5
Consumer	**25,858**	**1.8**	30,277	2.2
Other commercial loans	**74,585**	**5.2**	114,169	8.1
Other agricultural loans	**39,852**	**2.8**	48,779	3.5
State & political subdivision loans	**45,756**	**3.1**	63,328	4.5
Total loans	**1,441,533**	**100.0**	1,405,281	100.0
Less allowance for loan losses	**17,304**		15,815	
Net loans	**$ 1,424,229**		$ 1,389,466	

	2021/2020 Change Amount	%
Real estate:		
Residential	**$ (814)**	**(0.4)**
Commercial	**91,083**	**15.3**
Agricultural	**(3,147)**	**(1.0)**
Construction	**19,632**	**55.5**
Consumer	**(4,419)**	**(14.6)**
Other commercial loans	**(39,584)**	**(34.7)**
Other agricultural loans	**(8,927)**	**(18.3)**
State & political subdivision loans	**(17,572)**	**(27.7)**
Total loans	**$ 36,252**	**2.6**

2021

Total loans grew $36.3 million in 2021 and total $1.44 billion at the end of 2021. The primary driver of growth during 2021 was growth in commercial real estate in the Delaware market. This growth was offset by a decrease in other commercial loans of $39.6 million due to a decrease in PPP loans due to forgiveness and repayments of $30.4 million and $17.6 million in state and political subdivision loans due to customers refinancing on the bond market due to the low interest rate environment.

Residential real estate loans decreased $814,000 even as refinancing activity remained high in 2021, some of which met the requirements of the secondary market and were subsequently sold. During 2021, $44.7 million of residential real estate loans were originated for sale on the secondary market, which compares to $88.0 million for 2020. For loans sold on the secondary market, the Company recognizes fee income for servicing these sold loans, which is included in non-interest income.

The following table presents the maturity distribution of our loan portfolio as of December 31, 2021 (in thousands). The table does not include any estimate of prepayments which significantly shorten the average life of all loans and may cause our actual repayment experience to differ from that shown below. Demand loans having no stated schedule of repayments and no stated maturity are reported as due in one year or less.

	Due in One year or less	After one year but within five years	After five years through fifteen years	After fifteen years	Total
Real estate:					
Residential	$ 509	$ 6,807	$ 80,496	$ 113,285	$ 201,097
Commercial	28,666	151,485	331,361	175,826	687,338
Agricultural	4,128	18,871	135,297	153,715	312,011
Construction	983	16,488	26,954	10,611	55,036
Consumer	20,724	1,868	3,110	156	25,858
Other commercial loans	2,304	38,973	8,975	24,333	74,585
Other agricultural loans	1,673	15,557	4,112	18,510	39,852
State & political subdivision loans	732	1,742	16,977	26,305	45,756
	$ 59,719	$ 251,791	$ 607,282	$ 522,741	$ 1,441,533

The following table presents the portion of loans that have fixed interest rates or variable interest rates that fluctuate over the life of loans in accordance with changes in the interest rate index that mature after December 31, 2022.

Sensitivity of loans to changes in interest rates - loans due after December 31, 2022:	Predetermined interest rate	Floating or adjustable interest rate	Total
Real estate:			
Residential	$ 110,252	$ 90,336	$ 200,588
Commercial	259,144	399,528	658,672
Agricultural	15,907	291,976	307,883
Construction	23,167	30,886	54,053
Consumer	4,839	295	5,134
Other commercial loans	30,358	41,923	72,281
Other agricultural loans	10,109	28,070	38,179
State & political subdivision loans	29,893	15,131	45,024
	$ 483,669	$ 898,145	$ 1,381,814

Allowance for Loan Losses and Credit Quality Risk

The allowance for loan losses is maintained at a level which, in management's judgment, is adequate to absorb probable future loan losses inherent in the loan portfolio. The provision for loan losses is charged against current income. Loans deemed not collectable are charged-off against the allowance while subsequent recoveries increase the allowance. The allowance for loan losses was $17,304,000 or 1.20% of total loans as of December 31, 2021 as compared to $15,815,000 or 1.13% of loans as of December 31, 2020. The $1,489,000 increase is a result of a $1,550,000 provision for loan losses less net charge-offs of $61,000. During 2021, net charge-offs were low with no significant charge-offs occurring. The following table shows the distribution of the allowance for loan losses and the percentage of loans compared to total loans by loan category (dollars in thousands) as of December 31:

	2021 Amount	**%**	2020 Amount	%
Real estate loans:				
Residential	**$ 1,147**	**14.0**	$ 1,174	14.4
Commercial	**8,099**	**47.7**	6,216	42.4
Agricultural	**4,729**	**21.6**	4,953	22.4
Construction	**434**	**3.8**	122	2.5
Consumer	**262**	**1.8**	321	2.2
Other commercial loans	**1,023**	**5.2**	1,226	8.1
Other agricultural loans	**558**	**2.8**	864	3.5
State & political subdivision loans	**281**	**3.1**	479	4.5
Unallocated	**771**	**N/A**	460	N/A
Total allowance for loan losses	**$ 17,304**	**100.0**	$ 15,815	100.0

The following table provides information related to credit loss experience and net (charge-offs) recoveries for 2021, 2020 and 2019.

2021	Credit Loss Expense (Benefit)	Net (charge-offs) Recoveries	Average Loans	Ratio of net (charge-offs) recoveries to Average loans	Allowance to total loans	Non-accrual loans as a percent of loans	Allowance to total non-accrual loans
Real estate:							
Residential	**$ (27)**	**-**	**$ 203,062**	**0.00%**	**0.57%**	**0.30%**	**192.77%**
Commercial	**1,848**	**35**	**639,161**	**0.01%**	**1.18%**	**0.43%**	**275.01%**
Agricultural	**(224)**	**-**	**312,770**	**0.00%**	**1.52%**	**1.00%**	**150.94%**
Construction	**312**	**-**	**56,315**	**0.00%**	**0.79%**	**0.00%**	**NA**
Consumer	**(53)**	**(6)**	**24,125**	**(0.02%)**	**1.01%**	**0.00%**	**NA**
Other commercial loans	**(113)**	**(90)**	**99,839**	**(0.09%)**	**1.37%**	**0.19%**	**730.71%**
Other agricultural loans	**(306)**	**-**	**37,181**	**0.00%**	**1.40%**	**2.01%**	**69.49%**
State & political subdivision loans	**(198)**	**-**	**52,804**	**0.00%**	**0.61%**	**0.00%**	**NA**
Unallocated	**311**	**-**	**-**	**NA**	**NA**	**NA**	**NA**
Total	**$ 1,550**	**$ (61)**	**$ 1,425,257**	**0.00%**	**1.20%**	**0.53%**	227.21%

2020	Credit Loss Expense (Benefit)	Net (charge-offs) Recoveries	Average Loans	Ratio of net (charge-offs) recoveries to Average loans	Allowance to total loans	Non-accrual loans as a percent of loans	Allowance to total non-accrual loans
Real estate:							
Residential	$ 46	14	$ 210,696	0.01%	0.58%	0.40%	144.58%
Commercial	2,065	(398)	478,415	(0.08%)	1.04%	0.76%	137.25%
Agricultural	(84)	15	311,100	0.00%	1.57%	0.99%	158.09%
Construction	79	-	26,343	0.00%	0.34%	0.00%	NA
Consumer	238	(29)	20,986	(0.14%)	1.06%	0.00%	NA
Other commercial loans	3	(32)	112,054	(0.03%)	1.07%	1.12%	95.48%
Other agricultural loans	(97)	-	46,101	0.00%	1.77%	2.00%	88.71%
State & political subdivision loans	(57)	-	86,143	0.00%	0.76%	0.00%	NA
Unallocated	207	-	-	NA	NA	NA	NA
Total	$ 2,400	$ (430)	$ 1,291,838	(0.03%)	1.13%	0.76%	147.36%

2019	Credit Loss Expense (Benefit)	Net (charge-offs) Recoveries	Average Loans	Ratio of net (charge-offs) recoveries to Average loans	Allowance to total loans	Non-accrual loans as a percent of loans	Allowance to total non-accrual loans
Real estate:							
Residential	$ 41	(32)	$ 215,749	(0.01%)	0.51%	0.44%	115.80%
Commercial	1,012	(578)	340,695	(0.17%)	1.33%	1.49%	89.55%
Agricultural	758	-	298,996	0.00%	1.61%	0.83%	194.80%
Construction	(15)	0	19,085	0.00%	0.28%	0.00%	NA
Consumer	8	(16)	9,684	(0.17%)	1.13%	0.06%	1866.67%
Other commercial loans	(71)	(28)	74,986	(0.04%)	1.79%	2.63%	68.32%
Other agricultural loans	269	(60)	45,590	(0.13%)	1.74%	1.95%	89.56%
State & political subdivision loans	(226)	-	97,780	0.00%	0.57%	0.00%	NA
Unallocated	(101)	-	-	NA	NA	NA	NA
Total	$ 1,675	$ (714)	$ 1,102,565	(0.06%)	1.24%	1.03%	120.02%

The Company believes it utilizes a disciplined and thorough loan review process based upon its internal loan policy approved by the Company's Board of Directors. The purpose of the review is to assess loan quality, analyze delinquencies, identify problem loans, evaluate potential charge-offs and recoveries, and assess general overall economic conditions in the markets served. An external independent loan review is performed on our commercial portfolio at least semi-annually for the Company. The external consultant is engaged to 1) review a minimum of 50% of the dollar volume of the commercial loan portfolio on an annual basis, 2) new loans originated for over $1.0 million in the last year, 3) a majority of borrowers with commitments greater than or equal to $1.0 million, 4) selected loan relationships over $750,000 which are over 30 days past due, or classified Special Mention, Substandard, Doubtful, or Loss, and 5) such other loans which management or the consultant deems appropriate. As part of this review, our underwriting process and loan grading system is evaluated.

Management believes it uses the best information available to make such determinations and that the allowance for loan losses is adequate as of December 31, 2021. However, future adjustments could be required if circumstances differ substantially from assumptions and estimates used in making the initial determination. A prolonged downturn in the economy, changes in the economies of various segments of our agricultural and commercial portfolios, high unemployment rates, significant changes in the value of collateral and delays in receiving financial information from borrowers could result in increased levels of non-performing assets, charge-offs, loan loss provisions and reduction in income. Additionally, bank regulatory agencies periodically examine the Bank's allowance for loan losses. The banking agencies could require the recognition of additions to the allowance for loan losses based upon their judgment of information available to them at the time of their examination.

On a monthly basis, problem loans are identified and updated primarily using internally prepared past due reports. Based on data surrounding the collection process of each identified loan, the loan may be added or deleted from the monthly watch list. The watch list includes loans graded special mention, substandard, doubtful, and loss, as well as additional loans that management may choose to include. Watch list loans are continually monitored going forward until satisfactory conditions exist that allow management to upgrade and remove the loan from the watchlist. In certain cases, loans may be placed on non-accrual status or charged-off based upon management's evaluation of the borrower's ability to pay. All commercial loans, which include commercial real estate, agricultural real estate, state and political subdivision loans, other commercial loans and other agricultural loans, on non-accrual are evaluated quarterly for impairment.

The adequacy of the allowance for loan losses is subject to a formal, quarterly analysis by management of the Company. In order to better analyze the risks associated with the loan portfolio, the entire portfolio is divided into several categories. As stated above, loans on non-accrual status are specifically reviewed for impairment and given a specific reserve, if appropriate. Loans evaluated and not found to be impaired are included with other performing loans, by category, by their respective homogenous pools. Three year average historical loss factors were calculated for each pool and applied to the performing portion of the loan category for each year presented. The historical loss factors for both reviewed and homogeneous pools are adjusted based upon the following qualitative factors:

- Level of and trends in delinquencies, impaired/classified loans
    - Change in volume and severity of past due loans

    - Volume of non-accrual loans
    - Volume and severity of classified, adversely or graded loans
- Level of and trends in charge-offs and recoveries
- Trends in volume, terms and nature of the loan portfolio
- Effects of any changes in risk selection and underwriting standards and any other changes in lending and recovery policies, procedures and practices
- Changes in the quality of the Bank’s loan review system
- Experience, ability and depth of lending management and other relevant staff
- National, state, regional and local economic trends and business conditions
    - General economic conditions
    - Unemployment rates
    - Inflation / CPI
    - Changes in values of underlying collateral for collateral-dependent loans
- Industry conditions including the effects of external factors such as competition, legal, and regulatory requirements on the level of estimated credit losses.
- Existence and effect of any credit concentrations, and changes in the level of such concentrations
- Any change in the level of board oversight

See also “Note 5 – Loans and Related Allowance for Loan Losses” to the consolidated financial statements.

As a result of previous loss experiences and other risk factors utilized in determining the allowance, the Bank’s allocation of the allowance does not directly correspond to the actual balances of the loan portfolio. While commercial and agricultural real estate loans total 69.3% of the loan portfolio at December 31 2021, 74.1% of the allowance is assigned to these portions of the loan portfolio as these loans have more inherent risks than residential real estate or loans to state and political subdivisions. Residential real estate loans comprise 14.0% of the loan portfolio as of December 31, 2021 and 6.6% of the allowance is assigned to this segment as generally there are less inherent risks then commercial and agricultural loans.

The following table is a summary of our non-performing assets for the years ended December 31, 2021 and 2020. All non-accruing troubled debt restructurings (TDRs) are also included the non-accruing loans totals.

	2021	2020
Non-performing assets:		
Non-accruing loans	**$ 7,616**	$ 10,732
Accrual loans - 90 days or more past due	**46**	525
Total non-performing loans	**$ 7,662**	$ 11,257
Foreclosed assets held for sale	**1,180**	1,836
Total non-performing assets	**$ 8,842**	$ 13,093
Troubled debt restructurings (TDR)		
Non-accruing TDRs	**$ 4,295**	$ 7,026
Accrual TDRs	**6,810**	5,240
Total troubled debt restructurings	**$ 11,105**	$ 12,266

The following table identifies amounts of loans contractually past due 30 to 90 days and non-performing loans by loan category, as well as the change from December 31, 2020 to December 31, 2021 in non-performing loans (in thousands). Non-performing loans include those accruing loans that are contractually past due 90 days or more and non-accrual loans. Interest does not accrue on non-accrual loans. Subsequent cash payments received are applied to the outstanding principal balance or recorded as interest income, depending upon management's assessment of its ultimate ability to collect principal and interest.

	December 31, 2021				December 31, 2020			
		Non-Performing Loans				Non-Performing Loans		
	30 - 89 Days Past Due	90 Days Past Due Accruing	Non-accrual	Total Non-Performing	30 - 89 Days Past Due	90 Days Past Due Accruing	Non-accrual	Total Non-Performing
Real estate:								
Residential	$ 492	$ 13	$ 595	$ 608	$ 1,351	$ 275	$ 812	$ 1,087
Commercial	243	33	2,945	2,978	1,247	70	4,529	4,599
Agricultural	31	-	3,133	3,133	366	150	3,133	3,283
Construction	-	-	-	-	-	-	-	-
Consumer	163	-	-	-	155	30	-	30
Other commercial loans	28	-	140	140	930	-	1,284	1,284
Other agricultural loans	10	-	803	803	71	-	974	974
Total nonperforming loans	$ 967	$ 46	$ 7,616	$ 7,662	$ 4,120	$ 525	$ 10,732	$ 11,257

	Change in Non-Performing Loans 2021 / 2020	
	Amount	%
Real estate:		
Residential	$ (479)	(44.1)
Commercial	(1,621)	(35.2)
Agricultural	(150)	(4.6)
Construction	-	-
Consumer	(30)	(100.0)
Other commercial loans	(1,144)	(89.1)
Other agricultural loans	(171)	(17.6)
Total nonperforming loans	$ (3,595)	(31.9)

The Company has worked with customers directly affected by the COVID-19 pandemic. The Company has offered assistance in accordance with regulator guidelines. As a result of the current COVID-19 pandemic, the Company is engaging in more frequent communication with borrowers to better understand their situation and the challenges faced, allowing it to respond proactively as needs and issues arise. Should economic conditions worsen, the Company could experience increases in non-performing loans and further increases in its required allowance for loan losses and record additional provision expense. It is possible that the Company's asset quality measures could worsen at future measurement periods if the effects of the COVID-19 pandemic are prolonged.

For the year ended December 31, 2021, we recorded a provision for loan losses of $1,550,000 which compares to $2,400,000 for the same period in 2020, a decrease of $850,000. The decrease is primarily attributable to the impact that the COVID-19 pandemic had in 2020 on the national and local economies compared to 2021, as well as a decrease in organic loan growth in 2021 compared to 2020. Non-performing loans decreased $3.6 million from December 31, 2020 to December 31, 2021 with the decrease being primarily due to two customer relationships that paid off a $1.5 million of their relationships and additional relationships that returned to accrual status during 2021. At December 31, 2021, approximately 61.4% of the Bank’s non-performing loans are associated with the following three customer relationships:

- A commercial loan relationship with $1.3 million outstanding, and additional letters of credit of $1.7 million available, secured by undeveloped land, stone quarries and equipment, was on non-accrual status as of December 31, 2021. The Company services the natural gas industry, as well as local municipalities. As a result, the reduced exploration for natural gas in north central Pennsylvania has significantly impacted the cash flows of the customer, who provides excavation services and stone for pad construction related to these activities. During 2019, the Company had the underlying equipment collateral appraised. The 2019 appraisal indicated a decrease in collateral values compared to the appraisal ordered for the loan origination and an appraisal performed in 2017, however, the loan was still considered well secured on a loan to value basis at December 31, 2021. In 2021, the customer has liquidated some excess equipment and the funds have been utilized to pay down a portion of the loans. Management determined that no specific reserve was required as of December 31, 2021.The slowdown in the exploration for natural gas has significantly impacted the cash flows of the customer, who provides excavation services and stone for pad construction related to these activities. During 2019, the Company had the underlying equipment collateral appraised. The 2019 appraisal indicated a decrease in collateral values compared to the appraisal ordered for the loan origination and an appraisal performed in 2017, however, the loan is still considered well secured on a loan to value basis. In the fourth quarter of 2020, a forbearance agreement was signed with this customer. Management determined that no specific reserve was required as of December 31, 2021.

- An agricultural loan customer with a total loan relationship of $2.2 million, secured by real estate, equipment and cattle, was on non-accrual status as of December 31, 2021. The customer declared bankruptcy during the fourth quarter of 2018 and developed a workout plan that was approved by the bankruptcy court in the fourth quarter of 2019 and resulted in monthly payments resuming in late 2019 that continued in 2020 and 2021. Included within these loans to this customer are $792,000 of loans which are subject to Farm Service Agency guarantees. Depressed milk prices and the pandemic have created cash flow difficulties for this customer. Absent a sizable and sustained increase in milk prices, which is not assured, we will need to rely upon the collateral for repayment of interest and principal. During 2020, the Company had the underlying collateral appraised. Management determined that no specific reserve was required as of December 31, 2021.
- An agricultural loan customer with a total loan relationship of $1.2 million, secured by real estate was on non-accrual status as of December 31, 2021. The COVID-19 pandemic has escalated the cash flow difficulties this customer was experiencing. We expect that we will need to rely upon the collateral for repayment of interest and principal. Management reviewed the collateral and determined that no specific reserve was required as of December 31, 2021.

Management believes that the allowance for loan losses at December 31, 2021 was adequate at that date, which was based on the following factors:

- Three loan relationships comprise 61.4% of the non-performing loan balance, which did not require any specific reserves as of December 31, 2021.
- The Company has a history of low charge-offs, which were 0.00% and 0.03% of average loans for 2021 and 2020, respectively.

Bank Owned Life Insurance

The Company holds bank owned life insurance policies to offset current and future employee benefit costs. These policies provide the Bank with an asset that generates earnings to partially offset the current costs of benefits, and eventually (at the death of the insureds) provide partial recovery of cash outflows associated with the benefits. As of December 31, 2021 and 2020, the cash surrender value of the life insurance was $38.5 million and $32.6 million, respectively. The primary cause of the increase was the Bank purchased $7.8 million of additional insurance during 2021. During the first quarter of 2021, the Company received proceeds of $3,714,000, which included death benefits of $1,155,000 on two former employees of the Company. The change in cash surrender value, net of purchases and amounts acquired through acquisitions, is recognized in the results of operations. The amounts recorded as non-interest income totaled $1,828,000, $695,000 and $623,000 in 2021, 2020 and 2019, respectively with the increase due to the death benefits received in 2021. The Company evaluates annually the risks associated with the life insurance policies, including limits on the amount of coverage and an evaluation of the various carriers' credit ratings.

Effective January 1, 2015, the Company restructured its agreements so that any death benefits received from a policy while the insured person is an active employee of the Bank will be split with the beneficiary of the policy. Under the restructured agreements, the employee's beneficiary will be entitled to receive 50% of the net amount at risk from the proceeds. The policies acquired as part of the acquisition of MidCoast are only for the benefit of the Bank. The net amount at risk is the total death benefit payable less the cash surrender value of the policy as of the date of death. The policies acquired as part of the acquisition of FNB, provide a fixed dollar benefit for the beneficiary's' estate, which is dependent on several factors including whether the covered individual was a Director of FNB or an employee of FNB and their salary level. As of December 31, 2021 and 2020, included in other liabilities on the Consolidated Balance sheet is a liability of $696,000 and $687,000, respectively, for the obligation under the split-dollar benefit agreements.

Other Assets

2021

Other assets increased $3.4 million in 2021 to $22.8 million from $19.4 million in 2020. As a result of derivative transactions for the Company and customers, other assets increased $3.7 million. We extended several leases during the year, which resulted in the right of use asset for facilities increasing $978,000. As a result of the discount rates utilized for the pension plan, a pension asset was recorded of $792,000. Due to lower borrowing levels with FHLB of Pittsburgh, regulatory stock decreased $1.3 million during 2021. Foreclosed properties were sold during 2021, which resulted in a decrease to other assets of $656,000 million.

Deposits

The following table shows the breakdown of deposits by deposit type (dollars in thousands) at December 31:

	2021		2020		2019	
	Amount	**%**	Amount	%	Amount	%
Non-interest-bearing deposits	**$ 358,073**	**19.5**	$ 303,762	19.1	$ 203,793	16.9
NOW accounts	**485,292**	**26.4**	422,083	26.6	340,273	28.1
Savings deposits	**313,048**	**17.0**	255,853	16.1	224,456	18.5
Money market deposit accounts	**350,122**	**19.1**	225,968	14.2	169,865	14.0
Certificates of deposit	**329,616**	**18.0**	381,192	24.0	272,731	22.5
Total	**$ 1,836,151**	**100.0**	$ 1,588,858	100.0	$ 1,211,118	100.0

	2021/2020 Change		2020/2019 Change	
	Amount	**%**	Amount	%
Non-interest-bearing deposits	**$ 54,311**	**17.9**	$ 99,969	49.1
NOW accounts	**63,209**	**15.0**	81,810	24.0
Savings deposits	**57,195**	**22.4**	31,397	14.0
Money market deposit accounts	**124,154**	**54.9**	56,103	33.0
Certificates of deposit	**(51,576)**	**(13.5)**	108,461	39.8
Total	**$ 247,293**	**15.6**	$ 377,740	31.2

2021

Total deposits increased $247.3 million in 2021, or 15.6%. The driver of the increase was government stimulus funds in response to the COVID 19 pandemic, which included individuals, businesses and municipalities and all markets of Company. We continue to enhance our cash management services to improve our customer services and to grow deposits through our current customers. Brokered certificates of deposit decreased $23.8 million as maturing certificates were not replaced in 2021. As a percentage of total deposits, non-interest-bearing deposits totaled 19.5% as of the end of 2021, which compares to 19.1% at the end of 2020. The rates paid on certificates of deposit by the Company remain competitive with rates paid by our competition.

2020

Total deposits increased $377.7 million in 2020, or 31.2%. The primary driver of the growth was the MidCoast acquisition, in which $208.8 million of deposits were acquired. The remaining growth was driven by customers holding more cash as a result of the COVID-19 pandemic, and was experienced across all markets, which was facilitated by various government stimulus plans. As a percentage of total deposits, non-interest-bearing deposits totaled 19.1% as of the end of 2020, which compares to 16.9% at the end of 2019. As a result of market conditions in the first half of 2020, we issued long term brokered CD’s and had a balance of $23.8 million of brokered CD’s outstanding as of December 31, 2020 compared to $15.0 million as of December 31, 2019.

Remaining maturities of certificates of deposit in excess of FDIC insurance limits are as follows for December 31, 2021 (dollars in thousands):

3 months or less	**$ 9,464**
Over 3 months through 6 months	**7,424**
Over 6 months through 12 months	**27,422**
Over 12 months	**33,801**
Total	**$ 78,111**
As a percent of total certificates of deposit	**23.70%**

Uninsured deposits as of December 31, 2021 and 2020, are estimated based on regulatory reporting requirements to be $742,304,000 and $536,383,000, respectively.

Deposits by type of depositor are as follows (dollars in thousands) at December 31:

	2021		2020		2019	
	Amount	**%**	Amount	%	Amount	%
Individuals	**$ 938,331**	**51.1**	$ 865,041	54.4	$ 664,065	54.8
Businesses and other organizations	**534,402**	**29.1**	467,159	29.4	306,873	25.3
State & political subdivisions	**363,418**	**19.8**	256,658	16.2	240,180	19.9
Total	**$ 1,836,151**	**100.0**	$ 1,588,858	100.0	$ 1,211,118	100.0

Borrowed Funds

2021

Borrowed funds decreased $14.9 million during 2021 as a result of maturities and prepayments that occurred in 2021 that were not replaced due to deposit growth in 2021. Short term borrowings from the FHLB remained steady and totaled $25.0 million as of December 31, 2021 and 2020. Long term borrowings from the FHLB decreased $26.8 million and total $14.7 million. Term loans from the FHLB totaled $14.7 million and $41.5 million as of December 31, 2021 and 2020, respectively. The change in term loans was due to $21.8 million of term loans maturing during 2021 and prepaying an additional $5.0 million of term loans during 2021. In the second quarter of 2021, we issued $10.0 million of subordinated notes. (see Note 10 of the consolidated financial statements for additional information). Management continually monitors interest rates in order to minimize interest rate risk in future years and as part of this may extend some of the short term borrowings via term notes. The Bank has five interest rate swap agreements outstanding to convert floating-rate debt to fixed rate debt on notional amounts of $15.0 million, $10.0 million and three agreements of $6.0 million. The $15.0 million and $10.0 million were originated on April 1, 2020 and expire on April 1, 2025 and April 1, 2027. The three $6.0 million agreements originated on May 14, 2020 with a two year forward start date and expire on May 14, 2027, 2029 and 2032 The Company has an interest rate swap agreement outstanding that was entered into on April 13, 2020, to convert floating-rate debt to fixed rate debt on a notional amount of $7.5 million. The interest rate swap agreement expires on June 17, 2027. The interest rate swap instruments involve an agreement to receive a floating rate and pay a fixed rate, at specified intervals, calculated on the agreed-upon notional amounts. The differentials paid or received on interest rate swap agreements are recognized as adjustments to interest expense in the period. The fair value of the interest rate swaps at December 31, 2021 was $ 1,910,000 and is included within other assets on the consolidated balance sheets.

Other Liabilities

2021

Other liabilities increased $1.8 million to $20.5 million during 2021. We extended several leases during the year, which resulted in the right of use asset for facilities increasing $971,000. As a result of derivative transactions for the Company and customers, other liabilities increased $1.1 million. As a result of the discount rates utilized for the pension plan, the pension liability decreased $773,000. Employee benefit accruals, including profit sharing increased $624,000.

Stockholders' Equity

We evaluate stockholders' equity in relation to total assets and the risk associated with those assets. The greater our capital resources, the greater the likelihood of meeting our cash obligations and absorbing unforeseen losses. For these reasons, capital adequacy has been, and will continue to be, of paramount importance. Due to its importance, we develop a capital plan and stress test capital levels using various techniques and assumptions annually to ensure that in the event of unforeseen circumstances, we would remain in compliance with our capital plan approved by the Board of Directors and regulatory requirement levels.

Our Board of Directors determines our cash dividend rate after considering our capital requirements, current and projected net income, and other factors. In 2021 and 2020, the Company paid out 25.36% and 29.32% of net income in cash dividends, respectively.

As of December 31, 2021, the total number of common shares outstanding was 3,944,420. For comparative purposes, outstanding shares for prior periods were adjusted for the June 2021 stock dividend in computing earnings and cash dividends per share as detailed in Note 1 of the consolidated financial statements. During 2021, we purchased 23,390 shares of treasury stock at a weighted average cost of $58.74 per share. The Company awarded 4,660 shares of restricted stock to employees at a weighted average cost per share of $60.73 under an equity incentive plan. The Board of Directors was awarded 1,800 shares at a cost of $60.90 per share under an incentive plan.

2021

Stockholders' equity increased 9.4% in 2021 to $212.5 million. Excluding accumulated other comprehensive income (loss), stockholders' equity increased $21.0 million, or 10.9%., Net income for 2021 was $29.1 million, offset by net cash dividends of $7,383,000 and net treasury stock activity of $934,000. All of the Company's debt investment securities are classified as available-for-sale, making this portion of the Company's balance sheet more sensitive to the changing market value of investments. Accumulated other comprehensive income decreased $2,742,000 from December 31, 2020, primarily as result of the decrease in the fair market value of the investment portfolio. Total stockholders' equity was approximately 9.9% of total assets as of December 31, 2021, compared to 10.27% of total assets as of December 31, 2020.

LIQUIDITY

Liquidity is a measure of the Company's ability to efficiently meet normal cash flow requirements of both borrowers and depositors. Liquidity is needed to meet depositors' withdrawal demands, extend credit to meet borrowers' needs, provide funds for normal operating expenses and cash dividends, and fund future capital expenditures.

To maintain proper liquidity, we use funds management policies along with our investment and asset liability policies to assure we can meet our financial obligations to depositors, credit customers and stockholders. Management monitors liquidity by reviewing loan demand, investment opportunities, deposit pricing and the cost and availability of borrowing funds. Additionally, the bank has established various limits and ratios to monitor liquidity. On a quarterly basis, we stress test our liquidity position to ensure that the Bank has the capability of meeting its cash flow requirements in the event of unforeseen circumstances. The Company's historical activity in this area can be seen in the Consolidated Statement of Cash Flows from investing and financing activities.

Cash generated by operating activities, investing activities and financing activities influences liquidity management. The most important source of funds is the deposits that are primarily core deposits (deposits from customers with other relationships). Short-term debt from the Federal Home Loan Bank supplements the Company's availability of funds as well as a line of credit arrangement with a corresponding bank. Other sources of short-term funds include brokered CDs and the sale of loans, if needed.

The Company's use of funds is shown in the investing activity section of the Consolidated Statement of Cash Flows, where the net loan activity is detailed. Other significant uses of funds are capital expenditures, purchase of loans and acquisition premiums. Surplus funds are then invested in investment securities.

Capital expenditures, including software purchases in 2021 totaled $1,105,000, which included:

- Operations building in Wellsboro, Pennsylvania totaling $753,000
- Vehicle purchases totaling $82,000
- ATM upgrades totaling $124,000
- Building and ground improvements totaling $96,000

Capital expenditures, including software purchases in 2020 totaled $942,000, which included:

- Teller and imaging software totaling $709,000
- Leasehold improvements and certain equipment for an office opened in 2020 totaling $73,000
- Building and ground improvements totaling $73,000
- Computer, network and copier upgrades totaling $76,000

We expect these expenditures will support our initiatives and will create operating efficiencies, while providing quality customer service.

In addition to the Bank's cash balances, the Bank achieves additional liquidity primarily from its investment in the FHLB of Pittsburgh and the resulting borrowing capacity obtained through this investment, investments that mature in less than one year and expected principal repayments from mortgage backed securities. The Bank has a maximum borrowing capacity at the Federal Home Loan Bank of approximately $756.2 million, inclusive of any outstanding amounts, as a source of liquidity. The Bank also has two federal funds line with third party providers in the total amount of $34.0 million as of December 31, 2021, which is unsecured and a borrower in custody agreement was established with the FRB in the amount of $1.1 million, which is collateralized by $1.7 million of municipal loans.

The Company is a separate legal entity from the Bank and must provide for its own liquidity. In addition to its operating expenses, the Company is responsible for paying any dividends declared to its shareholders. The Company also has repurchased shares of its common stock. The Company's primary source of income is dividends received from the Bank. The Bank may not declare a dividend without approval of the FRB, unless the dividend to be declared by the Bank's Board of Directors does not exceed the total of: (i) the Bank's net profits for the current year to date, plus (ii) its retained net profits for the preceding two current years, less any required transfers to surplus. In addition, the Bank can only pay dividends to the extent that its retained net profits (including the portion transferred to surplus) exceed its bad debts. The FRB, the OCC, the PDB and the FDIC have formal and informal policies which provide that insured banks and bank holding companies should generally pay dividends only out of current operating earnings, with some exceptions. The Prompt Corrective Action Rules, described above, further limit the ability of banks to pay dividends, because banks which are not classified as well capitalized or adequately capitalized may not pay dividends and no dividend may be paid which would make the Bank undercapitalized after the dividend. At December 31, 2021, the Company (unconsolidated basis) had liquid assets of $15.0 million.

CONTRACTUAL OBLIGATIONS

The Company has various financial obligations, including contractual obligations which may require cash payments. The following table (in thousands) presents as of December 31, 2021, significant fixed and determinable contractual obligations to third parties by payment date. Further discussion of the obligations can be found in Notes 9, 10 and 18 to the Consolidated Financial Statements.

Contractual Obligations	One year or Less	One to Three Years	Three to Five Years	Over Five Years	Total
Deposits without a stated maturity	$ 1,506,535	$ -	$ -	$ -	$ 1,506,535
Time deposits	184,857	110,741	28,251	5,767	329,616
FHLB Advances	-	-	-	-	-
Term borrowings - FHLB	29,725	-	10,000	-	39,725
Note Payable	-	-	-	7,500	7,500
Subordinated Debt	-	-	-	10,000	10,000
Repurchase agreements	16,872	-	-	-	16,872
Operating leases	672	1,117	824	851	3,464
Total	$ 1,738,661	$ 111,858	$ 39,075	$ 24,118	$ 1,913,712

OFF-BALANCE SHEET ARRANGEMENTS

In the normal course of operations, we engage in a variety of financial transactions that, in accordance with generally accepted accounting principles are not recorded in our financial statements. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are used primarily to manage customers' requests for funding and take the form of loan commitments, unused lines of credit and letters of credit. For information about our loan commitments, unused lines of credit and letters of credit, see Note 16 of the notes to consolidated financial statements.

For the year ended December 31, 2021, we did not engage in any off-balance sheet transactions reasonably likely to have a material effect on our financial condition, results of operations or cash flows.

INTEREST RATE AND MARKET RISK MANAGEMENT

The objective of interest rate sensitivity management is to maintain an appropriate balance between the stable growth of income and the risks associated with maximizing income through interest sensitivity imbalances and the market value risk of assets and liabilities.

Because of the nature of our operations, we are not subject to foreign currency exchange or commodity price risk and, since the Company has no trading portfolio, it is not subject to trading risk.

At December 31, 2021, the Company had equity securities that represent only 0.6% of our investment portfolio, and therefore market risk related to equity securities is not significant.

The primary factors that make assets interest-sensitive include adjustable-rate features on loans and investments, loan repayments, investment maturities and money market investments. The primary components of interest-sensitive liabilities include maturing certificates of deposit, IRA certificates of deposit, repurchase agreements and short-term borrowings. Savings deposits, NOW accounts and money market investor accounts, with the exception of top interest tier money market and NOW accounts, are considered core deposits and are not short-term interest sensitive and therefore are included in the table below in the over five year column. Top interest tier money market and NOW accounts are included in the table below in the within three month column. Borrowings subject to swap arrangements are included in the table below based on the swap arrangement maturity.

The following table shows the cumulative static gap (at amortized cost) for various time intervals (dollars in thousands):

Maturity or Re-pricing of Company Assets and Liabilities as of December 31, 2021

	Within Three Months	Four to Twelve Months	One to Two Years	Two to Three Years	Three to Five Years	Over Five Years	Total
Interest-earning assets:							
Interest-bearing deposits at banks	$ 159,776	$ 6,950	$ 2,832	$ 250	$ -	$ -	$ 169,808
Investment securities	24,969	38,751	36,358	50,385	117,923	143,632	412,018
Residential mortgage loans	35,868	48,987	40,557	28,468	29,979	17,238	201,097
Construction loans	15,505	19,404	20,127	-	-	-	55,036
Commercial and farm loans	261,250	202,084	182,913	121,197	264,803	81,539	1,113,786
Loans to state & political subdivisions	8,077	3,920	3,563	4,277	13,496	12,423	45,756
Other loans	3,062	4,845	4,969	3,589	4,394	4,999	25,858
Total interest-earning assets	$ 508,507	$ 324,941	$ 291,319	$ 208,166	$ 430,595	$ 259,831	$ 2,023,359
Interest-bearing liabilities:							
NOW accounts	$ 314,959	$ -	$ -	$ -	$ -	$ 170,333	$ 485,292
Savings accounts	-	-	-	-	-	313,048	313,048
Money Market accounts	324,189	-	-	-	-	25,933	350,122
Certificates of deposit	53,247	131,610	68,192	42,549	28,251	5,767	329,616
Long-term borrowing	21,598	-	-	10,000	24,879	17,500	73,977
Total interest-bearing liabilities	$ 713,993	$ 131,610	$ 68,192	$ 52,549	$ 53,130	$ 532,581	$ 1,552,055
Excess interest-earning assets (liabilities)	$ (205,486)	$ 193,331	$ 223,127	$ 155,617	$ 377,465	$ (272,750)	
Cumulative interest-earning assets	$ 508,507	$ 833,448	$ 1,124,767	$ 1,332,933	$ 1,763,528	$ 2,023,359	
Cumulative interest-bearing liabilities	713,993	845,603	913,795	966,344	1,019,474	1,552,055	
Cumulative gap	$ (205,486)	$ (12,155)	$ 210,972	$ 366,589	$ 744,054	$ 471,304	
Cumulative interest rate sensitivity ratio (1)	0.71	0.99	1.23	1.38	1.73	1.30	

The previous table and the simulation models discussed below are presented assuming money market investment accounts and NOW accounts in the top interest rate tier are re-priced within the first three months. The loan amounts reflect the principal balances expected to be re-priced as a result of contractual amortization and anticipated early payoffs.

Gap analysis, one of the methods used by us to analyze interest rate risk, does not necessarily show the precise impact of specific interest rate movements on the Bank's net interest income because the re-pricing of certain assets and liabilities is discretionary and is subject to competition and other pressures. In addition, assets and liabilities within the same period may, in fact, be repaid at different times and at different rate levels. We have not experienced the kind of earnings volatility that might be indicated from gap analysis.

The Bank currently uses a computer simulation model to better measure the impact of interest rate changes on net interest income. We use the model as part of our risk management and asset liability management processes that we believe will effectively identify, measure, and monitor the Bank's risk exposure. In this analysis, the Bank examines the results of movements in interest rates with additional assumptions made concerning the timing of interest rate changes, prepayment speeds on mortgage loans and mortgage securities and deposit pricing movements. Shock scenarios, which assume a parallel shift in interest rates and is instantaneous, typically have the greatest impact on net interest income. The following is a rate shock analysis and the impact on net interest income as of December 31, 2021 (dollars in thousands):

Changes in Rates	Prospective One-Year Net Interest Income	Change in Prospective Net Interest Income	% Change in Prospective Net Interest Income
-100 Shock	61,171	(1,093)	(1.76)
Base	62,264	-	-
+100 Shock	62,260	(4)	(0.01)
+200 Shock	63,644	1,380	2.22
+300 Shock	64,512	2,248	3.61
+400 Shock	65,184	2,920	4.69

The model makes estimates, at each level of interest rate change, regarding cash flows from principal repayments on loans and mortgage backed securities, call activity of other investment securities, and deposit selection, re-pricing and maturity structure. Because of these assumptions, actual results could differ significantly from these estimates which would result in significant differences in the calculated projected change on net interest income. Additionally, the changes above do not necessarily represent the level of change under which management would undertake specific measures to realign its portfolio in order to reduce the projected level of change. The projections above utilize a static balance sheet and do not include any changes that may result from the growth of the Bank. Management has developed policy limits for acceptable changes in net interest income for multiple scenarios, including shock scenarios. As of December 31, 2021, changes in net interest income projected for all scenarios, including the shock scenarios noted above are in line with Bank policy limits for interest rate risk.

CRITICAL ACCOUNTING POLICIES; CRITICAL ACCOUNTING ESTIMATES

The Company's accounting policies are integral to understanding the results reported. The accounting policies are described in detail in Note 1 of the consolidated financial statements. Our most complex accounting policies require management's judgment to ascertain the valuation of assets, liabilities, commitments and contingencies. We have established detailed policies and control procedures that are intended to ensure valuation methods are well controlled and applied consistently from period to period. In addition, the policies and procedures are intended to ensure that the process for changing methodologies occurs in an appropriate manner. The following is a brief description of our current accounting policies involving significant management valuation judgments and critical accounting estimates.

Other than Temporary Impairment

All securities are evaluated periodically to determine whether a decline in their value is other than temporary and is a matter of judgment. For debt securities, management considers whether the present value of cash flows expected to be collected are less than the security's amortized cost basis (the difference defined as the credit loss), the magnitude and duration of the decline, the reasons underlying the decline and the Company's intent to sell the security or whether it is more likely than not that the Company would be required to sell the security before its anticipated recovery in market value, to determine whether the loss in value is other than temporary. Once a decline in value is determined to be other than temporary, if the Company does not intend to sell the security, and it is more-likely-than-not that it will not be required to sell the security, before recovery of the security's amortized cost basis, the charge to earnings is limited to the amount of credit loss. Any remaining difference between fair value and amortized cost (the difference defined as the non-credit portion) is recognized in other comprehensive income, net of applicable taxes. Otherwise, the entire difference between fair value and amortized cost is charged to earnings.

Allowance for Loan Losses

Arriving at an adequate level of allowance for loan losses involves a high degree of judgment. The Company's allowance for loan losses provides for probable losses based upon evaluations of known and inherent risks in the loan portfolio.

Management uses historical information to assess the adequacy of the allowance for loan losses as well as the prevailing business environment; as it is affected by changing economic conditions and various external factors, which may impact the portfolio in ways currently unforeseen. This evaluation is inherently subjective as it requires significant estimates that may be susceptible to significant change, subjecting the Bank to volatility of earnings. The allowance is increased by provisions for loan losses and by recoveries of loans previously charged-off and reduced by loans charged-off. For a full discussion of the Company's methodology of assessing the adequacy of the allowance for loan losses, refer to Note 1 of the consolidated financial statements.

Goodwill and Other Intangible Assets

As discussed in Note 1 of the consolidated financial statements, the Company performs an evaluation of goodwill for impairment on an annual basis, or more frequently if events or changes in circumstances indicate that the asset might be impaired. The Company performed a qualitative assessment to determine whether it is more likely than not that the fair value of the reporting unit is less than its carrying value. Based on the fair value of the reporting unit, no impairment of goodwill was recognized in 2021, 2020 or 2019.

Pension Benefits

Pension costs and liabilities are dependent on assumptions used in calculating such amounts. These assumptions include discount rates, benefits earned, interest costs, expected return on plan assets, mortality rates, and other factors. In accordance with GAAP, actual results that differ from the assumptions are accumulated and amortized over future periods and, therefore, generally affect recognized expense and the recorded obligation of future periods. While management believes that the assumptions used are appropriate, differences in actual experience or changes in assumptions may affect the Company's pension obligations and future expense. Our pension benefits are described further in Note 11 of the "Notes to Consolidated Financial Statements."

Deferred Tax Assets

We use an estimate of future earnings to support our position that the benefit of our deferred tax assets will be realized. If future income should prove non-existent or less than the amount of the deferred tax assets within the tax years to which they may be applied, the asset may not be realized and our net income will be reduced. Management also evaluates deferred tax assets to determine if it is more likely than not that the deferred tax benefit will be utilized in future periods. If not, a valuation allowance is recorded. Our deferred tax assets are described further in Note 12 of the consolidated financial statements.

Business Combinations

Business combinations are accounted for by applying the acquisition method. As of acquisition date, the identifiable assets acquired and liabilities assumed are measured at fair value and recognized separately from goodwill. Results of operations of the acquired entities are included in the consolidated statement of income from the date of acquisition. The calculation of intangible assets including core deposits and the fair value of loans are based on significant judgements. Core deposits intangibles are calculated using a discounted cash flow model based on various factors including discount rate, attrition rate, interest rate, cost of alternative funds and net maintenance costs.

Loans acquired in connection with acquisitions are recorded at their acquisition-date fair value with no carryover of related allowance for credit losses. Any allowance for loan loss on these pools reflect only losses incurred after the acquisition (meaning the present value of all cash flows expected at acquisition that ultimately are not to be received). Determining the fair value of the acquired loans involves estimating the principal and interest cash flows expected to be collected on the loans and discounting those cash flows at a market rate of interest. Management considers a number of factors in evaluating the acquisition-date fair value including the remaining life of the acquired loans, delinquency status, estimated prepayments, payment options and other loan features, internal risk grade, estimated value of the underlying collateral and interest rate environment.

ITEM 7A – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

This information is included under Item 7, "*Management's Discussion and Analysis of Financial Condition and Results of Operations – Interest Rate and Market Risk Management*", appearing in this Annual Report on Form 10-K.

ITEM 8 - FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

Citizens Financial Services, Inc.
Consolidated Balance Sheet

	December 31,			
(in thousands, except share data)		**2021**		2020
ASSETS:				
Cash and cash equivalents:				
Noninterest-bearing	**$**	**14,051**	$	16,374
Interest-bearing		**158,782**		52,333
Total cash and cash equivalents		**172,833**		68,707
Interest bearing time deposits with other banks		**11,026**		13,758
Equity securities		**2,270**		1,931
Available-for-sale securities		**412,402**		295,189
Loans held for sale		**4,554**		14,640
Loans (net of allowance for loan losses: 2021, $17,304; 2020, $15,815)		**1,424,229**		1,389,466
Premises and equipment		**17,016**		16,948
Accrued interest receivable		**5,235**		5,998
Goodwill		**31,376**		31,376
Bank owned life insurance		**38,503**		32,589
Other intangibles		**1,627**		1,668
Other assets		**22,792**		19,404
TOTAL ASSETS	**$**	**2,143,863**	$	1,891,674
LIABILITIES:				
Deposits:				
Noninterest-bearing	**$**	**358,073**	$	303,762
Interest-bearing		**1,478,078**		1,285,096
Total deposits		**1,836,151**		1,588,858
Borrowed funds		**73,977**		88,838
Accrued interest payable		**711**		1,017
Other liabilities		**20,532**		18,702
TOTAL LIABILITIES		**1,931,371**		1,697,415
STOCKHOLDERS' EQUITY:				
Preferred Stock $1.00 par value; authorized 3,000,000 shares 2021 and 2020; none issued in 2021 or 2020		**-**		-
Common Stock				
$1.00 par value; authorized 25,000,000 shares 2021 and 2020; issued 4,388,901 and 4,350,342 shares in 2021 and 2020, respectively		**4,389**		4,350
Additional paid-in capital		**78,395**		75,908
Retained earnings		**146,010**		126,627
Accumulated other comprehensive income (loss)		**(155)**		2,587
Treasury stock, at cost:				
444,481 and 428,492 shares for 2021 and 2020, respectively		**(16,147)**		(15,213)
TOTAL STOCKHOLDERS' EQUITY		**212,492**		194,259
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	**$**	**2,143,863**	$	1,891,674

See accompanying notes to consolidated financial statements.

Citizens Financial Services, Inc.
Consolidated Statement of Income
Year Ended December 31,

(in thousands, except per share data)	**2021**	**2020**	2019
INTEREST AND DIVIDEND INCOME:			
Interest and fees on loans	**$ 66,371**	$ 63,538	$ 54,911
Interest-bearing deposits with banks	**447**	401	407
Investment securities:			
Taxable	**3,820**	4,090	4,673
Nontaxable	**2,201**	1,869	1,492
Dividends	**378**	398	497
TOTAL INTEREST AND DIVIDEND INCOME	**73,217**	70,296	61,980
INTEREST EXPENSE:			
Deposits	**5,837**	6,851	9,219
Borrowed funds	**1,268**	1,254	2,821
TOTAL INTEREST EXPENSE	**7,105**	8,105	12,040
NET INTEREST INCOME	**66,112**	62,191	49,940
Provision for loan losses	**1,550**	2,400	1,675
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	**64,562**	59,791	48,265
NON-INTEREST INCOME:			
Service charges	**4,755**	4,221	4,687
Trust	**865**	803	750
Brokerage and insurance	**1,625**	1,297	1,141
Equity security gains (losses), net	**339**	(41)	120
Available for sale security gains, net	**212**	305	24
Gains on loans sold	**1,283**	2,168	473
Earnings on bank owned life insurance	**1,828**	695	623
Other	**1,398**	1,974	568
TOTAL NON-INTEREST INCOME	**12,305**	11,422	8,386
NON-INTEREST EXPENSES:			
Salaries and employee benefits	**25,902**	24,190	20,456
Occupancy	**2,966**	2,557	2,174
Furniture and equipment	**519**	757	674
Professional fees	**1,526**	1,517	1,423
Federal depository insurance	**522**	476	75
Pennsylvania shares tax	**880**	868	808
Amortization of intangibles	**192**	216	259
Merger and acquisition	**-**	2,179	466
ORE expenses	**439**	451	376
Software expenses	**1,321**	1,155	948
Other	**7,283**	6,481	5,682
TOTAL NON-INTEREST EXPENSES	**41,550**	40,847	33,341
Income before provision for income taxes	**35,317**	30,366	23,310
Provision for income taxes	**6,199**	5,263	3,820
NET INCOME	**$ 29,118**	$ 25,103	$ 19,490
PER COMMON SHARE DATA:			
EARNINGS PER SHARE - BASIC	**$ 7.38**	$ 6.53	$ 5.42
EARNINGS PER SHARE – DILUTED	**$ 7.38**	$ 6.53	$ 5.41
CASH DIVIDENDS PER SHARE	**$ 1.86**	$ 1.90	$ 1.74
Number of shares used in computation - basic	**3,945,299**	3,844,241	3,597,709
Number of shares used in computation - diluted	**3,945,299**	3,846,082	3,599,805

See accompanying notes to consolidated financial statements.

Citizens Financial Services, Inc.
Consolidated Statement of Changes in Comprehensive Income
Year Ended December 31,

(in thousands)	**2021**	2020	2019
Net Income	**$ 29,118**	$ 25,103	$ 19,490
Other Comprehensive (loss) income			
Securities available for sale			
Unrealized holding (loss) gain during the period	**(7,071)**	5,074	4,156
Income tax effect	**(1,485)**	1,066	873
Subtotal	**(5,586)**	4,008	3,283
Reclassification adjustment for gains included in income	**(212)**	(305)	(24)
Income tax effect	**(44)**	(65)	(4)
Subtotal	**(168)**	(240)	(20)
Unrealized gain (loss) on interest rate swap	**1,920**	(11)	-
Income tax effect	**402**	(2)	-
Other comprehensive gain (loss) on interest rate swap	**1,518**	(9)	-
Change in unrecognized pension costs	**1,892**	(688)	36
Income tax effect	**398**	(145)	7
Other comprehensive gain (loss) gain on unrecognized pension costs	**1,494**	(543)	29
Net other comprehensive (loss) income	**(2,742)**	3,216	3,292
Comprehensive income	**$ 26,376**	$ 28,319	$ 22,782

See accompanying notes to consolidated financial statements.

Citizens Financial Services, Inc.
Consolidated Statement of Changes in Stockholders' Equity

(in thousands, except share data)	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
Balance, December 31, 2018	3,904,212	$ 3,904	$ 53,099	$ 99,727	$ (3,921)	$ (13,580)	$ 139,229
Comprehensive income:							
Net income				19,490			19,490
Net other comprehensive income					3,292		3,292
Stock dividend (1%)	34,456	35	2,067	(2,102)			-
Purchase of treasury stock (21,551 shares)						(1,291)	(1,291)
Restricted stock, executive and Board of Director awards			(374)			489	115
Restricted stock vesting			254				254
Forfeited restricted stock			43			(43)	-
Cash dividends, $1.743 per share				(6,315)			(6,315)
Balance, December 31, 2019	3,938,668	$ 3,939	$ 55,089	$ 110,800	$ (629)	$ (14,425)	$ 154,774
Comprehensive income:							
Net income				25,103			25,103
Net other comprehensive income					3,216		3,216
Stock dividend (1%)	38,318	38	1,878	(1,916)			-
Stock issued for acquisition	373,356	373	18,854				19,227
Purchase of treasury stock (40,438 shares)						(2,122)	(2,122)
Restricted stock, executive and Board of Director awards			(260)			408	148
Restricted stock vesting			326				326
Sale of treasury stock			1			125	126
Forfeited restricted stock			19			(19)	-
Cash dividend reinvestment paid from treasury stock			1	(821)		820	-
Cash dividends, $1.900 per share				(6,539)			(6,539)
Balance, December 31, 2020	4,350,342	$ 4,350	$ 75,908	$ 126,627	$ 2,587	$ (15,213)	$ 194,259
Comprehensive income:							
Net income				**29,118**			**29,118**
Net other comprehensive loss					**(2,742)**		**(2,742)**
Stock dividend (1%)	**38,559**	**39**	**2,313**	**(2,352)**			**-**
Purchase of treasury stock (23,390 shares)						**(1,374)**	**(1,374)**
Restricted stock, executive and Board of Director awards			**(273)**			**444**	**171**
Restricted stock vesting			**443**				**443**
Forfeited restricted stock			**4**			**(4)**	**-**
Cash dividends, $1.861 per share				**(7,383)**			**(7,383)**
Balance, December 31, 2021	**4,388,901**	**$ 4,389**	**$ 78,395**	**$ 146,010**	**$ (155)**	**$ (16,147)**	**$ 212,492**

See accompanying notes to consolidated financial statements.

Citizens Financial Services, Inc.
Consolidated Statement of Cash Flows

(in thousands)	Year Ended December 31, 2021	2020	2019
Cash Flows from Operating Activities:			
Net income	**$ 29,118**	$ 25,103	$ 19,490
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	**1,550**	2,400	1,675
Depreciation and amortization	**1,113**	1,138	1,043
Amortization and accretion of loans and other assets	**(4,535)**	(3,960)	(545)
Amortization and accretion on investment securities	**2,215**	1,155	308
Deferred income taxes	**689**	367	317
Equity security (gains) losses, net	**(339)**	41	(120)
Available for sale security (gains) losses, net	**(212)**	(305)	(24)
Earnings on bank owned life insurance	**(1,828)**	(695)	(623)
Stock awards	**614**	473	369
Originations of loans held for sale	**(44,668)**	(88,024)	(21,157)
Proceeds from sales of loans held for sale	**55,621**	75,809	21,780
Realized gains on loans sold	**(1,283)**	(2,168)	(473)
(Increase) decrease in accrued interest receivable	**764**	(857)	(103)
Increase (decrease) in accrued interest payable	**(306)**	(235)	12
Other, net	**180**	1,580	(182)
Net cash provided by operating activities	**38,693**	11,822	21,767
Cash Flows from Investing Activities:			
Available-for-sale securities:			
Proceeds from sales of available-for-sale securities	**29,198**	23,415	10,489
Proceeds from maturity and principal repayments of securities	**55,520**	70,008	62,625
Purchase of securities	**(211,218)**	(143,987)	(68,963)
Purchase of equity securities	**-**	(1,339)	(65)
Proceeds from sale of equity securities	**-**	168	-
Proceeds from redemption of Regulatory Stock	**4,989**	9,454	10,787
Purchase of Regulatory Stock	**(3,688)**	(7,396)	(11,526)
Net increase in loans	**(32,111)**	(63,440)	(37,492)
Purchase of interest bearing time deposits	**-**	(350)	(248)
Proceeds from matured interest-bearing time deposits with other banks	**2,732**	848	1,490
Purchase of bank owned life insurance	**(7,800)**	-	-
Purchase of premises, equipment and software	**(1,105)**	(942)	(483)
Proceeds from sale of premises and equipment	**-**	-	7
Proceeds from life insurance	**3,714**	-	-
Proceeds from sale of foreclosed assets held for sale	**1,537**	1,805	1,056
Acquisition, net of cash paid	**-**	1,022	-
Net cash used in investing activities	**(158,232)**	(110,734)	(32,323)
Cash Flows from Financing Activities:			
Net increase in deposits	**247,293**	168,914	25,962
Proceeds from long-term borrowings	**9,869**	20,000	10,000
Repayments of long-term borrowings	**(26,800)**	(15,000)	(3,123)
Net increase (decrease) in short-term borrowed funds	**2,060**	(16,280)	(12,954)
Purchase of treasury stock	**(1,374)**	(2,122)	(1,291)
Sale of treasury stock to employee stock purchase plan	**-**	126	-
Dividends paid	**(7,383)**	(6,539)	(6,315)
Net cash provided by financing activities	**223,665**	149,099	12,279
Net increase in cash and cash equivalents	**104,126**	50,187	1,723
Cash and Cash Equivalents at Beginning of Year	**68,707**	18,520	16,797
Cash and Cash Equivalents at End of Year	**$ 172,833**	$ 68,707	$ 18,520
Supplemental Disclosures of Cash Flow Information:			
Interest paid	**$ 7,411**	$ 8,175	$ 12,028
Income taxes paid	**$ 5,500**	$ 4,750	$ 3,300
Non-cash activities:			

Stock dividend	**$**	**2,352**	$	1,916	$	2,102
Real estate acquired in settlement of loans	**$**	**906**	$	281	$	3,836
Right of use asset and liability	**$**	**1,636**	$	636	$	1,454

Acquisition of				Midcoast Community Bancorp Inc.		
Non-cash assets acquired						
Available-for-sale securities	**$**	**-**	$	-	**$**	**-**
Interest bearing time deposits with other banks		**-**		-		**-**
Loans		**-**		223,235		**-**
Premises and equipment		**-**		1,787		**-**
Accrued interest receivable		**-**		586		**-**
Bank owned life insurance		**-**		3,766		**-**
Intangibles		**-**		157		**-**
Deferred tax asset		**-**		3,402		**-**
Other assets		**-**		2,878		**-**
Goodwill		**-**		8,080		**-**
		-		243,891		**-**
Liabilities assumed						
Noninterest-bearing deposits		**-**		38,694		**-**
Interest-bearing deposits		**-**		170,132		**-**
Accrued interest payable		**-**		164		**-**
Borrowed funds		**-**		15,497		
Other liabilities		**-**		1,198		**-**
		-		225,685		**-**
Net non-cash liabilities acquired		**-**		18,206		**-**
Cash and cash equivalents acquired	**$**	**-**	$	8,637	**$**	**-**

See accompanying notes to consolidated financial statements.

CITIZENS FINANCIAL SERVICES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business and Organization

Citizens Financial Services, Inc. (individually and collectively, the "Company") is headquartered in Mansfield, Pennsylvania, and provides a full range of banking and related services through its wholly owned subsidiary, CZFS Acquisition Company, LLC (CZFS), and its wholly owned subsidiary, First Citizens Community Bank (the "Bank"), and its wholly owned subsidiaries, First Citizens Insurance Agency, Inc. ("First Citizens Insurance") and 1st Realty of PA, LLC ("Realty"). CZFS was formed in March 2020 as part of the merger with Midcoast Community Bancorp. Inc. (MidCoast). Realty was formed in March of 2019 to manage and sell properties acquired by the Bank in the settlement of a bankruptcy filing with a commercial customer. On December 11, 2015, the Company completed its acquisition of The First National Bank of Fredericksburg (FNB). On December 8, 2017, the Bank completed its acquisition of the S&T Bank branch in State College (State College). On April 17, 2020, the Company completed its acquisition of MidCoast. As of December 31, 2021, the Bank operates thirty full-service banking branches in Potter, Tioga, Bradford, Clinton, Lebanon, Lancaster, Berks, Schuylkill, Centre and Chester counties, Pennsylvania, Allegany County, New York, and the cities of Wilmington and Dover, Delaware, and a limited branch office in Union county, Pennsylvania. The Bank also provides trust services, including the administration of trusts and estates, retirement plans, and other employee benefit plans, along with a brokerage division that provides a comprehensive menu of investment services. The Bank serves individual and corporate customers and is subject to competition from other financial institutions and intermediaries with respect to these services. The Company and Bank are supervised by the Board of Governors of the Federal Reserve System, while the Bank is subject to additional regulation and supervision by the Pennsylvania Department of Banking.

A summary of significant accounting and reporting policies applied in the presentation of the accompanying financial statements follows:

Basis of Presentation

The financial statements are consolidated to include the accounts of the Company, and its subsidiary CZFS, and its subsidiary, First Citizens Community Bank, and its subsidiaries, First Citizens Insurance Agency, Inc. and 1st Realty of PA, LLC. These statements have been prepared in accordance with U.S. generally accepted accounting principles. All significant inter-company accounts and transactions have been eliminated in the consolidated financial statements.

Use of Estimates

In preparing the financial statements, management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses for the period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change relate to determination of the allowance for loan losses, goodwill, derivatives, pension plans and deferred tax assets and liabilities.

Operating Segments

An operating segment is defined as a component of an enterprise that engages in business activities that generates revenue and incurs expense, and the operating results of which are reviewed by the chief operating decision maker in the determination of resource allocation and performance. While the Company's chief decision makers monitor the revenue streams of the various Company's products, services and regions, operations are managed and financial performance is evaluated on a Company-wide basis. Consistent with our internal reporting, the Company's business activities are reported as one segment, which is community banking.

Cash and Cash Equivalents

Cash equivalents include cash on hand, deposits in banks and interest-earning deposits. Interest-earning deposits with original maturities of 90 days or less are considered cash equivalents.

Interest bearing time deposits with other banks are not included with cash and cash equivalents as the original maturities were greater than 90 days.

Investment Securities

Investment securities at the time of purchase are classified as one of the three following types:

Held-to-Maturity Securities - Includes securities that the Company has the positive intent and ability to hold to maturity. These securities are reported at amortized cost. The Company had no held-to-maturity securities as of December 31, 2021 and 2020.

Trading Securities - Includes debt and equity securities bought and held principally for the purpose of selling them in the near term. Such securities are reported at fair value with unrealized holding gains and losses included in earnings. The Company had no trading securities as of December 31, 2021 and 2020.

Available-for-Sale Securities – This category included debt securities not classified as held-to-maturity or trading securities that will be held for indefinite periods of time. These securities may be sold in response to changes in market interest or prepayment rates, needs for liquidity and changes in the availability of and yield of alternative investments. Such securities are reported at fair value, with unrealized holding gains and losses excluded from earnings and reported as a separate component of stockholders' equity, net of the estimated income tax effect.

The amortized cost of investment in debt securities is adjusted for amortization of premiums and accretion of discounts, computed by a method that results in a level yield. Gains and losses on the sale of investment securities are computed on the basis of specific identification of the adjusted cost of each security.

Debt securities are periodically reviewed for other-than-temporary impairment. Management considers whether the present value of future cash flows expected to be collected are less than the security's amortized cost basis (the difference defined as the credit loss), the magnitude and duration of the decline, the reasons underlying the decline and the Company's intent to sell the security or whether it is more likely than not that the Company would be required to sell the security before its anticipated recovery in market value, to determine whether the loss in value is other than temporary. Once a decline in value is determined to be other than temporary, if the Company does not intend to sell the security, and it is more-likely-than-not that it will not be required to sell the security, before recovery of the security's amortized cost basis, the charge to earnings is limited to the amount of credit loss. Any remaining difference between fair value and amortized cost (the difference defined as the non-credit portion) is recognized in other comprehensive income, net of applicable taxes. Otherwise, the entire difference between fair value and amortized cost is charged to earnings.

The fair value of investments, except certain state and municipal securities, is based on bid prices published in financial newspapers or bid quotations received from securities dealers. The fair value of certain state and municipal securities is not readily available through market sources other than dealer quotations, so fair value is based on quoted market prices of similar instruments, adjusted for differences between the quoted instruments and the instruments being valued.

Equity Securities – This category includes common stocks of public companies. Such securities are reported at fair value with unrealized holding gains and losses included in earnings.

Restricted Stock - Common stock of the Federal Reserve Bank, Federal Home Loan Bank of Pittsburgh (FHLB) and correspondent banks represent ownership in institutions which are wholly owned by other financial institutions. These restricted equity securities are accounted for at cost and are classified as other assets.

Loans Held for Sale

Certain newly originated fixed-rate residential mortgage loans are classified as held for sale, because it is management's intent to sell these residential mortgage loans. The residential mortgage loans held for sale are carried at the lower of aggregate cost or fair value.

Loans

Interest on all loans is recognized on the accrual basis based upon the principal amount outstanding. The accrual of interest income on loans is discontinued when, in the opinion of management, doubt exists as to the ability to collect such interest. Payments received on non-accrual loans are applied to the outstanding principal balance or recorded as interest income, depending upon our assessment of our ultimate ability to collect principal and interest. Loans are returned to the accrual status when factors indicating doubtful collectability cease to exist.

The Company recognizes nonrefundable loan origination fees, SBA fees and certain direct loan origination costs over the life of the related loan as an adjustment of loan yield using the interest method.

Allowance for Loan Losses

The allowance for loan losses represents the amount which management estimates is adequate to provide for probable losses inherent in the Company's loan portfolio. The allowance method is used in providing for loan losses. Accordingly, all loan losses are charged to the allowance and all recoveries are credited to it. The allowance for loan losses is established through a provision for loan losses which is charged to operations. The provision is based upon management's periodic evaluation of individual loans, the overall risk characteristics of the various portfolio segments, past experience with losses, the impact of economic conditions on borrowers, and other relevant factors. The estimates used in determining the adequacy of the allowance for loan losses are particularly susceptible to significant change in the near term.

Impaired loans are other commercial, other agricultural, municipal, agricultural real estate, commercial real estate loans and certain residential mortgages cross collateralized with commercial relationships for which it is probable that the Company will not be able to collect all amounts due according to the contractual terms of the loan agreement. The Company individually evaluates such loans for impairment and does not aggregate loans by major risk classifications. The definition of "impaired loans" is not the same as the definition of "non-accrual loans," although the two categories overlap. The Company may choose to place a loan on non-accrual status due to payment delinquency or uncertain collectability, while not classifying the loan as impaired if the loan is not a commercial, agricultural, municipal or commercial real estate loan. Factors considered by management in determining impairment include payment status and collateral value. The amount of impairment for these types of impaired loans is determined by the difference between the present value of the expected cash flows related to the loan, using the original interest rate, and its recorded value; or, as a practical expedient in the case of a collateral dependent loan, the difference between the fair value of the collateral and the recorded amount of the loans.

Mortgage loans on one to four family properties and all consumer loans are large groups of smaller balance homogeneous loans and are measured for impairment collectively. Loans that experience insignificant payment delays, which is defined as 90 days or less, generally are not classified as impaired. Management determines the significance of payment delays 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 borrower's prior payment record, and the amount of shortfall in relation to the principal and interest owed.

The Company allocates the allowance based on the factors described below, which conform to the Company's loan classification policy. In reviewing risk within the loan portfolio, management has determined there to be several different risk categories within the loan portfolio. The allowance for loan losses consists of amounts applicable to: (i) residential real estate loans; (ii) commercial real estate (iii) agricultural real estate loans; (iv) construction; (v) consumer loans; (vi) other commercial loans (vii) other agricultural loans and (viii) state and political subdivision loans. Factors considered in this process include general loan terms, collateral, and availability of historical data to support the analysis. Historical loss percentages for each risk category are calculated and used as the basis for calculating allowance allocations. Certain qualitative factors are evaluated to determine additional inherent risks in the loan portfolio, which are not necessarily reflected in the historical loss percentages. These factors are then added to the historical allocation percentage to get the adjusted factor to be applied to non classified loans. The following qualitative factors are analyzed:

- Level of and trends in delinquencies, impaired/classified loans
  - Change in volume and severity of past due loans
  - Volume of non-accrual loans
  - Volume and severity of classified, adversely or graded loans
- Level of and trends in charge-offs and recoveries
- Trends in volume, terms and nature of the loan portfolio
- Effects of any changes in risk selection and underwriting standards and any other changes in lending and recovery policies, procedures and practices
- Changes in the quality of the Bank’s loan review system
- Experience, ability and depth of lending management and other relevant staff
- National, state, regional and local economic trends and business conditions
  - General economic conditions
  - Unemployment rates
  - Inflation / CPI
  - Changes in values of underlying collateral for collateral-dependent loans
- Industry conditions including the effects of external factors such as competition, legal, and regulatory requirements on the level of estimated credit losses.
- Existence and effect of any credit concentrations, and changes in the level of such concentrations
- Any change in the level of board oversight

The Company analyzes its loan portfolio each quarter to determine the appropriateness of its allowance for loan losses.

Loan Charge-off Policies

Consumer loans are generally fully or partially charged down to the fair value of collateral securing the asset when the loan is 180 days past due for open-end loans or 120 days past due for closed-end loans unless the loan is well secured and in the process of collection. All other loans are generally charged down to the net realizable value when the loan is 90 days past due.

Troubled Debt Restructurings

In situations where, for economic or legal reasons related to a borrower's financial difficulties, management may grant a concession for other than an insignificant period of time to the borrower that would not otherwise be considered, 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 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. In addition to the allowance for the pooled portfolios, management has developed a separate allowance for loans that are identified as impaired through a TDR. TDRs are excluded from pooled loss forecasts and a separate reserve is provided under the accounting guidance for loan impairment.

Purchased Credit Impaired Loans

The Company purchased loans in connection with its acquisitions of FNB in 2015, the State College branch in 2017 and MidCoast in 2020, some of which showed evidence of credit deterioration as of the acquisition since origination. These purchased credit impaired (“PCI”) loans were recorded at the amount paid, such that there is no carryover of the seller’s allowance for loan losses. After acquisition, losses are recognized by an increase in the allowance for loan losses. Over the life of the loan, expected cash flows continue to be estimated. If this subsequent estimate indicated that the present value of expected cash flows is less than the carrying amount, a charge to the allowance for loan loss is made through a provision. If the estimate indicates that the present value of the expected cash flows is greater than the carrying amount, it is recognized as part of future interest income.

Such PCI loans are accounted for individually, and the Company estimates the amount and timing of expected cash flows for each loan. The expected cash flows in excess of the amount paid is recorded as interest income over the remaining life of the loan (accretable yield). The excess of the loan's contractual principal and interest over expected cash flows is not amortized over the remaining life of the loan (nonaccretable difference).

For loans purchased that did not show evidence of credit deterioration, the difference between the fair value of the loan at the acquisition date and the loan's face value is being amortized as a yield adjustment over the estimated remaining life of the loan using the effective interest method.

Foreclosed Assets Held For Sale

Foreclosed assets acquired in settlement of loans are carried at fair value, less estimated costs to sell. Prior to foreclosure, as the value of the underlying loan is written down to fair market value of the real estate or other assets to be acquired by a charge to the allowance for loan losses, if necessary. Any subsequent write-downs are charged against operating expenses. Operating expenses of such properties, net of related income and losses on disposition, are included in other expenses and gains and losses are included in other non-interest income or other non-interest expense.

Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost, less accumulated depreciation. Depreciation expense is computed on straight line and accelerated methods over the estimated useful lives of the assets, which range from 3 to 15 years for furniture, fixtures and equipment and 5 to 40 years for building premises. Repair and maintenance expenditures which extend the useful life of an asset are capitalized and other repair expenditures are expensed as incurred.

When premises or equipment are retired or sold, the remaining cost and accumulated depreciation are removed from the accounts and any gain or loss is credited to income or charged to expense, respectively.

The Company has operating leases for several branch locations. Generally, the underlying lease agreements do not contain any material residual value guarantees or material restrictive covenants. The Company may also lease certain office equipment under operating leases. Many of our leases include both lease (e.g., minimum rent payments) and non-lease components (e.g., common-area or other maintenance costs). The Company accounts for each component separately based on the standalone price of each component. In addition, there are several operating leases with lease terms of less than one year and therefore, we have elected the practical expedient to exclude these short-term leases from our right of use (ROU) assets and lease liabilities.

Most leases include one or more options to renew. The exercise of lease renewal options is typically at the sole discretion of management and is based on whether the extension options are reasonably certain to be exercised after giving proper consideration to all facts and circumstances of the lease. If management determines that the Company is reasonably certain to exercise the extension option(s), the additional term is included in the calculation of the lease liability.

As most of our leases do not provide an implicit rate, we use the fully collateralized FHLB borrowing rate, commensurate with the lease terms based on the information available at the lease commencement date in determining the present value of the lease payments

Intangible Assets

Intangible assets, other than goodwill, include core deposit intangibles and mortgage servicing rights (MSRs). Core deposit intangibles are a measure of the value of consumer demand and savings deposits acquired in business combinations accounted for as purchases. The core deposit intangibles are being amortized over 10 years using the sum-of-the-years digits method of amortization, while the covenant not to compete was amortized over four years on a straight line basis.

MSRs arise from the Company originating certain loans for the express purpose of selling such loans in the secondary market. The Company maintains all servicing rights for these loans. The loans held for sale are carried at lower of cost or market.

Originated MSRs are recorded by allocating total costs incurred between the loan and servicing rights based on their relative fair values. MSRs are amortized in proportion to the estimated servicing income over the estimated life of the servicing portfolio and measured annually for impairment.

The recoverability of the carrying value of intangible assets is evaluated on an ongoing basis, and permanent declines in value, if any, are charged to expense.

Goodwill

The Company utilizes a two-step process for testing the impairment of goodwill on at least an annual basis. This approach could cause more volatility in the Company's reported net income because impairment losses, if any, could occur irregularly and in varying amounts. The Company may also perform a qualitative assessment to determine whether it is more likely than not that the fair value of the reporting unit is less than its carrying value. Based on the fair value of the reporting unit, no impairment of goodwill was recognized in 2021, 2020 or 2019.

Bank Owned Life Insurance

The Company has purchased life insurance policies on certain employees. Any death benefits received from a policy while the insured person is an active employee of the Bank will be split with the beneficiary of the policy. Under these agreements, the Bank receives the cash surrender value of the policy plus 50% of the benefit in excess of the cash surrender value and the remaining amount of the payout will be given to the beneficiary named by the insured person in the policy. The Company is the sole beneficiary of any death benefits received from non-active insured persons. Additionally, as a result of the MidCoast acquisition, the Company acquired life insurance policies on former MidCoast employees. The Company is owner and sole beneficiary of these policies. The Company acquired life insurance policies on former FNB employees and directors, as part of the acquisition of FNB. The policies obtained as part of the acquisition provide a fixed dollar benefit to the former employee or director beneficiaries, whether or not the insured person is affiliated with the Company at the time of his or her death. Bank owned life insurance is recorded at its cash surrender value, or the amount that can be realized. Increases in the cash surrender value are recognized as other non-interest income. The obligation of $696,000 and $687,000 under split-dollar benefit agreements to former employees and directors or their beneficiaries have been recognized as liabilities on the consolidated balance sheet at December 31, 2021 and 2020. The expenses associated with the split dollar benefit were $9,000, $3,000 and $36,000 for 2021, 2020 and 2019, respectively.

Income Taxes

The Company and the Bank file a consolidated federal income tax return. Deferred tax assets and liabilities are computed based on the difference between the financial statement basis and income tax basis of assets and liabilities using the enacted marginal tax rates. Deferred income tax expenses or benefits are based on the changes in the net deferred tax asset or liability from period to period.

Derivatives

Derivative financial instruments are recognized as assets or liabilities at fair value. The Company has interest rate swap agreements which are used as part of its asset liability management to help manage interest rate risk. The Company does not use derivatives for trading purposes.

At the inception of a derivative contract, the Company designates the derivative as one of three types based on the purpose of the contract and belief as to its effectiveness as a hedge. These three types are (1) a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment ("fair value hedge"), (2) a hedge of a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability ("cash flow hedge"), or (3) an instrument with no hedging designation ("stand-alone derivative"). For a fair value hedge, the gain or loss on the derivative, as well as the offsetting loss or gain on the hedged item, are recognized in current earnings as fair values change. For a cash flow hedge, the gain or loss on the derivative is reported in other comprehensive income and is reclassified into earnings in the same periods during which the hedged transaction affects earnings. For both types of hedges, changes in the fair value of derivatives that are not highly effective in hedging the changes in fair value or expected cash flows of the hedged item are recognized immediately in current earnings. Changes in the fair value of derivatives that do not qualify for hedge accounting are reported currently in earnings, as non-interest income.

Net cash settlements on derivatives that qualify for hedge accounting are recorded in interest income or interest expense, based on the item being hedged. Net cash settlements on derivatives that do not qualify for hedge accounting are reported in non-interest income. Cash flows on hedges are classified in the cash flow statement the same as the cash flows of the items being hedged.

The Company formally documents the relationship between derivatives and hedged items, as well as the risk-management objective and the strategy for undertaking hedge transactions, at the inception of the hedging relationship. This documentation includes linking fair value or cash flow hedges to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivative instruments that are used are highly effective in offsetting changes in fair values or cash flows of the hedged items. The Company discontinues hedge accounting when it determines that the derivative is no longer effective in offsetting changes in the fair value or cash flows of the hedged item, the derivative is settled or terminates, a hedged forecasted transaction is no longer probable, a hedged firm commitment is no longer firm, or treatment of the derivative as a hedge is no longer appropriate or intended.

When hedge accounting is discontinued, subsequent changes in fair value of the derivative are recorded as non-interest income. When a fair value hedge is discontinued, the hedged asset or liability is no longer adjusted for changes in fair value and the existing basis adjustment is amortized or accreted over the remaining life of the asset or liability. When a cash flow hedge is discontinued but the hedged cash flows or forecasted transactions are still expected to occur, gains or losses that were accumulated in other comprehensive income are amortized into earnings over the same periods which the hedged transactions will affect earnings.

Employee Benefit Plans

The Company has noncontributory defined benefit pension plans covering employees hired before January 1, 2007 and employees acquired as part of the FNB acquisition. It is the Company's policy to fund pension costs on a current basis to the extent deductible under existing tax regulations. Such contributions are intended to provide not only for benefits attributed to service to date, but also for those expected to be earned in the future. The plan acquired as part of the FNB acquisition was terminated in 2019.

The Company has a defined contribution, 401(k) plan covering eligible employees. The employee may also contribute to the plan on a voluntary basis, up to a maximum percentage allowable not to exceed the limits of Code Sections 401(k). Under the plan, the Company also makes contributions on behalf of eligible employees, which vest immediately. For employees hired after January 1, 2007, in lieu of the pension plan, an additional annual discretionary 401(k) plan contribution is made and is equal to a percentage of an employee's base compensation.

The Company also has a profit-sharing plan for employees which provide tax-deferred salary savings to plan participants. The Company has a deferred compensation plan for directors who have elected to defer all or portions of their fees until their retirement or termination from service.

The Company has a restricted stock plan which covers eligible employees and non-employee corporate directors. Under the plan, awards are granted based upon performance related requirements and are subject to certain vesting criteria. Compensation cost related to restricted stock is recognized based on the market price of the stock at the grant date over the vesting period.

The Company has an employee stock purchase plan that allows employees to withhold money from their paychecks, which is then utilized to purchase shares of the Company's stock on either the open market or through treasury stock, if shares are unavailable on the open market.

The Company maintains a non-qualified supplemental executive retirement plan ("SERP") for certain executives to compensate those executive participants in the Company's noncontributory defined benefit pension plan whose benefits are limited by compensation limitations under current tax law. The SERP is considered an unfunded plan for tax and ERISA purposes and all obligations arising under the SERP are payable from the general assets of the Company. Expenses under the SERP are recognized as earned over the expected years of service.

The Company maintains a non-tax qualified executive deferred compensation plan ("Deferred Compensation Plan") for eligible employees designated by the board of directors. Each of the named executive officers are eligible to participate in the Deferred Compensation Plan. The Deferred Compensation Plan is considered an unfunded plan for tax and ERISA purposes and all obligations arising under the Deferred Compensation Plan are payable from the general assets of the Company. Expenses under the Deferred Compensation Plan are recognized as earned over the expected years of service.

Advertising Costs

Advertising costs are generally expensed as incurred and amounted to $460,000, $470,000 and $466,000 for the years ended December 31, 2021, 2020 and 2019, respectively.

Comprehensive Income (Loss)

The Company is required to present comprehensive income in a full set of general purpose financial statements for all periods presented. Other comprehensive income (loss) is comprised of unrealized holding gains (losses) on the available-for-sale securities portfolio and unrecognized pension costs.

Recent Accounting Pronouncements – Not yet effective

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments - Credit Losses: Measurement of Credit Losses on Financial Instruments*, which changes the impairment model for most financial assets. This Update is intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The underlying premise of the Update is that financial assets measured at amortized cost should be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. The allowance for credit losses should reflect management's current estimate of credit losses that are expected to occur over the remaining life of a financial asset. The income statement will be effected for the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. ASU 2016-13 is effective for annual and interim periods beginning after December 15, 2019, and early adoption is permitted for annual and interim periods beginning after December 15, 2018. With certain exceptions, transition to the new requirements will be through a cumulative effect adjustment to opening retained earnings as of the beginning of the first reporting period in which the guidance is adopted. In November 2019, the FASB issued ASU 2019-10, *Financial Instruments – Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*. This Update defers the effective date of ASU 2016-13 for SEC filers that are eligible to be smaller reporting companies, non-SEC filers, and all other companies to fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. We expect to recognize a one-time cumulative effect adjustment to the allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective, but cannot yet determine the magnitude of any such one-time adjustment or the overall impact of the new guidance on the consolidated financial statements. In that regard, we have formed a cross-functional working group. The working group is comprised of individuals from various functional areas including credit, loan origination and finance. We are currently working through our implementation plan which includes assessment and documentation of processes, internal controls and data sources; model development and documentation; and system configuration, among other things. We are also in the process of implementing a third-party vendor solution to assist us in the application of the ASU 2016-13. The adoption of the ASU 2016-13 could result in an increase in the allowance for loan losses as a result of changing from an "incurred loss" model, which encompasses allowances for current known and inherent losses within the portfolio, to an "expected loss" model, which encompasses allowances for losses expected to be incurred over the life of the portfolio. While we are currently unable to reasonably estimate the impact of adopting ASU 2016-13, we expect that the impact of adoption will be significantly influenced by the composition, characteristics and quality of our loan portfolio as well as the prevailing economic conditions and forecasts as of the adoption date.

In January 2017, the FASB issued ASU 2017-04, *Simplifying the Test for Goodwill Impairment*. To simplify the subsequent measurement of goodwill, the FASB eliminated Step 2 from the goodwill impairment test. In computing the implied fair value of goodwill under Step 2, an entity had to perform procedures to determine the fair value at the impairment testing date of its assets and liabilities (including unrecognized assets and liabilities) following the procedure that would be required in determining the fair value of assets acquired and liabilities assumed in a business combination. Instead, under the amendments in this Update, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting units fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. A public business entity that is a U.S. Securities and Exchange Commission (SEC) filer should adopt the amendments in this Update for its annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. In November 2019, the FASB issued ASU 2019-10, *Financial Instruments – Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*, which deferred the effective date for ASC 350, *Intangibles – Goodwill and Other*, for smaller reporting companies to fiscal years beginning after December 15, 2022, and interim periods within those fiscal years. This Update is not expected to have a significant impact on the Company's consolidated financial statements.

In April 2019, the FASB issued ASU 2019-04, *Codification Improvements to Topic 326, Financial Instruments – Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments,* which affects a variety of topics in the Codification and applies to all reporting entities within the scope of the affected accounting guidance. *Topic 326, Financial Instruments – Credit Losses* amendments are effective for SEC registrants for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. For all other public business entities, the effective date is for fiscal years beginning after December 15, 2020, and for all other entities, the effective date is for fiscal years beginning after December 15, 2021. *Topic 815, Derivatives and Hedging* amendments are effective for public business entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2019, and interim periods beginning after December 15, 2020. For entities that have adopted the amendments in Update 2017-12, the effective date is as of the beginning of the first annual period beginning after the issuance of this Update. *Topic 825, Financial Instruments* amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years. In November 2019, the FASB issued ASU 2019-10, *Financial Instruments – Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*. This Update defers the effective date of ASU 2016-13 for SEC filers that are eligible to be smaller reporting companies, non-SEC filers and all other companies to fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. Furthermore, the ASU provides a one-year deferral of the effective dates of the ASUs on derivatives and hedging for companies that are not public business entities. The Company qualifies as a smaller reporting company and does not expect to early adopt these ASUs.

In May 2019, the FASB issued ASU 2019-05, *Financial Instruments – Credit Losses, Topic 326*, which allows entities to irrevocably elect the fair value option for certain financial assets previously measured at amortized cost upon adoption of the new credit losses standard. To be eligible for the transition election, the existing financial asset must otherwise be both within the scope of the new credit losses standard and eligible for the applying the fair value option in ASC 825-10.3. The election must be applied on an instrument-by-instrument basis and is not available for either available-for-sale or held-to-maturity debt securities. For entities that elect the fair value option, the difference between the carrying amount and the fair value of the financial asset would be recognized through a cumulative-effect adjustment to opening retained earnings as of the date an entity adopted ASU 2016-13. Changes in fair value of that financial asset would subsequently be reported in current earnings. For entities that have not yet adopted ASU 2016-13, the effective dates and transition requirements are the same as those in ASU 2016-13. For entities that have adopted ASU 2016-13, ASU 2019-05 is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted once ASU 2016-13 has been adopted. In November 2019, the FASB issued ASU 2019-10, *Financial Instruments – Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*. The Update defers the effective date of ASU 2016-13 for SEC filers that are eligible to be smaller reporting companies, non-SEC filers and all other companies to fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. The Company qualifies as a smaller reporting company and does not expect to early adopt these ASUs.

In November 2019, the FASB issued ASU 2019-11, *Codification Improvements to Topic 326, Financial Instruments – Credit Losses*, to clarify its new credit impairment guidance in ASC 326, based on implementation issues raised by stakeholders. This Update clarified, among other things, that expected recoveries are to be included in the allowance for credit losses for these financial assets; an accounting policy election can be made to adjust the effective interest rate for existing troubled debt restructurings based on the prepayment assumptions instead of the prepayment assumptions applicable immediately prior to the restructuring event; and extends the practical expedient to exclude accrued interest receivable from all additional relevant disclosures involving amortized cost basis. The effective dates in this Update are the same as those applicable for ASU 2019-10. The Company qualifies as a smaller reporting company and does not expect to early adopt these ASUs.

In December 2019, the FASB issued ASU 2019-12, *Income Taxes (Topic 740)*, to simplify the accounting for income taxes, change the accounting for certain tax transactions, and make minor improvements to the codification. This Update provides a policy election to not allocate consolidated income taxes when a member of a consolidated tax return is not subject to income tax and provides guidance to evaluate whether a step-up in tax basis of goodwill relates to a business combination in which book goodwill was recognized or a separate transaction. The Update also changes current guidance for making an intraperiod allocation, if there is a loss in continuing operations and gains outside of continuing operations; determining when a deferred tax liability is recognized after an investor in a foreign entity transitions to or from the equity method of accounting; accounting for tax law changes and year-to-date losses in interim periods; and determining how to apply the income tax guidance to franchise taxes that are partially based on income. For public business entities, the amendments in this Update are effective for fiscal years and interim periods within those fiscal years, beginning after December 15, 2020. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2021, and interim periods within fiscal years beginning after December 15, 2022. This Update is not expected to have a significant impact on the Company’s consolidated financial statements.

In January 2020, the FASB issued ASU 2020-1, *Investments – Equity Securities (Topic 321), Investments – Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815)*, to clarify that an entity should consider observable transactions that require it to either apply or discontinue the equity method of accounting for the purposes of applying the measurement alternative in accordance with Topic 321 immediately before applying or upon discontinuing the equity method. The amendments also clarify that, for the purpose of applying paragraph 815-10-15-141(a) an entity should not consider whether, upon the settlement of the forward contract or exercise of the purchased option, individually or with existing investments, the underlying securities would be accounted for under the equity method in Topic 323 or the fair value option, in accordance with the financial instruments guidance in Topic 825. An entity also would evaluate the remaining characteristics in paragraph 815-10-15-141 to determine the accounting for those forward contracts and purchased options. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2021, and interim periods within those fiscal years. This Update is not expected to have a significant impact on the Company’s consolidated financial statements.

In March 2020, the FASB issued ASU 2020-3*, Codification Improvements to Financial Instruments.* This ASU was issued to improve and clarify various financial instruments topics, including the current expected credit losses (CECL) standard issued in 2016. The ASU includes seven issues that describe the areas of improvement and the related amendments to GAAP; they are intended to make the standards easier to understand and apply and to eliminate inconsistencies, and they are narrow in scope and are not expected to significantly change practice for most entities. Among its provisions, the ASU clarifies that all entities, other than public business entities that elected the fair value option, are required to provide certain fair value disclosures under ASC 825, *Financial Instruments*, in both interim and annual financial statements. It also clarifies that the contractual term of a net investment in a lease under Topic 842 should be the contractual term used to measure expected credit losses under Topic 326. Amendments related to ASU 2019-04 are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is not permitted before an entity’s adoption of ASU 2016-01. Amendments related to ASU 2016-13 for entities that have not yet adopted that guidance are effective upon adoption of the amendments in ASU 2016-13. Early adoption is not permitted before an entity’s adoption of ASU 2016-13. Amendments related to ASU 2016-13 for entities that have adopted that guidance are effective for fiscal years beginning after December 15, 2019, including interim periods within those years. Other amendments are effective upon issuance of this ASU. The Company is currently evaluating the impact the adoption of the standard will have on the Company’s consolidated financial position or results of operations.

In March 2020, the FASB issued ASU 2020-4, *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting, March 2020*, to provide temporary optional expedients and exceptions to the U.S. GAAP guidance on contract modifications and hedge accounting to ease the financial reporting burdens of the expected market transition from LIBOR and other interbank offered rates to alternative reference rates, such as Secured Overnight Financing Rate. Entities can elect not to apply certain modification accounting requirements to contracts affected by what the guidance calls reference rate reform, if certain criteria are met. An entity that makes this election would not have to remeasure the contracts at the modification date or reassess a previous accounting determination. Also, entities can elect various optional expedients that would allow them to continue applying hedge accounting for hedging relationships affected by reference rate reform, if certain criteria are met, and can make a one-time election to sell and/or reclassify held-to-maturity debt securities that reference an interest rate affected by reference rate reform. The amendments in this ASU are effective for all entities upon issuance through December 31, 2022. It is too early to predict whether a new rate index replacement and the adoption of the ASU will have a material impact on the Company's financial statements.

In August 2020, the FASB issued ASU 2020-6, *Debt – Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging – Contracts in Entity's Own Equity (Subtopic 815-40)*, which simplifies the accounting for certain financial instruments with characteristics of liabilities and equity, including convertible instruments and contracts on an entity's own equity. This ASU removes from U.S. GAAP the separation models for (1) convertible debt with a cash conversion feature and (2) convertible instruments with a beneficial conversion feature. As a result, entities will not separately present in equity an embedded conversion feature in such debt. Instead, they will account for a convertible debt instrument wholly as debt, and for convertible preferred stock wholly as preferred stock (i.e., as a single unit of account), unless (1) a convertible instrument contains features that require bifurcation as a derivative under ASC 815 or (2) a convertible debt instrument was issued at a substantial premium. This ASU requires entities to provide expanded disclosures about the terms and features of convertible instruments, how the instruments have been reported in the entity's financial statements, and information about events, conditions, and circumstances that can affect how to assess the amount or timing of an entity's future cash flows related to those instruments. The amendments in this ASU are effective for public business entities that are not smaller reporting companies, for fiscal years beginning after December 15, 2021, and interim periods within those fiscal years. For all other entities, this ASU is effective for fiscal years beginning after December 15, 2023, and interim periods within those fiscal years. The guidance may be early adopted for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. This Update is not expected to have a significant impact on the Company's financial statements.

In October 2020, the FASB issued ASU 2020-08, *Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs,* which clarifies that, for each reporting period, an entity should reevaluate whether a callable debt security is within the scope of ASC 310-20-35-33. For public business entities, ASU 2020-08 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020. Early application is not permitted. For all other entities, ASU 2020-08 is effective for fiscal years beginning after December 15, 2021, and interim periods within fiscal years beginning after December 15, 2022. This Update is not expected to have a significant impact on the Company's financial statements.

In October 2020, the FASB issued ASU 2020-10, *Codification Improvements*, which makes minor technical corrections and clarifications to the ASC. The amendments in Sections B and C of the ASU are effective for annual periods beginning after December 15, 2020, for public business entities. For all other entities, the amendments are effective for annual periods beginning after December 15, 2021, and interim periods within annual periods beginning after December 15, 2022. This Update is not expected to have a significant impact on the Company's financial statements.

In January 2021, the FASB issued ASU 2021-01, *Reference Rate Reform (Topic 848)*, which provides optional temporary guidance for entities transitioning away from the London Interbank Offered Rate (LIBOR) and other interbank offered rates (IBORs) to new references rates so that derivatives affected by the discounting transition are explicitly eligible for certain optional expedients and exceptions within Topic 848. ASU 2021-01 clarifies that the derivatives affected by the discounting transition are explicitly eligible for certain optional expedients and exceptions in Topic 848. ASU 2021-01 is effective immediately for all entities. Entities may elect to apply the amendments on a full retrospective basis as of any date from the beginning of an interim period that includes or is subsequent to March 12, 2020, or on a prospective basis to new modifications from any date within an interim period that includes or is subsequent to the date of the issuance of a final update, up to the date that financial statements are available to be issued. The amendments in this update do not apply to contract modifications made, as well as new hedging relationships entered into, after December 31, 2022, and to existing hedging relationships evaluated for effectiveness for periods after December 31, 2022, except for certain hedging relationships existing as of December 31, 2022, that apply certain optional expedients in which the accounting effects are recorded through the end of the hedging relationship. The Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In May 2021, the FASB issued ASU 2021-04, *Earnings Per Share (Topic 260), Debt – Modifications and Extinguishments (Subtopic 470-50), Compensation – Stock Compensation (Topic 718), and Derivatives and Hedging – Contracts in Entity's Own Equity (Subtopic 815-40),* which requires an entity to treat a modification of an equity-classified warrant that does not cause the warrant to become liability-classified as an exchange of the original warrant for a new warrant. This guidance applies whether the modification is structured as an amendment to the terms and conditions of the warrant or as termination of the original warrant and issuance of a new warrant. An entity should measure the effect of a modification as the difference between the fair value of the modified warrant and the fair value of that warrant immediately before modification. The amendments in this Update are effective for all entities for fiscal years beginning after December 15, 2021, including interim periods within those fiscal years. An entity should apply the amendments prospectively to modifications or exchanges occurring on or after the effective date of the amendments. Early adoption is permitted for all entities, including adoption in an interim period. If an entity elects to early adopt the amendments in this Update in an interim period, the guidance should be applied as of the beginning of the fiscal year that includes that interim period. This Update is not expected to have a significant impact on the Company's financial statements.

In July 2021, the FASB issued ASU 2021-05, *Leases (Topic 842),* which amends ASC 842 so that lessors are no longer required to recognize a selling loss upon commencement of a lease with variable lease payments that, prior to the amendments, would have been classified as a sales-type or direct financing lease. Furthermore, a lessor must classify as an operating lease any lease that would otherwise be classified as a sales-type or direct financing lease and that would result in the recognition of a selling loss at lease commencement, provided that the lease includes variable lease payments that do not depend on an index or rate. For public business entities and certain not-for-profit entities and employee benefit plans that have adopted ASC 842, the amendments are effective for fiscal years beginning after December 15, 2021, and for interim periods within those fiscal years. For all other entities that have adopted ASC 842, the amendments are effective for fiscal years beginning after December 15, 2021, and for interim periods within fiscal years beginning after December 15, 2022. All entities that have adopted ASC 842 are permitted to early adopt the amendments in ASU 2021-05. The amendments in ASU 2021-05 are effective as of the same date as the guidance in ASC 842 for entities that have not adopted ASC 842. This Update is not expected to have a significant impact on the Company's financial statements.

In August 2021, the FASB issued ASU 2021-06, *Presentation of Financial Statements (Topic 205), Financial Services – Depository and Lending (Topic 942), and Financial Services – Investment Companies (Topic 946): Amendments to SEC Paragraphs Pursuant to SEC Final Rule Releases No. 33-10786, Amendments to Financial Disclosures about Acquired and Disposed Businesses, and No. 33-10835, Update of Statistical Disclosures for Bank and Savings and Loan Registrants (SEC Update)*, to amend SEC paragraphs in the Accounting Standards Codification to reflect the issuance of SEC Release No. 33-10786, *Amendments to Financial Disclosures about Acquired and Disposed Businesses*, and No. 33-10835, *Update of Statistical Disclosures for Bank and Savings and Loan Registrants*. This ASU was effective upon issuance and did not have a significant impact on the Company's financial statements.

In October 2021, the FASB issued ASU 2021-08, *Business Combinations (Topic 805): Accounting for Contract Assets and Contract Liabilities from Contracts with Customers*, which addresses how an acquirer should recognize and measure revenue contracts acquired in a business combination. For public business entities, the ASU is effective for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. For all other entities, the ASU is effective for fiscal years beginning after December 15, 2023, including interim periods within those fiscal years.

Treasury Stock

The purchase of the Company's common stock is recorded at cost. At the date of subsequent reissue, the treasury stock account is reduced by the cost of such stock on a last-in-first-out basis.

Cash Flows

The Company utilizes the net reporting of cash receipts and cash payments for deposit, short-term borrowing and lending activities.

Trust, Brokerage and Insurance Assets and Income

Assets held by the Company in a fiduciary or agency capacity for its customers are not included in the consolidated financial statements since such assets are not assets of the Company. The majority of trust revenue is earned and collected monthly, with the amount determined based on a percentage of the fair value of the trust assets under management. Trust fees are contractually agreed with each customer, and fee levels vary based mainly on the size of assets under management. None of the contracts with trust customers provide for incentive-based fees. In addition, trust revenue includes fees for provision of services, including employee benefit plan administration, tax return preparation and estate planning and settlement. Fees for such services are billed based on contractual arrangements or established fee schedules and are typically billed upon completion of providing such services. Brokerage and insurance commissions from the sales of investments and insurance products recognized on a trade date basis as the performance obligation is satisfied at the point in time in which the trade is processed. Additional fees are based on a percentage of the market value of customer accounts and billed on a monthly or quarterly basis. The Company's performance obligation under the contracts with certain customers is generally satisfied through the passage of time as the Company monitors and manages the assets in the customer's portfolio and is not dependent on certain return or performance level of the customer's portfolio. Other performance obligations (such as the delivery of account statements to customers) are generally considered immaterial to the overall transaction price.

Earnings Per Share

The following table sets forth the computation of earnings per share. Earnings per share calculations give retroactive effect to stock dividends declared by the Company.

	2021	2020	2019
Basic earnings per share computation:			
Net income applicable to common stock	**$29,118,000**	$25,103,000	$19,490,000
Weighted average common shares outstanding	**3,945,299**	3,844,241	3,597,709
Earnings per share - basic	**$7.38**	$6.53	$5.42
Diluted earnings per share computation:			
Net income applicable to common stock	**$29,118,000**	$25,103,000	$19,490,000
Weighted average common shares outstanding for basic earnings per share	**3,945,299**	3,844,241	3,597,709
Add: Dilutive effects of restricted stock	**-**	1,841	2,096
Weighted average common shares outstanding for dilutive earnings per share	**3,945,299**	3,846,082	3,599,805
Earnings per share - dilutive	**$7.38**	$6.53	$5.41

Nonvested shares of restricted stock totaling 5,494, 4,302 and 3,576 were outstanding during 2021, 2020 and 2019, respectively, but were not included in the computation of diluted earnings per common share because to do so would be anti-dilutive. These anti-dilutive shares had per share prices ranging from $44.93-63.19, $58.37-$62.93 and $52.44-$62.93 for 2021, 2020 and 2019, respectively.

Reclassification

Certain of the prior year amounts have been reclassified to conform to the current year presentation. Such reclassifications had no material effect on net income or stockholders' equity.

2. REVENUE RECOGNITION

Under ASC Topic 606, management determined that the primary sources of revenue emanating from interest and dividend income on loans and investments along with noninterest revenue resulting from investment security gains, loan servicing, gains on loans sold and earnings on bank owned life insurances are not within the scope of this topic. The main types of noninterest income within the scope of the standard are as follows:

- Service charges on deposit accounts – The Company has contracts with its deposit customers where fees are charged if certain parameters are not met. These agreements can be cancelled at any time by either the Company or the deposit customer. Revenue from these transactions is recognized on a monthly basis as the Company has an unconditional right to the fee consideration. The Company also has transaction fees related to specific transactions or activities resulting from a customer request or activity that include overdraft fees, online banking fees, interchange fees, ATM fees and other transaction fees. All of these fees are attributable to specific performance obligations of the Company where the revenue is recognized at a defined point in time upon the completion of the requested service/transaction.

- Trust fees – Typical contracts for trust services are based on a fixed percentage of the assets earned ratably over a defined period and billed on a monthly basis. Fees charged to customers' accounts are recognized as revenue over the period during which the Company fulfills its performance obligation under the contract (i.e., holding client asset in a managed fiduciary trust account). For these accounts, the performance obligation of the Company is typically satisfied by holding and managing the customer's assets over time. Other fees related to specific customer requests are attributable to specific performance obligations of the Company where the revenue is recognized at a defined point in time, upon completion of the requested service/transaction.

- Gains (losses) on sale of other real estate owned – Gains and losses are recognized at the completion of the property sale when the buyer obtains control of the real estate and all of the performance obligations of the Company have been satisfied. Evidence of the buyer obtaining control of the asset include transfer of the property title, physical possession of the asset, and the buyer obtaining control of the risks and rewards related to the asset. In situations where the Company agrees to provide financing to facilitate the sale, additional analysis is performed to ensure that the contract for sale identifies the buyer and seller, the asset to be transferred, payment terms, and that the contract has a true commercial substance and that collection of amounts due from the buyer are reasonable. In situations where financing terms are not reflective of current market terms, the transaction price is discounted impacting the gain/loss and the carrying value of the asset.

- Brokerage and insurance – Fees include commissions from the sales of investments and insurance products recognized on a trade date basis as the performance obligation is satisfied at the point in time in which the trade is processed. Additional fees are based on a percentage of the market value of customer accounts and billed on a monthly or quarterly basis. The Company's performance obligation under the contracts with certain customers is generally satisfied through the passage of time as the Company monitors and manages the assets in the customer's portfolio and is not dependent on certain return or performance level of the customer's portfolio. Fees for these services are billed monthly and are recorded as revenue at the end of the month for which the wealth management service has been performed. Other performance obligations (such as the delivery of account statements to customers) are generally considered immaterial to the overall transaction price.

The following table depicts the disaggregation of revenue derived from contracts with customers to depict the nature, amount, timing, and uncertainty of revenue and cash flows for the years ended December 31, 2021, 2020 and 2019 (in thousands). All revenue in the table below relates to goods and services transferred at a point in time.

Revenue stream			
Service charges on deposit accounts	**2021**	2020	2019
Overdraft fees	**$ 1,111**	$ 1,171	$ 1,536
Statement fees	**225**	207	206
Interchange revenue	**2,801**	2,287	2,294
ATM income	**388**	323	392
Other service charges	**230**	233	259
Total Service Charges	**4,755**	4,221	4,687
Trust	**865**	803	750
Brokerage and insurance	**1,625**	1,297	1,141
Other	**492**	339	348
Total	**$ 7,737**	$ 6,660	$ 6,926

3. RESTRICTIONS ON CASH AND DUE FROM BANKS

Effective, March 26, 2020, the Federal Reserve reduced reserve requirements to zero for all depository institutions. There were no required federal reserves included in "Cash and due from banks" at December 31, 2021 or December 31, 2020. The required reserves are used to facilitate the implementation of monetary policy by the Federal Reserve System. The required reserves are computed by applying prescribed ratios to the classes of average deposit balances. These are held in the form of vault cash and a depository amount held with the Federal Reserve Bank. Federal law prohibits the Company from borrowing from the Bank unless the loans are secured by specific collateral.

Non-retirement account deposits with one financial institution are insured up to $250,000. At times, the Company maintains cash and cash equivalents with other financial institutions in excess of the insured amount.

4. INVESTMENT SECURITIES

The amortized cost, gross unrealized gains and losses, and fair value of investment securities at December 31, 2021 and 2020 were as follows (in thousands):

December 31, 2021		Amortized Cost		Gross Unrealized Gains		Gross Unrealized Losses		Fair Value
Available-for-sale securities:								
U.S. Agency securities	**$**	**73,803**	**$**	**976**	**$**	**(834)**	**$**	**73,945**
U.S. Treasuries		**116,743**		**63**		**(1,459)**		**115,347**
Obligations of state and political subdivisions		**109,367**		**2,706**		**(52)**		**112,021**
Corporate obligations		**10,378**		**39**		**(84)**		**10,333**
Mortgage-backed securities in government sponsored entities		**101,727**		**597**		**(1,568)**		**100,756**
Total available-for-sale securities	**$**	**412,018**	**$**	**4,381**	**$**	**(3,997)**	**$**	**412,402**
December 31, 2020								
Available-for-sale securities:								
U.S. Agency securities	$	79,065	$	2,403	$	(52)	$	81,416
U.S. Treasuries		27,442		601		-		28,043
Obligations of state and political subdivisions		100,089		2,938		(55)		102,972
Corporate obligations		6,413		96		-		6,509
Mortgage-backed securities in government sponsored entities		74,512		1,874		(137)		76,249
Total available-for-sale securities	$	287,521	$	7,912	$	(244)	$	295,189

The following table shows the Company's gross unrealized losses and fair value, aggregated by investment category and length of time, that the individual securities have been in a continuous unrealized loss position, at December 31, 2021 and 2020 (in thousands). As of December 31, 2021, the Company owned 138 securities each of whose fair value was less than its cost basis.

	Less than Twelve Months				Twelve Months or Greater				Total			
2021		**Fair Value**		**Gross Unrealized Losses**		**Fair Value**		**Gross Unrealized Losses**		**Fair Value**		**Gross Unrealized Losses**
U.S. agency securities	**$**	**26,754**	**$**	**(387)**	**$**	**7,542**	**$**	**(447)**	**$**	**34,296**	**$**	**(834)**
U.S. Treasuries		**106,794**		**(1,459)**		**-**		**-**		**106,794**		**(1,459)**
Obligations of states and political subdivisions		**10,744**		**(26)**		**2,899**		**(26)**		**13,643**		**(52)**
Corporate obligations		**6,922**		**(84)**		**-**		**-**		**6,922**		**(84)**
Mortgage-backed securities in government sponsored entities		**60,182**		**(1,305)**		**7,975**		**(263)**		**68,157**		**(1,568)**
Total securities	**$**	**211,396**	**$**	**(3,261)**	**$**	**18,416**	**$**	**(736)**	**$**	**229,812**	**$**	**(3,997)**

2020	Less than Twelve Months Fair Value	Less than Twelve Months Gross Unrealized Losses	Twelve Months or Greater Fair Value	Twelve Months or Greater Gross Unrealized Losses	Total Fair Value	Total Gross Unrealized Losses
U.S. agency securities	$ 13,720	$ (52)	$ -	$ -	$ 13,720	$ (52)
Obligations of states and political subdivisions	5,407	(55)	-	-	5,407	(55)
Mortgage-backed securities in government sponsored entities	14,600	(99)	5,633	(38)	20,233	(137)
Total securities	$ 33,727	$ (206)	$ 5,633	$ (38)	$ 39,360	$ (244)

As of December 31, 2021, the Company's investment securities portfolio contained unrealized losses on U.S. Treasuries, agency securities issued or backed by the full faith and credit of the United States government or are generally viewed as having the implied guarantee of the U.S. government, obligations of states and political subdivisions, corporate obligations and mortgage backed securities in government sponsored entities. For fixed maturity available for sale investments management considers whether the present value of cash flows expected to be collected are less than the security's amortized cost basis (the difference defined as the credit loss), the magnitude and duration of the decline, the reasons underlying the decline and the Company's intent to sell the security or whether it is more likely than not that the Company would be required to sell the security before its anticipated recovery in market value, to determine whether the loss in value is other than temporary. Once a decline in value is determined to be other than temporary, if the Company does not intend to sell the security, and it is more-likely-than-not that it will not be required to sell the security, before recovery of the security's amortized cost basis, the charge to earnings is limited to the amount of credit loss. Any remaining difference between fair value and amortized cost (the difference defined as the non-credit portion) is recognized in other comprehensive income, net of applicable taxes. Otherwise, the entire difference between fair value and amortized cost is charged to earnings. As of December 31, 2021 and 2020, the Company had concluded that any impairment of its investment securities portfolio outlined in the above table is not other than temporary and is the result of interest rate changes, sector credit rating changes, or company-specific rating changes that are not expected to result in the non-collection of principal and interest during the period.

Proceeds from sales of securities available-for-sale during 2021, 2020 and 2019 were $29,198,000, $23,415,000, and $10,489,000, respectively. The gross gains realized during 2021 consisted of $177,000 and $125,000 from the sales of six treasury securities and three agency securities, respectively. The gross losses realized during 2021 consisted of $90,000 from the sale of one agency security. The gross gains realized during 2020 consisted of $344,000 from the sales of seventeen mortgage backed securities. The gross losses realized during 2020 consisted of $39,000 from the sale of two mortgage backed securities. The gross gains realized during 2019 consisted of $1,000 and $24,000 from the sales of two agency securities and four treasury securities, respectively. The gross losses realized during 2019 consisted of $1,000 from the sale of one agency security. Gross gains and gross losses were realized as follows on available for sale securities (in thousands):

	2021	2020	2019
Gross gains	**$ 302**	$ 344	$ 25
Gross losses	**(90)**	(39)	(1)
Net gains	**$ 212**	$ 305	$ 24

The following table presents the net gains (losses) on the Company's equity investments recognized in earnings during 2021, 2020 and 2019 and the portion of unrealized gains for the period that relates to equity investments held at December 31, 2021, 2020 and 2019 (in thousands):

Equity Securities	**2021**	2020	2019
Net gains (losses) recognized in equity securities during the period	**$ 339**	$ (109)	$ 120
Less: Net gains realized on the sale of equity securities during the period	**-**	68	-
Net unrealized gains (losses)	**$ 339**	$ (41)	$ 120

Investment securities with an approximate carrying value of $295,028,000 and $245,351,000 at December 31, 2021 and 2020, respectively, were pledged to secure public funds and certain other deposits as provided by law and certain borrowing arrangements of the Company.

Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. The amortized cost and fair value of debt securities at December 31, 2021, by contractual maturity are shown below (in thousands). Municipal securities that have been refunded and will therefore pay-off on the call date are reflected in the table below utilizing the call date as the date of repayment as payment is guaranteed on that date:

Available-for-sale securities:	Amortized Cost	Fair Value
Due in one year or less	$ 15,002	$ 15,175
Due after one year through five years	108,284	108,590
Due after five years through ten years	133,646	132,786
Due after ten years	155,086	155,851
Total	$ 412,018	$ 412,402

5. LOANS AND RELATED ALLOWANCE FOR LOAN LOSSES

The Company grants commercial, industrial, agricultural, residential, and consumer loans primarily to customers throughout north central, central and south central Pennsylvania, southern New York and Wilmington and Dover, Delaware. Although the Company had a diversified loan portfolio at December 31, 2021 and 2020, a substantial portion of its debtors' ability to honor their contracts is dependent on the economic conditions within these regions. The following table summarizes the primary segments of the loan portfolio, as well as how those segments are analyzed within the allowance for loan losses as of December 31, 2021 and 2020 (in thousands):

2021	**Total Loans**	**Individually evaluated for impairment**	**Loans acquired with deteriorated credit quality**	**Collectively evaluated for impairment**
Real estate loans:				
Residential	**$ 201,097**	**$ 620**	**$ 14**	**$ 200,463**
Commercial	**687,338**	**8,381**	**2,145**	**676,812**
Agricultural	**312,011**	**5,355**	**1,643**	**305,013**
Construction	**55,036**	**-**	**-**	**55,036**
Consumer	**25,858**	**-**	**-**	**25,858**
Other commercial loans	**74,585**	**186**	**-**	**74,399**
Other agricultural loans	**39,852**	**991**	**-**	**38,861**
State and political subdivision loans	**45,756**	**-**	**-**	**45,756**
Total	**1,441,533**	**15,533**	**3,802**	**1,422,198**
Allowance for loan losses	**17,304**	**121**	**-**	**17,183**
Net loans	**$ 1,424,229**	**$ 15,412**	**$ 3,802**	**$ 1,405,015**
2020				
Real estate loans:				
Residential	$ 201,911	$ 990	$ 20	$ 200,901
Commercial	596,255	9,183	2,937	584,135
Agricultural	315,158	4,645	1,686	308,827
Construction	35,404	-	-	35,404
Consumer	30,277	2	-	30,275
Other commercial loans	114,169	1,335	232	112,602
Other agricultural loans	48,779	1,122	-	47,657
State and political subdivision loans	63,328	-	-	63,328
Total	1,405,281	17,277	4,875	1,383,129
Allowance for loan losses	15,815	510	-	15,305
Net loans	$ 1,389,466	$ 16,767	$ 4,875	$ 1,367,824

During 2021 the Company continued to participate in the Paycheck Protection Program ("PPP"), administered directly by the U.S. SBA. The PPP provides loans to small businesses who were affected by economic conditions as a result of COVID-19 to provide cash-flow assistance to employers who maintain their payroll (including healthcare and certain related expenses), mortgage interest, rent, leases, utilities and interest on existing debt during the COVID-19 emergency. As of December 31, 2021 and 2020, the Company had outstanding principal balances of $6.8 million and $37.2 million, respectively, of PPP loans that are included in other commercial loans. During 2021, the Company originated $24.3 million of loans, of which $6.0 million remain outstanding as of December 31, 2021. During 2020, the Company originated $54.3 million of loans under this program of which

$806,000 remain outstanding as of December 31, 2021. The PPP loans are fully guaranteed by the SBA, have an interest rate of 1.0% per annum, and may be eligible for forgiveness by the SBA to the extent that the proceeds are used to cover eligible payroll costs, interest costs, rent, and utility costs over a period of up to 24 weeks after the loan is made as long as certain conditions are met regarding employee retention and compensation levels. PPP loans deemed eligible for forgiveness by the SBA will be repaid by the SBA to the Company. The SBA has issued guidance for forgiveness with a streamlined approach for loans of $150,000 or less.

In accordance with the SBA terms and conditions on these PPP loans, the Company received approximately $3.8 million in fees associated with the processing of these loans in 2021 and 2020. Upon funding of the loan, these fees were deferred and will be amortized over the life of the loan as an adjustment to yield in accordance with FASB ASC 310-20-25-2. As of December 31, 2021, $270,000 of deferred fees remain to be amortized related to the PPP loans.

As of December 31, 2021 and 2020, net unamortized loan fees, including PPP fees, and costs of $2,038,000 and $2,344,000, respectively, were included in the carrying value of loans. Purchased loans acquired in connection with the FNB acquisition, the State College branch acquisition and the MidCoast acquisition were recorded at fair value on their acquisition date without a carryover of the related allowance for loan losses.

Upon acquisition, the Company evaluated whether an acquired loan was within the scope of ASC 310-30, Receivables-Loans and Debt Securities Acquired with Deteriorated Credit Quality. PCI loans are loans that have evidence of credit deterioration since origination and it is probable at the date of acquisition that the Company will not collect all contractually required principal and interest payments. The fair value of PCI loans, on the acquisition date, was determined, primarily based on the fair value of the loans' collateral. The carrying value of PCI loans was $3,802,000 and $4,875,000 at December 31, 2021 and 2020, respectively. The carrying value of the PCI loans was determined by projected discounted contractual cash flows.

On the acquisition date, the preliminary estimate of the unpaid principal balance for all loans evidencing credit impairment acquired in the MidCoast acquisition was $8,005,000 and the estimated fair value of the loans was $4,869,000. Total contractually required payments on these loans, including interest, at the acquisition date was $8,801,000. However, the Company's preliminary estimate of expected cash flows was $5,835,000 at the acquisition date. At the acquisition date, the Company established a credit risk related non-accretable discount (a discount representing amounts which are not expected to be collected from the customer nor liquidation of collateral) of $2,966,000 relating to these impaired loans, reflected in the recorded net fair value. Such amount is reflected as a non-accretable fair value adjustment to loans. The Company further estimated the timing and amount of expected cash flows in excess of the estimated fair value and established an accretable discount of $966,000 on the acquisition date relating to these impaired loans.

The table below presents the components of the purchase accounting adjustments related to the purchased impaired loans acquired in the MidCoast Acquisition as of April 17, 2020 (in thousands):

	April 17, 2020
Contractually required principal and interest at acquisition	$ 8,801
Non-accretable discount	(2,966)
Expected cash flows	5,835
Accretable discount	(966)
Estimated fair value	$ 4,869

Changes in the accretable discount for PCI loans were as follows for the years ended December 31, 2021 and 2020 (in thousands):

	December 31, 2021	December 31, 2020
Balance at beginning of period	**$ 788**	$ 89
Addition due to MidCoast Acquisition	**-**	966
Accretion	**(499)**	(267)
Reclassification of non-accretable discount	**81**	-
Balance at end of period	**$ 370**	$ 788

The following table presents additional information regarding PCI loans (in thousands):

	December 31, 2021	December 31, 2020
Outstanding balance	$ 6,159	$ 8,958
Carrying amount	3,802	4,875

Real estate loans serviced for Freddie Mac, Fannie Mae and the FHLB, which are not included in the Consolidated Balance Sheet, totaled $197,037,000 and $178,986,000 at December 31, 2021 and 2020, respectively. Loans sold to Freddie Mac and Fannie Mae were sold without recourse and total $184,897,000 and $162,050,000 at December 31, 2021 and 2020, respectively. Additionally, the Bank acquired a portfolio of loans sold to the FHLB during the acquisition of FNB, which were sold under the Mortgage Partnership Finance Program ("MPF"). The Bank was not an active participant in the MPF program in 2021 or 2020. The MPF portfolio balance was $12,140,000 and $16,936,000 at December 31, 2021 and 2020, respectively. The FHLB maintains a first-loss position for the MPF portfolio that totals $157,000. Should the FHLB exhaust its first-loss position, recourse to the Bank's credit enhancement would be up to the next $590,000 of losses. The Bank did not experience any losses for the MPF portfolio during 2021, 2020 or 2019.

The segments of the Bank's loan portfolio are disaggregated into classes to a level that allows management to monitor risk and performance. Residential real estate mortgages consist of 15 to 30 year first mortgages on residential real estate, while residential real estate home equities are consumer purpose installment loans or lines of credit secured by a mortgage which is often a second lien on residential real estate with terms of 15 years or less. Commercial real estate are business purpose loans secured by a mortgage on commercial real estate. Agricultural real estate are loans secured by a mortgage on real estate used in agriculture production. Construction real estate are loans secured by residential or commercial real estate used during the construction phase of residential and commercial projects. Consumer loans are typically unsecured or primarily secured by collateral other than real estate and overdraft lines of credit connected with customer deposit accounts. Other commercial loans are loans for commercial purposes primarily secured by non-real estate collateral. Other agricultural loans are loans for agricultural purposes primarily secured by non real estate collateral. State and political subdivisions are loans for state and local municipalities for capital and operating expenses or tax free loans used to finance commercial development.

Management considers other commercial loans, other agricultural loans, commercial and agricultural real estate loans and state and political subdivision loans which are 90 days or more past due to be impaired. Certain residential mortgages, home equity and consumer loans that are cross collateralized with commercial relationships determined to be impaired may be classified as impaired as well. These loans are analyzed to determine if it is probable that all amounts will not be collected according to the contractual terms of the loan agreement. If management determines that the value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized through an allowance allocation or a charge-off to the allowance.

The following table includes the recorded investment and unpaid principal balances for impaired loans by class, with the associated allowance amount as of December 31, 2021 and 2020, if applicable (in thousands):

2021	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance
Real estate loans:					
Mortgages	$ 697	$ 495	$ 45	$ 540	$ 6
Home Equity	97	37	43	80	6
Commercial	9,330	8,096	285	8,381	61
Agricultural	5,694	5,167	188	5,355	14
Consumer	-	-	-	-	-
Other commercial loans	813	92	94	186	34
Other agricultural loans	1,274	991	-	991	-
Total	$ 17,905	$ 14,878	$ 655	$ 15,533	$ 121

2020	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance
Real estate loans:					
Mortgages	$ 1,070	$ 740	$ 123	$ 863	$ 9
Home Equity	150	70	57	127	9
Commercial	9,847	8,323	860	9,183	95
Agricultural	4,811	2,799	1,846	4,645	83
Consumer	2	2	-	2	-
Other commercial loans	1,908	1,094	241	1,335	170
Other agricultural loans	1,262	19	1,103	1,122	144
Total	$ 19,050	$ 13,047	$ 4,230	$ 17,277	$ 510

The following table includes the average investment in impaired loans and the income recognized on impaired loans for 2021, 2020 and 2019 (in thousands):

2021	**Average Recorded Investment**	**Interest Income Recognized**	**Interest Income Recognized Cash Basis**
Real estate loans:			
Mortgages	**$ 682**	**$ 16**	**$ -**
Home Equity	**99**	**4**	**-**
Commercial	**8,789**	**288**	**31**
Agricultural	**4,562**	**82**	**-**
Other commercial loans	**704**	**2**	**-**
Other agricultural loans	**1,044**	**3**	**-**
Total	**$ 15,880**	**$ 395**	**$ 31**
2020			
Real estate loans:			
Mortgages	$ 956	$ 20	$ -
Home Equity	139	6	-
Commercial	10,354	358	27
Agricultural	3,918	75	-
Consumer	3	-	-
Other commercial loans	1,671	3	-
Other agricultural loans	1,237	6	-
Total	$ 18,278	$ 468	$ 27
2019			
Real estate loans:			
Mortgages	$ 1,062	$ 16	$ -
Home Equity	119	6	-
Commercial	11,756	453	24
Agricultural	4,899	78	-
Consumer	2	-	-
Other commercial loans	2,056	1	-
Other agricultural loans	1,400	4	-
Total	$ 21,294	$ 558	$ 24

Credit Quality Information

For commercial real estate loans, agricultural real estate loans, construction loans, other commercial loans, other agricultural loans and state and political subdivision loans, management uses a nine point internal risk rating system to monitor the credit quality. The first five categories are considered not criticized and are aggregated as “Pass” rated. The criticized rating categories utilized by management generally follow bank regulatory definitions. The definitions of each rating are defined below:

- Pass (Grades 1-5) – These loans are to customers with credit quality ranging from an acceptable to very high quality and are protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral.

- Special Mention (Grade 6) – This loan grade is in accordance with regulatory guidance and includes loans where a potential weakness or risk exists, which could cause a more serious problem if not corrected.

- Substandard (Grade 7) – This loan grade is in accordance with regulatory guidance and includes loans that have a well-defined weakness based on objective evidence and are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

- Doubtful (Grade 8) – This loan grade is in accordance with regulatory guidance and includes loans that have all the weaknesses inherent in a substandard asset. In addition, these weaknesses make collection or liquidation in full highly questionable and improbable, based on existing circumstances.

- Loss (Grade 9) – This loan grade is in accordance with regulatory guidance and includes loans that are considered uncollectible, or of such value that continuance as an asset is not warranted.

To help ensure that risk ratings are accurate and reflect the present and future capacity of borrowers to repay the loan as agreed, the Company's loan rating process includes several layers of internal and external oversight. The Company's loan officers are responsible for the timely and accurate risk rating of the loans in each of their portfolios at origination and on an ongoing basis under the supervision of management. All commercial and agricultural loans are reviewed annually to ensure the appropriateness of the loan grade. In addition, the Company engages an external consultant on at least an annual basis. The external consultant is engaged to 1) review a minimum of 50% of the dollar volume of the commercial loan portfolio on an annual basis, 2) review new loans originated over $1.0 million in the last years, 3) review a majority of borrowers with commitments greater than or equal to $1.0 million, 4) review selected loan relationships over $750,000 which are over 30 days past due, or classified Special Mention, Substandard, Doubtful, or Loss, and 5) such other loans which management or the consultant deems appropriate.

The following tables represent credit exposures by internally assigned grades as of December 31, 2021 and 2020 (in thousands):

2021	**Pass**	**Special Mention**	**Substandard**	**Doubtful**	**Loss**	**Ending Balance**
Real estate loans:						
Commercial	**$ 646,137**	**$ 35,332**	**$ 5,869**	**$ -**	**$ -**	**$ 687,338**
Agricultural	**291,537**	**15,105**	**5,369**	**-**	**-**	**312,011**
Construction	**55,036**	**-**	**-**	**-**	**-**	**55,036**
Other commercial loans	**70,932**	**3,289**	**316**	**48**	**-**	**74,585**
Other agricultural loans	**37,800**	**1,351**	**701**	**-**	**-**	**39,852**
State and political subdivision loans	**45,588**	**168**	**-**	**-**	**-**	**45,756**
Total	**$ 1,147,030**	**$ 55,245**	**$ 12,255**	**$ 48**	**$ -**	**$ 1,214,578**

2020	Pass	Special Mention	Substandard	Doubtful	Loss	Ending Balance
Real estate loans:						
Commercial	$ 563,121	$ 24,329	$ 8,805	$ -	$ -	$ 596,255
Agricultural	289,216	14,307	11,635	-	-	315,158
Construction	35,404	-	-	-	-	35,404
Other commercial loans	106,604	3,808	3,672	85	-	114,169
Other agricultural loans	45,758	1,431	1,590	-	-	48,779
State and political subdivision loans	58,649	4,372	307	-	-	63,328
Total	$ 1,098,752	$ 48,247	$ 26,009	$ 85	$ -	$ 1,173,093

For residential real estate mortgages, home equities and consumer loans, credit quality is monitored based on whether the loan is performing or non-performing, which is typically based on the aging status of the loan and payment activity, unless a specific action, such as bankruptcy, repossession, death or significant delay in payment occurs to raise awareness of a possible credit event. Non-performing loans include those loans that are considered nonaccrual, described in more detail below and all loans past due 90 or more days. The following table presents the recorded investment in those loan classes based on payment activity as of December 31, 2021 and 2020 (in thousands):

2021	**Performing**	**Non-performing**	**PCI**	**Total**
Real estate loans:				
Mortgages	**$ 150,320**	**$ 608**	**$ 14**	**$ 150,942**
Home Equity	**50,122**	**33**	**-**	**50,155**
Consumer	**25,858**	**-**	**-**	**25,858**
Total	**$ 226,300**	**$ 641**	**$ 14**	**$ 226,955**

2020	Performing	Non-performing	PCI	Total
Real estate loans:				
Mortgages	$ 145,843	$ 1,039	$ 20	$ 146,902
Home Equity	54,961	48	-	55,009
Consumer	30,247	30	-	30,277
Total	$ 231,051	$ 1,117	$ 20	$ 232,188

Aging Analysis of Past Due Loans by Class

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by the length of time a recorded payment is past due. The following table includes an aging analysis of the recorded investment of past due loans as of December 31, 2021 and 2020 (in thousands):

2021	**30-59 Days Past Due**	**60-89 Days Past Due**	**90 Days Or Greater**	**Total Past Due**	**Current**	**PCI**	**Total Financing Receivables**	**90 Days and Accruing**
Real estate loans:								
Mortgages	**$ 220**	**$ 170**	**$ 209**	**$ 599**	**$ 150,329**	**$ 14**	**$ 150,942**	**$ 13**
Home Equity	**103**	**-**	**33**	**136**	**50,019**	**-**	**50,155**	**33**
Commercial	**127**	**115**	**1,969**	**2,211**	**682,982**	**2,145**	**687,338**	**-**
Agricultural	**31**	**-**	**1,367**	**1,398**	**308,970**	**1,643**	**312,011**	**-**
Construction	**-**	**-**	**-**	**-**	**55,036**	**-**	**55,036**	**-**
Consumer	**163**	**1**	**-**	**164**	**25,694**	**-**	**25,858**	**-**
Other commercial loans	**17**	**10**	**92**	**119**	**74,466**	**-**	**74,585**	**-**
Other agricultural loans	**10**	**-**	**-**	**10**	**39,842**	**-**	**39,852**	**-**
State and political subdivision loans	**-**	**-**	**-**	**-**	**45,756**	**-**	**45,756**	**-**
Total	**$ 671**	**$ 296**	**$ 3,670**	**$ 4,637**	**$ 1,433,094**	**$ 3,802**	**$ 1,441,533**	**$ 46**
Loans considered non-accrual	**$ -**	**$ -**	**$ 3,624**	**$ 3,624**	**$ 3,992**	**$ -**	**$ 7,616**	
Loans still accruing	**671**	**296**	**46**	**1,013**	**1,429,102**	**3,802**	**1,433,917**	
Total	**$ 671**	**$ 296**	**$ 3,670**	**$ 4,637**	**$ 1,433,094**	**$ 3,802**	**$ 1,441,533**	

2020	30-59 Days Past Due	60-89 Days Past Due	90 Days Or Greater	Total Past Due	Current	PCI	Total Financing Receivables	90 Days and Accruing
Real estate loans:								
Mortgages	$ 864	$ 414	$ 518	$ 1,796	$ 145,086	$ 20	$ 146,902	$ 252
Home Equity	152	62	34	248	54,761	-	55,009	23
Commercial	836	439	1,822	3,097	590,221	2,937	596,255	70
Agricultural	2,283	-	1,329	3,612	309,860	1,686	315,158	150
Construction	-	-	-	-	35,404	-	35,404	-
Consumer	147	9	30	186	30,091	-	30,277	30
Other commercial loans	930	-	133	1,063	112,874	232	114,169	-
Other agricultural loans	1,044	-	-	1,044	47,735	-	48,779	-
State and political subdivision loans	-	-	-	-	63,328	-	63,328	-
Total	$ 6,256	$ 924	$ 3,866	$ 11,046	$ 1,389,360	$ 4,875	$ 1,405,281	$ 525
Loans considered non-accrual	$ 3,032	$ 28	$ 3,341	$ 6,401	$ 4,331	$ -	$ 10,732	
Loans still accruing	3,224	896	525	4,645	1,385,029	4,875	1,394,549	
Total	$ 6,256	$ 924	$ 3,866	$ 11,046	$ 1,389,360	$ 4,875	$ 1,405,281	

Nonaccrual Loans

Loans are considered for nonaccrual status upon reaching 90 days delinquency, unless the loan is well secured and in the process of collection, although the Company may be receiving partial payments of interest and partial repayments of principal on such loans or if full payment of principal and interest is not expected.

The following table reflects the loans on nonaccrual status as of December 31, 2021 and 2020, respectively. The balances are presented by class of loan (in thousands):

	2021	2020
Real estate loans:		
Mortgages	$ 595	$ 787
Home Equity	-	25
Commercial	2,945	4,529
Agricultural	3,133	3,133
Other commercial loans	140	1,284
Other agricultural loans	803	974
	$ 7,616	$ 10,732

Interest income on loans would have increased by approximately $573,000, $756,000 and $647,000 during 2021, 2020 and 2019, respectively, if these loans had performed in accordance with their terms.

Loan Modifications Related to COVID-19

The Company has elected to follow the loan modification guidance under Section 4013 of the CARES Act with regard to COVID-19 modifications made between March 1, 2020 and the earlier of either January 1, 2022 or the 60th day after the end of the COVID-19 national emergency. Under section 4013 of the CARES Act, loans less than 30 days past due as of December 31, 2019 will be considered current for COVID-19 modifications. A financial institution can then suspend the requirements under GAAP for loan modifications related to COVID-19 that would otherwise be categorized as a TDR, and suspend any determination of a loan modified as a result of COVID-19 as being a TDR, including the requirement to determine impairment for accounting purposes. Similarly, the Financial Accounting Standards Board has confirmed that short-term modifications made on a good-faith basis in response to COVID-19 to loan customers who were current prior to any relief are not TDRs. A modification of six months or less is considered to be a short-term loan modification. In response to the COVID-19 pandemic, the Company has prudently executed loan modifications for existing loan customers, which includes deferrals of interest and in certain cases deferrals of principal and interest. The following table presents information regarding loans which were subject to a loan modification related to COVID-19 during 2021, with balances as of December 31, 2020 and December 31, 2021, as well as the balance by modification type as of December 31, 2021 (dollars in thousands).

	Number of loans	Balance as of December 31, 2020	Number of loans	Balance as of December 31, 2021	Principal and Interest Deferral	Principal Deferral	% of loans as of December 31, 2021
Real estate loans:							
Mortgages	1	$ 209	-	$ -	$ -	$ -	0.00%
Home Equity	1	49	-	-	-	-	0.00%
Commercial	12	26,039	-	-	-	-	0.00%
Agricultural	3	181	-	-	-	-	0.00%
Other commercial loans	2	249	-	-	-	-	0.00%
Total	19	$ 26,727	-	$ -	$ -	$ -	0.00%

Troubled Debt Restructurings (TDRs)

In situations where, for economic or legal reasons related to a borrower's financial difficulties, management may grant a concession for other than an insignificant period of time to the borrower that would not otherwise be considered, the related loan is classified as a TDR. Management strives to identify borrowers in financial difficulty early and work with them to modify 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 by calculating the present value of the revised loan terms and comparing this balance to the Company's investment in the loan prior to the restructuring. As these loans are individually evaluated, they are excluded from pooled portfolios when calculating the allowance for loan and lease losses and a separate allocation within the allowance for loan and lease losses is provided. Management continually evaluates loans that are considered TDRs, including payment history under the modified loan terms, the borrower's ability to continue to repay the loan based on continued evaluation of their operating results and cash flows from operations. Based on this evaluation management would no longer consider a loan to be a TDR when the relevant facts support such a conclusion. As of December 31, 2021, 2020 and 2019, included within the allowance for loan losses are reserves of $26,000, $257,000 and $345,000, respectively, that are associated with loans modified as TDRs.

Loan modifications that are considered TDRs completed during the years ended December 31, 2021, 2020 and 2019 were as follows (dollars in thousands):

2021	**Number of contracts**		**Pre-modification Outstanding Recorded Investment**		**Post-Modification Outstanding Recorded Investment**	
	Interest Modification	**Term Modification**	**Interest Modification**	**Term Modification**	**Interest Modification**	**Term Modification**
Real estate loans:						
Commercial	**-**	**4**	**$ -**	**$ 1,469**	**$ -**	**$ 1,469**
Agricultural	**-**	**4**	**-**	**2,090**	**-**	**2,090**
Total	**-**	**8**	**$ -**	**$ 3,559**	**$ -**	**$ 3,559**
2020						
Real estate loans:						
Mortgages	-	1	$ -	$ 2	$ -	$ 2
Commercial	-	10	-	2,456	-	2,456
Agricultural	-	2	-	494	-	494
Consumer	-	1	-	3		3
Other commercial loans	-	2	-	1,094		1,094
Other agricultural loans	-	1	-	19	-	19
Total	-	17	$ -	$ 4,068	$ -	$ 4,068
2019						
Real estate loans:						
Mortgages	-	1	$ -	$ 4	$ -	$ 4
Home Equity	-	1	-	40	-	40
Commercial	-	6	-	918	-	918
Agricultural	-	5	-	1,731	-	1,731
Consumer	-	1	-	3		3
Other commercial loans	-	1	-	55		55
Other agricultural loans	-	5	-	1,054	-	1,054
Total	-	20	$ -	$ 3,805	$ -	$ 3,805

Recidivism, or the borrower defaulting on its obligation pursuant to a modified loan, results in the loan once again becoming a non-accrual loan. Recidivism occurs at a notably higher rate than do defaults on new origination loans, so modified loans present a higher risk of loss than do new origination loans. The following table presents the recorded investment in loans that were modified as TDRs during each 12-month period prior to the current reporting periods, which begin January 1, 2021, 2020 and 2019, respectively, and that subsequently defaulted during these reporting periods (dollars in thousands):

	December 31, 2021		December 31, 2020		December 31, 2019	
	Number of contracts	**Recorded investment**	Number of contracts	Recorded investment	Number of contracts	Recorded investment
Real estate loans:						
Commercial	**-**	**$ -**	1	$ 110	-	$ -
Agricultural	**-**	**-**	-	-	1	1,439
Other agricultural loans	**-**	**-**	-	-	3	137
Total recidivism	**-**	**$ -**	1	$ 110	4	$ 1,576

Foreclosed Assets Held For Sale

Foreclosed assets acquired in settlement of loans are carried at fair value, less estimated costs to sell, and are included in other assets on the Consolidated Balance Sheet. As of December 31, 2021 and 2020 included with other assets are $1,180,000 and $1,836,000, respectively, of foreclosed assets. As of December 31, 2021, included within the foreclosed assets is $353,000 of consumer residential mortgages that were foreclosed on or received via a deed in lieu transaction prior to the period end. As of December 31, 2021, the Company has initiated formal foreclosure proceedings on $224,000 of consumer residential mortgages, which have not yet been transferred into foreclosed assets.

Allowance for Loan Losses

The following tables roll forward the balance of the allowance for loan and lease losses for the years ended December 31, 2021, 2020 and 2019 and is segregated into the amount required for loans individually evaluated for impairment and the amount required for loans collectively evaluated for impairment as of December 31, 2021, 2020 and 2019 (in thousands):

	Balance at December 31, 2020	**Charge-offs**	**Recoveries**	**Provision**	**Balance at December 31, 2021**	**Individually evaluated for impairment**	**Collectively evaluated for impairment**
Real estate loans:							
Residential	**$ 1,174**	**$ -**	**$ -**	**$ (27)**	**$ 1,147**	**$ 12**	**$ 1,135**
Commercial	**6,216**	**(54)**	**89**	**1,848**	**8,099**	**61**	**8,038**
Agricultural	**4,953**	**-**	**-**	**(224)**	**4,729**	**14**	**4,715**
Construction	**122**	**-**	**-**	**312**	**434**	**-**	**434**
Consumer	**321**	**(27)**	**21**	**(53)**	**262**	**-**	**262**
Other commercial loans	**1,226**	**(133)**	**43**	**(113)**	**1,023**	**34**	**989**
Other agricultural loans	**864**	**-**	**-**	**(306)**	**558**	**-**	**558**
State and political subdivision loans	**479**	**-**	**-**	**(198)**	**281**	**-**	**281**
Unallocated	**460**	**-**	**-**	**311**	**771**	**-**	**771**
Total	**$ 15,815**	**$ (214)**	**$ 153**	**$ 1,550**	**$ 17,304**	**$ 121**	**$ 17,183**

	Balance at December 31, 2019	Charge-offs	Recoveries	Provision	Balance at December 31, 2020	Individually evaluated for impairment	Collectively evaluated for impairment
Real estate loans:							
Residential	$ 1,114	$ -	$ 14	$ 46	$ 1,174	$ 18	$ 1,156
Commercial	4,549	(435)	37	2,065	6,216	95	6,121
Agricultural	5,022	(4)	19	(84)	4,953	83	4,870
Construction	43	-	-	79	122	-	122
Consumer	112	(50)	21	238	321	-	321
Other commercial loans	1,255	(44)	12	3	1,226	170	1,056
Other agricultural loans	961	-	-	(97)	864	144	720
State and political subdivision loans	536	-	-	(57)	479	-	479
Unallocated	253	-	-	207	460	-	460
Total	$ 13,845	$ (533)	$ 103	$ 2,400	$ 15,815	$ 510	$ 15,305

	Balance at December 31, 2018	Charge-offs	Recoveries	Provision	Balance at December 31, 2019	Individually evaluated for impairment	Collectively evaluated for impairment
Real estate loans:							
Residential	$ 1,105	$ (32)	$ -	$ 41	$ 1,114	$ 32	$ 1,082
Commercial	4,115	(578)	-	1,012	4,549	251	4,298
Agricultural	4,264	-	-	758	5,022	151	4,871
Construction	58	-	-	(15)	43	-	43
Consumer	120	(49)	33	8	112	-	112
Other commercial loans	1,354	(38)	10	(71)	1,255	147	1,108
Other agricultural loans	752	(60)	-	269	961	154	807
State and political subdivision loans	762	-	-	(226)	536	-	536
Unallocated	354	-	-	(101)	253	-	253
Total	$ 12,884	$ (757)	$ 43	$ 1,675	$ 13,845	$ 735	$ 13,110

As discussed in Footnote 1, management evaluates various qualitative factors on a quarterly basis. The following are explanations for the changes in the allowance by portfolio segments:

2021

Residential - There was a decrease in the historical loss factor for residential loans when comparing 2020 and 2021 and a slight decrease in the specific reserve for residential loans between 2020 and 2021. The qualitative factor for the level of past due loans for residential real estate loans was decreased due to a decrease in past due loans during 2021.

Commercial real estate– There was a decrease in the historical loss factor and the specific reserve for commercial real estate loans from 2020 to 2021. The qualitative factor for the volume of non-accrual loans was decreased for commercial real estate loans due to a decrease in the volume of non-accrual loans during 2021. The decrease in the qualitative factors was offset by the increase in the commercial real estate portfolio, which resulted in the provision for 2021.

Agricultural real estate – There was no change in the historical loss factor for agricultural real estate loans from 2020 to 2021 The specific reserve for agricultural real estate loans decreased from 2020 to 2021. The qualitative factor for the volume and severity of classified, adversely or graded loans was decreased for agricultural real estate loans during 2021 due to a decrease in substandard loans.

Construction - There was no change in the historical loss factor or specific reserve for construction loans from 2020 to 2021. The qualitative factors for trends in volume, terms and nature of the portfolio, experience and depth of lending management and relevant staff, and changes in value of underlying value of collateral were increased for the construction loan portfolio during 2021 due to the increase in the overall size of the portfolio, the increase in the size of individual construction loans and the complexity of the construction projects funded.

Consumer - There was a decrease in the historical loss factor for consumer loans from 2020 to 2021. The negative provision was due to a decrease in consumer loans.

Other commercial - There was an increase in the historical loss factor for other commercial loans when comparing 2020 and 2021. The specific reserve for other commercial loans decreased from 2020 to 2021. The qualitative factors for the level of past due loans, the volume of non-accrual loans and the volume and severity of classified, adversely or graded loans were decreased for other commercial loans due to a decrease in past due loans, non-accrual loans and substandard loans during 2021.

Other agricultural - There was a decrease in the historical loss factor for other agricultural loans from 2020 to 2021. The specific reserve for other agricultural loans decreased from 2020 to 2021. The qualitative factor for the volume and severity of classified, adversely or graded loans was decreased for other agricultural loans during 2021 due to a decrease in substandard loans. The negative provision was primarily due to the overall decrease in other agricultural loans.

Municipal loans - There was no change in the historical loss factor or specific reserve for municipal loans from 2020 to 2021. The qualitative factor for the volume and severity of classified, adversely or graded loans was decreased for municipal loans during 2021 due to a decrease in substandard loans. The negative provision was primarily due to the overall decrease in other municipal loans during 2021.

2020

Residential - There was a slight decrease in the historical loss factor for residential loans when comparing 2019 and 2020 and a slight decrease in the specific reserve for residential loans between 2019 and 2020. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for residential loan categories due to a general deterioration in economic activity and increase in unemployment as a result of the Covid-19 pandemic during 2020.

Commercial real estate– There was an increase in the historical loss factor for commercial real estate loans from 2019 to 2020. The specific reserve for commercial real estate loans decreased from 2019 to 2020. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for commercial real estate loan categories due to a general deterioration in economic activity and increase in unemployment as a result of the Covid-19 pandemic during 2020.

Agricultural real estate – There was a decrease in the historical loss factor and specific reserve for agricultural real estate loans from 2019 to 2020. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for agricultural real estate loans due to a general deterioration in economic activity and increase in unemployment as a result of the Covid-19 pandemic during 2020.

Consumer - There was a slight decrease in the historical loss factor for consumer loans from 2019 to 2020. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for consumer loan categories due to a general deterioration in economic activity and increase in unemployment as a result of the Covid-19 pandemic during 2020.

Other commercial - There was an increase in the historical loss factor for other commercial loans when comparing 2019 and 2020. The specific reserve for other commercial loans increased from 2019 to 2020. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for other commercial loans due to a general deterioration in economic activity and increase in unemployment as a result of the Covid-19 pandemic during 2020. The majority of the increase in other commercial loans was attributable to PPP loans, which are guaranteed by the SBA and therefore do not have an associated allowance and loans acquired in the MidCoast acquisition, which are not subject to the allowance.

Other agricultural - There was a slight decrease in the historical loss factor for other agricultural loans from 2019 to 2020. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for other agricultural loan categories due to a general deterioration in economic activity and increase in unemployment as a result of the Covid-19 pandemic during 2020.

Municipal loans - There was no change in the historical loss factor or specific reserve for municipal loans from 2019 to 2020. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for municipal loans due to a general deterioration in economic activity and increase in unemployment as a result of the Covid-19 pandemic during 2020. The negative provision for state and political loans in 2020 is due to the decrease in the amount of state and political loans outstanding from 2019 to 2020.

2019

Residential - There was a slight increase in the historical loss factor for residential loans when comparing 2018 and 2019. The specific reserve for residential loans decreased slightly between 2018 and 2019. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for residential loan categories due to an increase in the unemployment rates in the local economy during 2019.

Commercial real estate– There was an increase in the historical loss factor for commercial real estate loans from 2018 to 2019. The specific reserve for commercial real estate loans increased from 2018 to 2019. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for all commercial real estate loans due to an increase in the unemployment rates in the local economy during 2019. The qualitative factors for changes in the levels of and trends in delinquencies, impaired and classified loans was decreased due to a lower amount of classified and past due loans.

Agricultural real estate – There was an increase in the historical loss factor for agricultural real estate loans from 2018 to 2019. The specific reserve for agricultural real estate loans increased from 2018 to 2019. The qualitative factors for changes in levels of and trends in delinquencies, impaired/classified loans were increased for agricultural real estate due to an increase in classified loans. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for agricultural real estate loans due to an increase in the unemployment rates in the local economy during 2019.

Other commercial - There was a slight decrease in the historical loss factor for other commercial loans when comparing 2018 and 2019. The specific reserve for other commercial loans decreased from 2018 to 2019. The qualitative factors for changes in levels of and trends in delinquencies, impaired/classified loans were decreased for other commercial loans due to a decrease in classified and non-accrual loans. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for other commercial loans due to an increase in the unemployment rates in the local economy during 2019.

Other agricultural - There was a slight increase in the historical loss factor for other agricultural loans from 2018 to 2019. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for other agricultural loan categories due to an increase in the unemployment rates in the local economy during 2019.

Municipal loans - There was no change in the historical loss factor or specific reserve for municipal loans from 2018 to 2019. The qualitative factor for national, state, regional and local economic trends and business conditions was increased for municipal loans due to an increase in the unemployment rates in the local economy during 2019. The qualitative factors for changes in the levels of and trends in delinquencies, impaired and classified loans was decreased due to a lower amount of special mention loans.

6. PREMISES & EQUIPMENT

Premises and equipment at December 31, 2021 and 2020 are summarized as follows (in thousands):

	December 31, 2021	December 31, 2020
Land	**$ 5,462**	$ 5,385
Buildings	**20,094**	19,373
Furniture, fixtures and equipment	**7,275**	7,046
Construction in process	**67**	147
	32,898	31,951
Less: accumulated depreciation	**15,882**	15,003
Premises and equipment, net	**$ 17,016**	$ 16,948

Depreciation expense amounted to $922,000, $921,000 and $784,000 for 2021, 2020 and 2019, respectively.

7. GOODWILL AND OTHER INTANGIBLE ASSETS

The following table provides the gross carrying value and accumulated amortization of intangible assets as of December 31, 2021 and 2020 (in thousands):

	December 31, 2021			December 31, 2020		
	Gross carrying value	**Accumulated amortization**	**Net carrying value**	Gross carrying value	Accumulated amortization	Net carrying value
Amortized intangible assets (1):						
MSRs	**$ 2,499**	**$ (1,326)**	**$ 1,173**	$ 2,153	$ (1,131)	$ 1,022
Core deposit intangibles	**1,943**	**(1,489)**	**454**	1,943	(1,297)	646
Total amortized intangible assets	**$ 4,442**	**$ (2,815)**	**$ 1,627**	$ 4,096	$ (2,428)	$ 1,668
Unamortized intangible assets:						
Goodwill	**$ 31,376**			$ 31,376		

(1) Excludes fully amortized intangible assets

The following table provides the current year and estimated future amortization expense for the next five years of amortized intangible assets (in thousands). We based our projections of amortization expense shown below on existing asset balances at December 31, 2021. Future amortization expense may vary from these projections:

		MSRs		Core deposit intangibles		Total
Year ended December 31, 2021	**$**	**265**	**$**	**192**	**$**	**457**
Estimate for year ended December 31,						
2022		305		156		461
2023		244		121		365
2024		192		86		278
2025		146		50		196
2026		107		17		124

8. FEDERAL HOME LOAN BANK (FHLB) STOCK

As a member of the FHLB of Pittsburgh, the Bank is required to maintain a minimum investment in stock of the FHLB that varies with the level of advances outstanding with the FHLB. As of December 31, 2021 and 2020, included in other assets, the Bank held $3,292,000 and $4,593,000, respectively, of FHLB stock. The stock does not have a readily determinable fair value and as such is classified as restricted stock, carried at cost and evaluated by management. The stock's value is determined by the ultimate recoverability of the par value rather than by recognizing temporary declines. The determination of whether the par value will ultimately be recovered is influenced by criteria such as the following: (a) A significant decline in net assets of the FHLB as compared to the capital stock amount and the length of time this situation has persisted (b) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance (c) the impact of legislative and regulatory changes on the customer base of the FHLB and (d) the liquidity position of the FHLB. Management evaluated the stock and concluded that the stock was not impaired for the periods presented herein. Management considered that the FHLB's regulatory capital ratios are strong, liquidity appears adequate, new shares of FHLB stock continue to exchange hands at the $100 par value and the FHLB has repurchased shares of excess capital stock from its members and has paid a quarterly cash dividend.

9. DEPOSITS

The following table shows the breakdown of deposits as of December 31, 2021 and 2020, by deposit type (in thousands):

		2021		2020
Non-interest-bearing deposits	**$**	**358,073**	$	303,762
NOW accounts		**485,292**		422,083
Savings deposits		**313,048**		255,853
Money market deposit accounts		**350,122**		225,968
Certificates of deposit		**329,616**		381,192
Total	**$**	**1,836,151**	$	1,588,858

Certificates of deposit of $250,000 or more amounted to $79,610,000 and $75,869,000 at December 31, 2021 and 2020, respectively. Brokered deposits totaled $23,839,000 as of December 31, 2020. There were no brokered certificates of deposits as of December 31, 2021.

Following are maturities of certificates of deposit as of December 31, 2021 (in thousands):

2022	$	184,857
2023		68,192
2024		42,549
2025		16,257
2026		11,994
Thereafter		5,767
Total certificates of deposit	$	329,616

10. BORROWED FUNDS AND REPURCHASE AGREEMENTS

The following table shows the breakdown of borrowed funds as of December 31, 2021 and 2020 (dollars in thousands):

	Securities Sold Under Agreements to Repurchase(a)	FHLB Advances (b)	Federal Funds Lines (c)	FRB BIC Line (d)	Subordinated Debt (e)	Notes Payable (f)	Term Loans(g)	Total Borrowed Funds
2021								
Balance at December 31	**$ 16,873**	**$ -**	**$ -**	**$ -**	**$ 9,879**	**$ 7,500**	**$ 39,725**	**$ 73,977**
Highest balance at any month-end	**16,873**	**-**	**-**	**-**	**9,879**	**7,500**	**66,525**	**100,777**
Average balance	**14,726**	**-**	**-**	**-**	**7,036**	**7,500**	**55,360**	**84,622**
Weighted average interest rate:								
Paid during the year	**0.06%**	**0.00%**	**0.51%**	**0.22%**	**4.17%**	**3.57%**	**1.26%**	**1.50%**
As of year-end	**0.08%**	**0.00%**	**0.00%**	**0.00%**	**4.18%**	**3.57%**	**1.15%**	**1.56%**
2020								
Balance at December 31	$ 14,813	$ -	$ -	$ -	$ -	$ 7,500	$ 66,525	$ 88,838
Highest balance at any month-end	14,813	67,106	-	-	-	7,500	79,022	168,441
Average balance	12,903	12,371	-	109	-	7,500	60,355	93,238
Weighted average interest rate:								
Paid during the year	0.36%	1.63%	0.51%	0.34%	0.00%	3.83%	1.19%	1.34%
As of year-end	0.11%	0.00%	0.00%	0.00%	0.00%	3.57%	1.12%	1.16%

(a) We utilize securities sold under agreements to repurchase to facilitate the needs of our customers and to facilitate secured short-term funding needs. Securities sold under agreements to repurchase are stated at the amount of cash received in connection with the transaction. We monitor collateral levels on a continuous basis. We may be required to provide additional collateral based on the fair value of the underlying securities. Securities pledged as collateral under repurchase agreements are maintained with our safekeeping agents. The collateral pledged on the repurchase agreements by the remaining contractual maturity of the repurchase agreements in the Consolidated Balance Sheets as of December 31, 2021 and December 31, 2020 is presented in the following tables (in thousands).

	Remaining Contractual Maturity of the Agreements				
2021	Overnight and Continuous	Up to 30 Days	30 - 90 Days	Greater than 90 days	Total
Repurchase Agreements:					
U.S. agency securities	**$ 17,155**	**$ -**	**$ -**	**$ -**	**$ 17,155**
Total carrying value of collateral pledged	**$ 17,155**	**$ -**	**$ -**	**$ -**	**$ 17,155**
Total liability recognized for repurchase agreements					**$ 16,873**

	Remaining Contractual Maturity of the Agreements				
2020	Overnight and Continuous	Up to 30 Days	30 - 90 Days	Greater than 90 days	Total
Repurchase Agreements:					
U.S. agency securities	$ 16,735	$ -	$ -	$ -	$ 16,735
Total carrying value of collateral pledged	$ 16,735	$ -	$ -	$ -	$ 16,735
Total liability recognized for repurchase agreements					$ 14,813

(b) FHLB Advances consist of an "Open RepoPlus" agreement with the FHLB of Pittsburgh. FHLB "Open RepoPlus" advances are short-term borrowings that bear interest based on the FHLB discount rate or Federal Funds rate, whichever is higher. The Company has a borrowing limit of $756,225,000, inclusive of any outstanding advances and letters of credit. FHLB advances are secured by a blanket security agreement that includes the Company's FHLB stock, as well as certain investment and mortgage-backed securities held in safekeeping at the FHLB and certain residential and commercial mortgage loans. A portion of these advances, $25.0 million, are subject to interest rate swap arrangements. See Note 17 for additional information.

(c) The federal funds lines consist of unsecured lines from two third party banks at market rates. The Company has a borrowing limit totaling $34,000,000, inclusive of any outstanding balances. No specific collateral is required to be pledged for these borrowings.

(d) The Federal Reserve Bank Borrower in Custody (FRB BIC) Line consists of a borrower in custody in agreement opened in January 2010 with the Federal Reserve Bank of Philadelphia secured by municipal loans maintained in the Company's possession. As of December 31, 2021 and 2020, the Company has a borrowing limit of $1,068,000 and $4,379,000, respectively, inclusive of any outstanding advances. The approximate carrying value of the municipal loan collateral was $1,683,000 and $12,932,000 as of December 31, 2021 and 2020, respectively.

(e) In April 2021, the Company issued $10.0 million of fixed to floating rate subordinated notes that mature on April 16, 2031, unless redeemed earlier. The notes bear interest at 4% per annum through April 16, 2026 and subsequently pay interest at the 90-day average secured overnight financing rate, determined on the determination date of the applicable interest period, plus 323 basis points. The Company may redeem the notes, in whole or in part, on or after April 16, 2026, and at any time upon the occurrence of certain events, subject in each case to the approval of the Board of Governors of the Federal Reserve System (the "Federal Reserve"). Issuance costs associated with the notes totaled $131,000 and were capitalized and will be amortized over the life of the note on a straight-line basis, which approximates the effective yield method. As of December 31, 2021, the net unamortized issuance costs totaled $121,000.

(f) In December 2003, the Company formed a special purpose entity ("Entity") to issue $7,500,000 of floating rate obligated mandatory redeemable trust preferred securities as part of a pooled offering. The rate was determined quarterly and floated based on the 3 month LIBOR plus 2.80 percent. The Entity may redeem them, in whole or in part, at face value after December 17, 2008, and on a quarterly basis thereafter. The Company borrowed the proceeds of the issuance from the Entity in December 2003 in the form of a $7,500,000 note payable. Debt issue costs of $75,000 have been capitalized and fully amortized as of December 31, 2008. Under current accounting rules, the Company's minority interest in the Entity was recorded at the initial investment amount and is included in the other assets section of the balance sheet. The Entity is not consolidated as part of the Company's consolidated financial statements. The $7,500,000 note payable is subject to an interest rate swap arrangement. See Note 17 for additional information.

(g) Term Loans consist of separate loans with the FHLB of Pittsburgh as follows (dollars in thousands):

Interest Rate	Maturity	**December 31, 2021**	December 31, 2020
Fixed:			
0.38%	January 4, 2021	**-**	25,000
0.26%	January 3, 2022	**25,000**	-
2.08%	January 6, 2022	**4,725**	4,725
2.46%	March 28, 2024	**5,000**	5,000
1.69%	August 20, 2024	**5,000**	5,000
2.61%	February 3, 2021	**-**	2,000
3.52%	July 12, 2021	**-**	2,000
2.37%	August 20, 2021	**-**	2,800
0.25%	July 9, 2021	**-**	15,000
1.24%	March 3, 2025	**-**	5,000
Total term loans		**$ 39,725**	$ 66,525

Following are maturities of borrowed funds as of December 31, 2021 (in thousands):

2022	$ 46,598
2023	-
2024	10,000
2025	-
2026	-
Thereafter	17,379
Total borrowed funds	$ 73,977

11. EMPLOYEE BENEFIT PLANS

<u>Noncontributory Defined Benefit Pension Plan</u>

The Bank sponsors a trusteed, noncontributory defined benefit pension plan covering substantially all employees and officers hired prior to January 1, 2007. The Bank also assumed the noncontributory defined benefit pension plan of FNB when it was acquired during 2015. The FNB plan was frozen prior to the acquisition and therefore, no additional benefits will accrue for employees covered under that plan. The Board of Directors in 2018 voted to terminate the plan acquired as part of the FNB acquisition with final settlement occurring in the fourth quarter of 2019. These two plans are collectively referred to herein as "the Plans". The pension plans call for benefits to be paid to eligible employees at retirement based primarily upon years of service with the Bank and compensation rates during employment. Upon retirement or other termination of employment, employees can elect either an annuity benefit or a lump sum distribution of vested benefits in the pension plan. The Bank's funding policy is to make annual contributions, if needed, based upon the funding formula developed by the pension plans' actuary. The Bank did not make any contributions to the pension plans in 2021, 2020 or 2019.

In lieu of the pension plan, employees with a hire date of January 1, 2007 or later are eligible to receive, after meeting length of service requirements, an annual discretionary 401(k) plan contribution from the Bank equal to a percentage of an employee's base compensation. The contribution amount is placed in a separate account within the 401(k) plan and is subject to a vesting requirement. Contributions by the Company totaled $290,000, $212,0000 and $200,000 for 2021, 2020 and 2019, respectively.

The following table sets forth the obligation and funded status of the Plans as of December 31 (in thousands):

		2021		2020
Change in benefit obligation				
Benefit obligation at beginning of year	**$**	**14,020**	$	13,027
Service cost		**380**		330
Interest cost		**270**		332
Actuarial (Gain) / Loss		**(438)**		1,810
Settlement gain		**(17)**		(34)
Benefits paid		**(1,092)**		(1,445)
Benefit obligation at end of year		**13,123**		14,020
Change in plan assets				
Fair value of plan assets at beginning of year		**13,247**		13,277
Actual return (loss) on plan assets		**1,761**		1,415
Employer contribution		**-**		-
Benefits paid		**(1,092)**		(1,445)
Fair value of plan assets at end of year		**13,916**		13,247
Funded status	**$**	**793**	$	(773)

Amounts not yet recognized as a component of net periodic pension cost as of December 31 (in thousands):

Amounts recognized in accumulated other comprehensive loss consists of:		**2021**		2020
Net loss	**$**	**2,491**	$	4,383
Prior service cost		**-**		-
Total	**$**	**2,491**	$	4,383

The accumulated benefit obligation for the defined benefit pension plan was $13,123,000 and $14,020,000 at December 31, 2021 and 2020 respectively.

The components of net periodic benefit costs for the years ended December 31 are as follows (in thousands):

		2021		2020		2019	Affected line item on the Consolidated Statement of Income
Service cost	**$**	**380**	$	330	$	289	Salary and Employee Benefits
Interest cost		**270**		332		588	Other Expenses
Return on plan assets		**(895)**		(862)		(924)	Other Expenses
Settlement loss (gain)		**235**		302		(259)	Other Expenses
Net amortization and deferral		**336**		233		272	Other Expenses
Net periodic benefit cost	**$**	**326**	$	335	$	(34)	

The estimated net loss that will be amortized from accumulated other comprehensive loss into the net periodic benefit cost (income) in 2022 is $142,000.

The weighted-average assumptions used to determine benefit obligations at December 31, 2021 and 2020 is summarized in the following table. The change in the discount rate is the primary driver of the actuarial gain that occurred in 2021 of $438,000.

	2021	2020
Discount rate FCCB Plan	**2.25%**	2.00%
Rate of compensation increase	**3.00%**	3.00%

The weighted-average assumptions used to determine net periodic benefit cost (income) for the year ended December 31. Due to the decision to terminate the pension plan acquired as part of the FNB acquisition, the discount rate for the plans will be separated for 2019.

	2021	2020	2019
Discount rate FCCB Plan	**2.00%**	2.75%	4.00%
Discount rate FNB Plan	**NA**	NA	3.49%
Expected long-term return on plan assets FCCB plan	**7.00%**	7.00%	7.00%
Rate of compensation increase	**3.00%**	3.00%	3.00%

The long-term rate of return on plan assets gives consideration to returns currently being earned on plan assets as well as future rates expected to be earned. The investment objective is to maximize total return consistent with the interests of the participants and beneficiaries, and prudent investment management. The allocation of the pension plan assets is determined on the basis of sound economic principles and is continually reviewed in light of changes in market conditions. Asset allocation favors equity securities, with a target allocation of 50-70%. The target allocation for debt securities is 30-50%. At December 31, 2021, the pension plan had a sufficient cash and money market position in order to re-allocate the equity portfolio for diversification purposes and reduce risk in the total portfolio. The following table sets forth by level, within the fair value hierarchy as defined in footnote 19, the Plan's assets at fair value as of December 31, 2021 and 2020 (dollars in thousands):

2021	**Level I**	**Level II**	**Level III**	**Total**	**Allocation**
Assets					
Cash and cash equivalents	**$ 188**	**$ -**	**$ -**	**$ 188**	**1.4%**
Equity Securities	**6,291**	**-**	**-**	**6,291**	**45.2%**
Mutual Funds and ETF's	**5,246**	**-**	**-**	**5,246**	**37.7%**
Corporate Bonds	**-**	**2,191**	**-**	**2,191**	**15.7%**
Total	**$ 11,725**	**$ 2,191**	**$ -**	**$ 13,916**	**100.0%**

2020	Level I	Level II	Level III	Total	Allocation
Assets					
Cash and cash equivalents	$ 456	$ -	$ -	$ 456	3.4%
Equity Securities	5,709	-	-	5,709	43.1%
Mutual Funds and ETF's	4,410	-	-	4,410	33.3%
Corporate Bonds	-	2,672	-	2,672	20.2%
Total	$ 10,575	$ 2,672	$ -	$ 13,247	100.0%

Equity securities include the Company's common stock in the amounts of $686,000 (4.9% of total plan assets) and $627,000 (4.7% of total plan assets) at December 31, 2021 and 2020, respectively.

The Bank does not expect to make a contribution to its pension plan in 2022. Expected future benefit payments that the Bank estimates from its pension plan are as follows (in thousands):

2022	$ 420
2023	634
2024	806
2025	1,161
2026	2,130
2027 - 2031	3,944

Defined Contribution Plan

The Company sponsors a voluntary 401(k) savings plan which eligible employees can elect to contribute up to the maximum amount allowable not to exceed the limits of IRS Code Sections 401(k). Under the plan, the Company also makes required contributions on behalf of the eligible employees. The Company's contributions vest immediately. Contributions by the Company totaled $563,000, $518,000 and $446,000 for 2021, 2020 and 2019, respectively.

Directors' Deferred Compensation Plan

The Company's directors may elect to defer all or portions of their fees until their retirement or termination from service. Amounts deferred under the deferred compensation plan earn interest based upon the highest current rate offered to certificate of deposit customers. Amounts deferred under the deferred compensation plan are not guaranteed and represent a general liability of the Company. As of December 31, 2021 and 2020, an obligation of $587,000 and $632,000, respectively, was included in other liabilities for this plan in the Consolidated Balance Sheet. Amounts included in interest expense on the deferred amounts totaled $6,000, $8,000 and $19,000 for the years ended December 31, 2021, 2020 and 2019, respectively.

Restricted Stock Plan

The Company maintains a Restricted Stock Plan (the Plan) whereby employees and non-employee corporate directors are eligible to receive awards of restricted stock based upon performance related requirements. Awards granted under the Plan are in the form of the Company's common stock and maybe subject to certain vesting requirements including in the case of employees, continuous employment or service with the Company. In April 2016, the Company's stockholder authorized a total of 150,000 shares of the Company's common stock to be made available under the Plan. As of December 31, 2021, 119,391 shares remain available to be issued under the Plan. The Plan assists the Company in attracting, retaining and motivating employees to make substantial contributions to the success of the Company and to increase the emphasis on the use of equity as a key component of compensation. The following table details the vesting, awarding and forfeiting of unearned restricted shares during 2021:

	2021	
	Shares	**Weighted Average Market Price**
Outstanding, beginning of year	**10,202**	**$ 55.93**
Granted	**4,660**	**60.73**
Forfeited	**(70)**	**55.03**
Vested	**(7,838)**	**56.51**
Outstanding, end of year	**6,954**	**$ 58.51**

Compensation cost related to restricted stock is recognized based on the market price of the stock at the grant date over the vesting period. Compensation expense related to restricted stock was $318,000, $333,000 and $299,000 for the years ended December 31, 2021, 2020 and 2019, respectively. The per share weighted-average grant-date fair value of restricted shares granted during 2021, 2020 and 2019 was $60.73, $50.89 and $60.02, respectively. At December 31, 2021, the total compensation cost related to nonvested awards that has not yet been recognized was $407,000, which is expected to be recognized over the next 3 years.

Supplemental Executive Retirement Plan

The Company maintains a non-qualified supplemental executive retirement plan ("SERP") for certain executives to compensate those executive participants in the Company's noncontributory defined benefit pension plan whose benefits are limited by compensation limitations under current tax law. At December 31, 2021 and 2020, an obligation of $2,509,000 and $2,077,000, respectively, for the SERP was included in other liabilities in the Consolidated Balance Sheet. Expenses related to the SERP totaled $473,000, $107,000 and $251,000 for the years ended December 31, 2021, 2020 and 2019, respectively. Benefit payments for 2021 and 2020 were $42,000 and $32,000, respectively. There were no benefit payments in 2019.

Deferred Compensation Plan

The Company in 2018 initiated a non-qualified executive deferred compensation plan for eligible employees designated by the Board of Directors. At December 31, 2021 and 2020, an obligation of $940,000 and $631,000, respectively, was included in other liabilities for the deferred compensation plan in the Consolidated Balance Sheet. Expenses related to the deferred compensation plan totaled $309,000, $230,000 and $343,000 for the years ended December 31, 2021, 2020 and 2019, respectively. There were no benefit payments in 2021, 2020 or 2019.

Salary Continuation Plan

The Company maintains a salary continuation plan for certain employees acquired through the acquisition of the FNB. At December 31, 2021 and 2020 an obligation of $646,000 and $673,000, respectively, was included in other liabilities for this plan in the Consolidated Balance Sheet. Expenses related to the salary continuation plan totaled $49,000, $51,000 and $52,000 for the years ended December 31, 2021, 2020 and 2019, respectively.

Continuation of Life Insurance Plan

The Company, as part of the acquisition of FNB, has promised a continuation of life insurance coverage to certain persons post-retirement. GAAP requires the recording of post-retirement costs and a liability equal to the present value of the cost of post-retirement insurance during the person's term of service. The estimated present value of future benefits to be paid totaled $696,000 and $687,000 at December 31, 2021 and 2020, respectively, which is included in other liabilities in the Consolidated Balance Sheet. Expenses for the plan totaled $9,000, $2,600 and $36,000 for the years ended December 31, 2021, 2020 and 2019, respectively.

12. INCOME TAXES

The provision for income taxes consists of the following (in thousands):

	Year Ended December 31,		
	2021	2020	2019
Currently payable	**$ 5,510**	$ 4,896	$ 3,503
Deferred tax liability (asset)	**689**	367	317
Provision for income taxes	**$ 6,199**	$ 5,263	$ 3,820

The following temporary differences gave rise to the net deferred tax asset and liabilities at December 31, 2021 and 2020, respectively (in thousands):

Deferred tax assets:	**2021**	2020
Allowance for loan losses	**$ 4,712**	$ 5,135
Deferred compensation	**491**	520
Merger & acquisition costs	**1**	2
Allowance for losses on available-for-sale securities	**4**	15
Pension and other retirement obligation	**360**	599
Unrealized loss on interest rate swap	**-**	2
Interest on non-accrual loans	**795**	778
Incentive plan accruals	**536**	489
Other real estate owned	**16**	16
Low income housing tax credits	**137**	131
NOL carry forward	**1,226**	1,321
Right of use asset	**686**	482
Accrued vacation	**168**	187
Other	**159**	224
Total	**$ 9,291**	$ 9,901

Deferred tax liabilities:	2021	2020
Premises and equipment	**$ (559)**	$ (612)
Investment securities accretion	**(90)**	(68)
Loan fees and costs	**(644)**	(333)
Goodwill and core deposit intangibles	**(2,309)**	(2,293)
Mortgage servicing rights	**(246)**	(215)
Unrealized gains on available-for-sale securities	**(81)**	(1,612)
Unrealized gains on equity securities	**(61)**	-
Unrealized gains on interest rate swap	**(401)**	-
Right of use asset	**(685)**	(480)
Other	**(133)**	(245)
Total	**(5,209)**	(5,858)
Deferred tax (liability) asset, net	**$ 4,082**	$ 4,043

No valuation allowance was established at December 31, 2021 and 2020, due to the Company's ability to carryback to taxes paid in previous years and certain tax strategies, coupled with the anticipated future taxable income as evidenced by the Company's earnings potential.

The total provision for income taxes is different from that computed at the statutory rates due to the following items (dollars in thousands):

	Year Ended December 31,		
	2021	2020	2019
Provision at statutory rates on pre-tax income	**$ 7,413**	$ 6,377	$ 4,895
Effect of tax-exempt income	**(764)**	(936)	(920)
Low income housing tax credits	**(141)**	(141)	(141)
Bank owned life insurance	**(384)**	(146)	(131)
Nondeductible interest	**44**	44	52
Nondeductible merger and acquisition expenses	**-**	32	38
Other items	**31**	33	27
Provision for income taxes	**$ 6,199**	$ 5,263	$ 3,820
Statutory tax rates	**21%**	21%	21%
Effective tax rates	**17.6%**	17.3%	16.4%

The Company prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Benefits from tax positions should be recognized in the financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority that would have full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be derecognized in the first subsequent financial reporting period in which that threshold is no longer met. There is currently no liability for uncertain tax positions and no known unrecognized tax benefits. With limited exception, the Company's federal and state income tax returns for taxable years through 2017 have been closed for purposes of examination by the federal and state taxing authorities.

Investments in Qualified Affordable Housing Projects

As of December 31, 2021 and 2020, the Company was invested in five and four partnerships, respectively, that provide affordable housing. The balance of the investments, which is included within other assets in the Consolidated Balance Sheet, was $288,000 and $216,000 as of December 31, 2021 and 2020, respectively. Investments purchased prior to January 1, 2015, are accounted for utilizing the effective yield method. As of December 31, 2021, the Company has $141,000 of tax credits remaining that will be recognized over one year for partnerships entered into prior to January 1, 2021. During 2021, the Company entered into an additional partnership that is expected to generate tax credits of $2,951,000 that will be utilized over the next twelve years. Tax credits of $141,000 were recognized as a reduction of tax expense during 2021, 2020 and 2019. Included within other expenses on the Consolidated Statement of Income was $108,000 of amortization of the investments in qualified affordable housing projects for 2021, 2020 and 2019, respectively.

13. ACCUMULATED OTHER COMPREHENSIVE (LOSS) INCOME

The components of accumulated other comprehensive income (loss), net of tax, as of December 31, were as follows (in thousands):

	2021	2020
Net unrealized gain on securities available for sale	**$ 385**	$ 7,668
Tax effect	**(81)**	(1,610)
Net -of-tax amount	**304**	6,058
Unrealized gain (loss) on interest rate swap	**1,910**	(11)
Tax effect	**(401)**	2
Net -of-tax amount	**1,509**	(9)
Unrecognized pension costs	**(2,491)**	(4,383)
Tax effect	**523**	921
Net -of-tax amount	**(1,968)**	(3,462)
Total accumulated other comprehensive (loss) income	**$ (155)**	$ 2,587

The following tables present the changes in accumulated other comprehensive income (loss) by component net of tax for the years ended December 31, 2021, 2020 and 2019 (in thousands):

	Unrealized gain (loss) on available for sale securities (a)	Unrealized gain (loss) on interest rate swap (a)	Defined Benefit Pension Items (a)	Total
Balance as of December 31, 2018	$ (973)	$ -	$ (2,948)	$ (3,921)
Other comprehensive income (loss) before reclassifications (net of tax)	3,283	-	(186)	3,097
Amounts reclassified from accumulated other comprehensive income (loss) (net of tax)	(20)	-	215	195
Net current period other comprehensive income (loss)	3,263	-	29	3,292
Balance as of December 31, 2019	$ 2,290	$ -	$ (2,919)	$ (629)
Balance as of December 31, 2019	$ 2,290	$ -	$ (2,919)	$ (629)
Other comprehensive income (loss) before reclassifications (net of tax)	4,008	4	(727)	3,285
Amounts reclassified from accumulated other comprehensive income (loss) (net of tax)	(240)	(13	184	(69)
Net current period other comprehensive income (loss)	3,768	(9)	(543)	3,216
Balance as of December 31, 2020	$ 6,058	$ (9)	$ (3,462)	$ 2,587
Balance as of December 31, 2020	**$ 6,058**	**$ (9)**	**$ (3,462)**	**$ 2,587**
Other comprehensive income (loss) before reclassifications (net of tax)	**(5,586)**	**1,371**	**1,229**	**(2,986)**
Amounts reclassified from accumulated other comprehensive income (loss) (net of tax)	**(168)**	**147**	**265**	**244**
Net current period other comprehensive income (loss)	**(5,754)**	**1,518**	**1,494**	**(2,742)**
Balance as of December 31, 2021	**$ 304**	**$ 1,509**	**$ (1,968)**	**$ (155)**

(a) Amounts in parentheses indicate debits

The following table presents the significant amounts reclassified out of each component of accumulated other comprehensive loss for the years ended December 31, 2021, 2020 and 2019 (in thousands):

Details about accumulated other comprehensive income (loss)	Amount reclassified from accumulated comprehensive income (loss) (a)			Affected line item in the Consolidated Statement of Income
	December 31,			
	2021	2020	2019	
Unrealized gains and losses on available for sale securities				
	$ 212	$ 305	$ 24	Available for sale securities gains, net
	(44)	(65)	(4)	Provision for income taxes
	$ 168	$ 240	$ 20	Net of tax
Unrealized gain (loss) on interest rate swap	**$ (147)**	$ 18	$ -	Interest expense
	32	(5)	-	Provision for income taxes
	$ (115)	$ 13	$ -	Net of tax
Defined benefit pension items				
	$ (336)	$ (233)	$ (272)	Other expenses
	71	49	57	Provision for income taxes
	$ (265)	$ (184)	$ (215)	Net of tax
Total reclassifications	**$ (97)**	$ 56	$ (195)	

(a) Amounts in parentheses indicate debits

14. RELATED PARTY TRANSACTIONS

Certain executive officers and directors of the Company, or companies in which they have 10 percent or more beneficial ownership, were indebted to the Bank. A summary of loan activity for the years ended December 31, 2021 and 2020 with officers, directors, stockholders and associates of such persons is listed below (in thousands):

	Year Ended December 31,	
	2021	2020
Balance, beginning of year	**$ 12,970**	$ 13,457
New loans	**5,341**	5,098
Repayments	**(6,631)**	(5,585)
Balance, end of year	**$ 11,680**	$ 12,970

15. REGULATORY MATTERS

Dividend Restrictions:

The approval of the Federal Reserve Board (FRB) is required for the Bank to pay dividends to the Company if the total of all dividends declared in any calendar year exceeds the Bank's net income (as defined) for that year combined with its retained net income for the preceding two calendar years. Under this formula, the Bank can declare dividends in 2022 without approval of the FRB or Pennsylvania Department of Banking of approximately $30,429,000, plus the Bank's 2022 year-to-date net income at the time of the dividend declaration.

Loans:

The Bank is subject to regulatory restrictions which limit its ability to loan funds to the Company. At December 31, 2021, the Bank's regulatory lending limit amounted to approximately $29,855,000.

Regulatory Capital Requirements:

Federal regulations require the Bank to maintain minimum amounts of capital. Specifically, the Bank is required to maintain certain minimum dollar amounts and ratios of Total, Tier I and Common Equity Tier I capital to risk-weighted assets and of Tier I capital to average total assets.

In addition to the capital requirements, the Federal Deposit Insurance Corporation Improvement Act (FDICIA) established five capital categories ranging from "well capitalized" to "critically under-capitalized." Should any institution fail to meet the requirements to be considered "adequately capitalized", it would become subject to a series of increasingly restrictive regulatory actions.

As permitted by applicable federal regulation, the Bank has opted to use the community bank leverage ratio (the "CBLR") framework for determining its capital adequacy. Under the CBLR framework a qualifying community bank is considered well-capitalized if its leverage ratio (Tier 1 capital divided by average total consolidated assets) exceeds 9%. Following the passage of the Coronavirus Aid, Relief, and Economic Security ("CARES") Act in response to the COVID-19 pandemic, the federal banking regulators revised the CBLR framework as follows: (i) beginning in the second quarter of 2020, a qualifying community bank need only have a leverage ratio of at least 8%, subject to the other qualifying requirements, and (ii) if a qualifying community bank's leverage ratio falls below 8%, then it will have two calendar quarters to maintain a leverage ratio of 7% or greater. These revisions under the CARES Act are effective April 23, 2020 and will terminate upon the earlier of the termination of the national emergency related to COVID-19 or December 31, 2020. Following such termination there is a grace period for returning to the 9% CBLR threshold. The CBLR will be set at 8% for the remainder of 2020, 8.5% for 2021, and 9% thereafter. The grace period is also adjusted to account for the graduating increase. As a result, in 2020 and 2021, a qualifying community bank utilizing the grace period must maintain a CBLR of at least 7% and 7.5%, respectively. Thereafter, a qualifying community bank utilizing the grace period must maintain a CBLR of at least 8%. If a qualifying community bank fails to maintain the applicable minimum CBLR during the grace period, or if it is unable to restore compliance with the CBLR within the grace period, then it will revert to the Basel III capital framework and the normal Prompt Corrective Action capital categories will apply. At December 31, 2021 and 2020, the Bank was considered "well-capitalized" under the CBLR framework, with a leverage ratio of 8.94% and 8.75%, respectively.

16. COMMITMENTS, CONTINGENT LIABILITIES, RISKS AND UNCERTAINTIES

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

Credit Extension Commitments

The Company's exposure to credit loss from nonperformance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual amount of these instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. Financial instruments, whose contract amounts represent credit risk at December 31, 2021 and 2020, are as follows (in thousands):

	2021	2020
Commitments to extend credit	**$275,998**	$274,327
Standby letters of credit	**17,083**	21,978
	$293,081	$296,305

Commitments to extend credit are legally binding agreements to lend to customers. Commitments generally have fixed expiration dates or other termination clauses and may require payment of fees. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future liquidity requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Company on extension of credit is based on management's credit assessment of the counter party.

Standby letters of credit are conditional commitments issued by the Company to guarantee a financial agreement between a customer and a third party. Performance letters of credit represent conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. These instruments are issued primarily to support bid or performance related contracts. The coverage period for these instruments is typically a one-year period with an annual renewal option subject to prior approval by management. Fees earned from the issuance of these letters are recognized during the coverage period. For secured letters of credit, the collateral is typically Bank deposit instruments or customer business assets.

The Company also offers limited overdraft protection as a non-contractual courtesy which is available to demand deposit accounts in good standing for business, personal or household use. The non-contractual amount of financial instruments with off-balance sheet risk at December 31, 2021 was $12,230,000. The Company reserves the right to discontinue this service without prior notice.

Legal and Regulatory Proceedings

In the ordinary course of business, the Company is subject to legal proceedings, including claims, litigation, investigations and administrative proceedings, all of which are considered incidental to the normal conduct of business. Litigation may relate to lending, deposit and other customer relationships, vendor and contractual issues, employee matters, intellectual property matters, personal injuries and torts, regulatory and legal compliance, and other matters. The Company believes it has substantial defenses to the claims asserted against it in its currently outstanding legal proceedings and, with respect to such legal proceedings, intends to defend itself vigorously.

The Company assesses its liabilities and contingencies in connection with outstanding legal proceedings utilizing the latest information available. Where it is probable that the Company will incur a loss and the amount of the loss can be reasonably estimated, the Company records a liability in its consolidated financial statements. These legal reserves may be increased or decreased to reflect any relevant developments. Where a loss is not probable or the amount of a probable loss is not reasonably estimable, the Company does not accrue legal reserves. Additionally, for those matters where a loss is reasonably possible and the amount of loss is reasonably estimable, the Company estimates the amount of losses that it could incur beyond the accrued legal reserves. Under U.S. GAAP, an event is “reasonably possible” if “the chance of the future event or events occurring is more than remote but less than likely” and an event is “remote" if “the chance of the future event or events occurring is slight.”

While the outcome of legal proceedings and the timing of the ultimate resolution are inherently difficult to predict, based on information currently available, advice of counsel and available insurance coverage, the Company believes that it has established adequate legal reserves. Further, based upon available information, the Company is of the opinion that these legal proceedings, individually or in the aggregate, will not have a material adverse effect on the Company’s financial condition or results of operations. However, in the event of unexpected future developments, it is reasonably possible that an adverse outcome in any of the matters discussed above could be material to the Company’s business, consolidated financial position, results of operations or cash flows for any particular reporting period of occurrence.

Paycheck Protection Program (PPP)

Since the opening of the PPP, several larger banks have been subject to litigation regarding the process and procedures that such banks used in processing applications for the PPP. The Company may be exposed to the risk of similar litigation, from both customers and non-customers that approached the bank regarding PPP loans, regarding the process and procedures used in processing applications for the PPP. If any such litigation is filed against and is not resolved in a manner favorable to the Company, it may result in significant financial liability or adversely affect reputation. In addition, litigation can be costly, regardless of outcome. Any financial liability, litigation costs or reputational damage caused by PPP-related litigation could have a material adverse impact on our business, financial condition and results of operations.

The Company also has credit risk on PPP loans if a determination is made by the SBA that there is a deficiency in the manner in which the loan was originated, funded, or serviced by, such as an issue with the eligibility of a borrower to receive a PPP loan, which may or may not be related to the ambiguity in the laws, rules and guidance regarding the operation of the PPP. In the event of a loss resulting from a default on a PPP loan and a determination by the SBA that there was a deficiency in the manner in which the PPP loan was originated, funded, or serviced by the Company , the SBA may deny its liability under the guaranty, reduce the amount of the guaranty, or, if it has already paid under the guaranty, seek recovery of any loss related to the deficiency from the Company.

17. DERIVATIVE FINANCIAL INSTRUMENTS

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. The Company manages economic risks, including interest rate, liquidity, and credit risk, primarily by managing the amount, sources, and duration of its assets and liabilities and through the use of derivative financial instruments. Specifically, the Company enters into derivative financial instruments to manage exposures that arise from business activities that result in the receipt or payment of future known and uncertain cash amounts, the value of which are determined by interest rates. The Company's derivative financial instruments are used to manage differences in the amount, timing, and duration of the Company's known or expected cash receipts and its known or expected cash payments principally related to certain variable rate borrowings.

Cash Flow Hedges of Interest Rate Risk

The Company's objectives in using interest rate derivatives are to add stability to interest income and expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company has entered into interest rate swaps as part of its interest rate risk management strategy. These interest rate swaps are designated as cash flow hedges and involve the receipt of variable rate amounts from a counterparty in exchange for the Company making fixed interest payments. As of December 31, 2021 and 2020, the Company had six interest rate swaps with a notional of $50.5 million associated with the Company's cash outflows associated with various floating-rate amounts.

For derivatives designated as cash flow hedges, the effective portion of changes in the fair value of the derivative is initially reported in other comprehensive income (outside of earnings), net of tax, and subsequently reclassified to earnings when the hedged transaction affects earnings, and the ineffective portion of changes in the fair value of the derivative is recognized directly in earnings. The Company assesses the effectiveness of each hedging relationship by comparing the changes in cash flows of the derivative hedging instrument with the changes in cash flows of the designated hedged transactions. The Company did not recognize any hedge ineffectiveness in earnings during the periods ended December 31, 2021 and 2020. Amounts reported in accumulated other comprehensive income related to derivatives will be reclassified to interest expense as interest payments are made on the Company's variable-rate liabilities. During the next twelve months, the Company estimates that $0 will be reclassified as an increase in interest expense.

Customer Swaps

The Company also enters into derivative contracts, which consist of interest rate swaps, to facilitate the needs of customers desiring to manage interest rate risk. These swaps are not designated as accounting hedges under ASC 815, Derivatives and Hedging. In order to economically hedge the interest rate risk associated with offering this product, the Company simultaneously enters into derivative contracts with third parties to offset the customer contracts, such that the Company minimizes its net risk exposure resulting from such transactions. The derivative contracts are structured such that the notional amounts decrease over time to generally match the expected amortization of the underlying loans. These derivatives are not speculative and arise from a service provided to customers. The Company utilizes a loan hedging program to accommodate clients preferring a fixed rate loan. The loan documents include an addendum with a zero premium collar. The zero premium collar is a cap and floor at the same interest rate, resulting in a fixed rate to the borrower. To hedge this embedded option, the Company enters into a dealer facing trade exactly mirroring the terms of the loan addendum. At December 31, 2021, the Company had interest rate swaps related to this program with an aggregate notional amount of $87.3 million.

Counterparty Credit Risk

As a result of its derivative contracts, the Company is exposed to credit risk. Specifically, approved counterparties and exposure limits are defined. On at least an annual basis, the customer derivative contracts and related counterparties are evaluated for credit risk with an adjustment made to the contracts fair value. In accordance with the interest rate agreements with derivative dealers, the Company may be required to post margin to these counterparties. At December 31, 2021, the Company has required collateral with certain of its derivative counterparties in the amount of $5.2 million and was not holding collateral of any derivative counterparties.

The following table reflects the estimated fair value positions of derivative contracts as of December 31, 2021:

Derivatives designated as hedging instruments under ASC 815 (in thousands):

Third party interest rate swaps	Balance Sheet Location	Notional Amount	Interest rate Paid	Interest rate Received	Fair Value December 31, 2021	Fair Value December 31, 2020
Maturing in 2025	other assets/(other liabilities)	$ 15,000	Fixed - 0.57%	3-Month Libor	$ 291	$ (143)
Maturing in 2027	other assets/(other liabilities)	10,000	Fixed - 0.65%	3-Month Libor	361	(50)
Maturing in 2027	other assets/(other liabilities)	7,500	Fixed - 3.57%	3-Month Libor + 280	239	(87)
Maturing in 2027	other assets/(other liabilities)	6,000	Fixed - 0.61%	3-Month Libor	244	24
Maturing in 2029	other assets/(other liabilities)	6,000	Fixed - 0.72%	3-Month Libor	329	74
Maturing in 2032	other assets/(other liabilities)	6,000	Fixed - 0.82%	3-Month Libor	446	171
		$ 50,500			$ 1,910	$ (11)

Derivatives not designated as hedging instruments under ASC 815 (in thousands):

Interest Rate Products	Balance Sheet Location	December 31, 2021 Notional Amount	December 31, 2021 Fair Value	December 31, 2020 Notional Amount	December 31, 2020 Fair Value
Zero Premium Collar	other assets/(other liabilities)	$ 67,375	$ (1,817)	$ 64,013	$ 1,111
Zero Premium Collar	other assets/(other liabilities)	$ 19,938	$ 284	$ -	$ -
Dealer Offset to Zero Premium Collar	other assets/(other liabilities)	$ 67,375	$ 1,817	$ 64,013	$ (1,111)
Dealer Offset to Zero Premium Collar	other assets/(other liabilities)	$ 19,938	$ (284)	$ -	$ -

The following table presents the effect of the Company's cash flow hedge accounting on Accumulated Other Comprehensive Income for the periods ended December 31, 2021 and 2020 (in thousands):

The Effect of Fair Value and Cash Flow Hedge Accounting on Accumulated Other Comprehensive Income

Derivatives in Hedging relationships	Amount of (Loss) Gain Recognized in OCI on Derivatives, Year Ended December 31, 2021	2020	Location of Gain Reclassified from Accumulated OCI into Income	Amount of (loss) gain reclassified from Accumulated OCI into income, Year Ended December 31, 2021	2020
Interest rate Products	$ 1,921	$ (11)	Interest Expense	$ (147)	$ 18

18. LEASES

A lease is defined as a contract, or part of a contract, that conveys the right to control the use of identified property, plant or equipment for a period of time in exchange for consideration. On January 1, 2019, the Company adopted ASU No. 2016-02 *"Leases" (Topic 842)* and all subsequent ASUs that modified Topic 842. For the Company, Topic 842 primarily affected the accounting treatment for operating lease agreements in which the Company is the lessee.

Lessee Accounting

Substantially all of the leases in which the Company is the lessee are comprised of real estate property for branches with terms extending through 2030. All of the Company's leases are classified as operating leases, and therefore, were previously not recognized on the Company's Consolidated Balance Sheet. With the adoption of Topic 842, operating lease agreements are required to be recognized on the consolidated statements of condition as right-of-use ("ROU") assets and corresponding lease liabilities.

The following table represents the Consolidated Balance Sheet classification of the Company's ROU assets and lease liabilities (in thousands). The Company elected not to include short-term leases (i.e., leases with initial terms of twelve months or less), on the Consolidated Balance Sheet.

Lease Type	Balance at December 31, 2021	2020	Affected line item on the Consolidated Balance Sheet
Right of Use Assets			
Operating	**$ 3,264**	$ 2,286	Other Assets
Lease Liabilities:			
Operating	**$ 3,266**	$ 2,295	Other Liabilities

The calculated amount of the ROU assets and lease liabilities in the table above are impacted by the length of the lease term and the discount rate used to present value the minimum lease payments. The Company's lease agreements often include one or more options to renew at the Company's discretion. If at lease inception, the Company considers the exercising of a renewal option to be reasonably certain, the Company will include the extended term in the calculation of the ROU asset and lease liability. Regarding the discount rate, Topic 842 requires the use of the rate implicit in the lease whenever this rate is readily determinable. As this rate is rarely determinable, the Company utilizes its incremental borrowing rate at lease inception, on a collateralized basis, over a similar term. For operating leases existing prior to January 1, 2019, the rate for the remaining lease term as of January 1, 2019 was used. The following table displays the weighted average remaining lease term and the weighted average discount rate for the Company's operating leases outstanding as of December 31, 2021:

	Operating
Weighted average term (years)	**6.16**
Weighted average discount rate	**1.84%**

The following table represents lease costs and other lease information for the years ended December 31, 2021, and 2020, respectively (in thousands). As the Company elected not to separate lease and non-lease components and instead to account for them as a single lease component, the variable lease cost primarily represents variable payments such as common area maintenance and utilities.

Lease Cost	December 31, 2021	2020	2019
Operating lease cost	**$ 676**	$ 571	$ 340
Variable lease cost	**63**	50	88
Total lease cost	**$ 739**	$ 621	$ 428

Future minimum payments for operating leases with initial or remaining terms of one year or more as of December 31, 2021 along with a reconciliation to the discounted amount recorded on the December 31, 2021 Consolidated Balance Sheet (in thousands):

Undiscounted cash flows due within	Operating
2022	**672**
2023	**604**
2024	**513**
2025	**447**
2026	**377**
2027 and thereafter	**851**
Total undiscounted cash flows	**3,464**
Impact of present value discount	**(198)**
Amount reported on balance sheet	**$ 3,266**

19. FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company established a hierarchal disclosure framework associated with the level of pricing observability utilized in measuring assets and liabilities at fair value. The three broad levels defined by this hierarchy are as follows:

Level I: Quoted prices are available in active markets for identical assets or liabilities as of the reported date.

Level II: Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these assets and liabilities include items for which quoted prices are available but traded less frequently, and items that are fair valued using other financial instruments, the parameters of which can be directly observed.

Level III: Assets and liabilities that have little to no pricing observability as of the reported date. These items do not have two-way markets and are measured using management's best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality, the Company's creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. Our valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Company's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. Transfers between levels of the fair value hierarchy are recognized on the actual date of the event or circumstances that caused the transfer, which generally coincides with the Company's monthly and/or quarterly valuation process.

Assets and Liabilities Required to be Measured at Fair Value on a Recurring Basis

The fair values of equity securities and securities available for sale are determined by quoted prices in active markets, when available, and classified as Level I. If quoted market prices are not available, the fair value is determined by a matrix pricing, which is a mathematical technique, widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities and classified as Level II. The fair values consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things.

The following tables present the assets reported on the consolidated balance sheet at their fair value on a recurring basis as of December 31, 2021 and 2020 (in thousands) by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

2021	Level I	Level II	Level III	Total
Fair value measurements on a recurring basis:				
Assets:				
Equity securities	$ 2,270	$ -	$ -	$ 2,270
Available for sale securities:				
U.S. Agency securities	-	73,945	-	73,945
U.S. Treasuries securities	115,347	-	-	115,347
Obligations of state and political subdivisions	-	112,021	-	112,021
Corporate obligations	-	10,333	-	10,333
Mortgage-backed securities in government sponsored entities	-	100,756	-	100,756
Other Assets:				
Derivative instruments	-	4,011	-	4,011
Liabilities:				
Derivative instruments	-	(2,101)	-	(2,101)

2020	Level I	Level II	Level III	Total
Fair value measurements on a recurring basis:				
Assets:				
Equity securities	$ 1,931	$ -	$ -	$ 1,931
Available for sale securities:				
U.S. Agency securities	-	81,416	-	81,416
U.S. Treasuries securities	28,043	-	-	28,043
Obligations of state and political subdivisions	-	102,972	-	102,972
Corporate obligations	-	6,509	-	6,509
Mortgage-backed securities in government sponsored entities	-	76,249	-	76,249
Other Assets:				
Derivative instruments	-	1,111	-	1,111
Liabilities:				
Derivative instruments	-	(1,122)	-	(1,122)

Financial Instruments, Non-Financial Assets and Non-Financial Liabilities Recorded at Fair Value on a Nonrecurring Basis

The Company may be required, from time to time, to measure certain financial assets, financial liabilities, non-financial assets and non-financial liabilities at fair value on a nonrecurring basis in accordance with U.S. generally accepted accounting principles. These include assets that are measured at the lower of cost or market value that were recognized at fair value below cost at the end of the period. Certain non-financial assets measured at fair value on a non-recurring basis include foreclosed assets (upon initial recognition or subsequent impairment), non-financial assets and non-financial liabilities measured at fair value in the second step of a goodwill impairment test, and intangible assets and other non-financial long-lived assets measured at fair value for impairment assessment. Non-financial assets measured at fair value on a non-recurring basis during 2021 and 2020 include certain foreclosed assets which, upon initial recognition, were remeasured and reported at fair value through a charge-off to the allowance for possible loan losses and certain foreclosed assets which, subsequent to their initial recognition, were remeasured at fair value through a write-down included in other non-interest expense.

Assets measured at fair value on a nonrecurring basis as of December 31, 2021 and 2020 (in thousands) are included in the table below:

2021	**Level I**	**Level II**	**Level III**	**Total**
Impaired Loans	**$ -**	**$ -**	**$ 459**	**$ 459**
Other real estate owned	**-**	**-**	**552**	**552**

2020	Level I	Level II	Level III	Total
Impaired Loans	$ -	$ -	$ 3,243	$ 3,243
Other real estate owned	-	-	1,700	1,700

- ***Impaired Loans -*** The Company has measured impairment on impaired loans generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent third-party appraisals of the properties. In some cases, management may adjust the appraised value due to the age of the appraisal, changes in market conditions, or observable deterioration of the property since the appraisal was completed. Additionally, management makes estimates about expected costs to sell the property which are also included in the net realizable value. If the fair value of the collateral dependent loan is less than the carrying amount of the loan a specific reserve for the loan is made in the allowance for loan losses or a charge-off is taken to reduce the loan to the fair value of the collateral (less estimated selling costs) and the loan is included in the table above as a Level III measurement. If the fair value of the collateral exceeds the carrying amount of the loan, then the loan is not included in the table above as it is not currently being carried at its fair value. The fair values above excluded estimated selling costs of $47,000 and $356,000 at December 31, 2021 and 2020, respectively.

- ***Other Real Estate Owned –*** OREO is carried at the lower of cost or fair value, less estimated costs to sell, which is measured at the date of foreclosure. If the fair value of the collateral exceeds the carrying amount of the loan, no charge-off or adjustment is necessary, the loan is not considered to be carried at fair value, and is therefore not included in the table above. If the fair value of the collateral is less than the carrying amount of the loan, management will charge the loan down to its estimated realizable value. The fair value of OREO is based on the appraised value of the property, which is generally unadjusted by management and is based on comparable sales for similar properties in the same geographic region as the subject property, and is included in the above table as a Level II measurement. In some cases, management may adjust the appraised value due to the age of the appraisal, changes in market conditions, or observable deterioration of the property since the appraisal was completed. In these cases, the loans are categorized in the above table as a Level III measurement since these adjustments are considered to be unobservable inputs. Income and expenses from operations and further declines in the fair value of the collateral subsequent to foreclosure are included in net expenses from OREO.

The following table provides a listing of the significant unobservable inputs used in the fair value measurement process for items valued utilizing level III techniques (dollars in thousands).

2021	Fair Value	Valuation Technique(s)	Unobservable input	Range	Weighted average
Impaired Loans	**459**	Appraised Collateral Values	Discount for time since appraisal	0-100%	23.38%
			Selling costs	8%-10%	8.27%
			Holding period	6 - 12 months	11.52 months
Other real estate owned	**552**	Appraised Collateral Values	Discount for time since appraisal	20-44%	41.76%

2020	Fair Value	Valuation Technique(s)	Unobservable input	Range	Weighted average
Impaired Loans	3,243	Appraised Collateral Values	Discount for time since appraisal	0-100%	20.61%
			Selling costs	5%-10%	9.51%
			Holding period	6 - 12 months	11.65 months
Other real estate owned	1,700	Appraised Collateral Values	Discount for time since appraisal	20-31%	28.67%

Financial Instruments Not Required to be Measured or Reported at Fair Value

The carrying amount and fair value of the Company's financial instruments that are not required to be measured or reported at fair value on a recurring basis are as follows (in thousands):

December 31, 2021	**Carrying Amount**	**Fair Value**	**Level I**	**Level II**	**Level III**
Financial assets:					
Interest bearing time deposits with other banks	**$ 11,026**	**$ 11,026**	**$ -**	**$ -**	**$ 11,026**
Loans held for sale	**4,554**	**4,554**	**-**	**-**	**4,554**
Net loans	**1,424,229**	**1,426,698**	**-**	**-**	**1,426,698**
Financial liabilities:					
Deposits	**1,836,151**	**1,836,179**	**1,506,535**	**-**	**329,644**
Borrowed funds	**73,977**	**72,346**	**-**	**-**	**72,346**

December 31, 2020	Carrying Amount	Fair Value	Level I	Level II	Level III
Financial assets:					
Interest bearing time deposits with other banks	$ 13,758	$ 13,758	$ -	$ -	$ 13,758
Loans held for sale	14,640	14,640	-	-	14,640
Net loans	1,389,466	1,404,166	-	-	1,404,166
Financial liabilities:					
Deposits	1,588,858	1,593,738	1,506,535	-	87,206
Borrowed funds	88,838	88,263	-	-	88,263

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the

Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions can significantly affect the estimates.

Estimated fair values have been determined by the Company using historical data, as generally provided in the Company's regulatory reports, and an estimation methodology suitable for each category of financial instruments. The carrying amounts for cash and cash equivalents, bank owned life insurance, regulatory stock, accrued interest receivable and payable approximate fair value and are considered Level I measurements.

20. CONDENSED FINANCIAL INFORMATION - PARENT COMPANY ONLY

The following is condensed financial information for Citizens Financial Services, Inc.:

CITIZENS FINANCIAL SERVICES, INC.
CONDENSED BALANCE SHEET

	December 31,	
(in thousands)	**2021**	2020
Assets:		
Cash	**$ 15,046**	$ 5,301
Investments	**2,150**	1,866
Investment in subsidiary:	**212,057**	194,312
Other assets	**1,297**	846
Total assets	**$ 230,550**	$ 202,325
Liabilities:		
Other liabilities	**$ 679**	$ 566
Borrowed funds	**17,379**	7,500
Total liabilities	**18,058**	8,066
Stockholders' equity	**212,492**	194,259
Total liabilities and stockholders' equity	**$ 230,550**	$ 202,325

CITIZENS FINANCIAL SERVICES, INC.
CONDENSED STATEMENT OF INCOME

	Year Ended December 31,		
(in thousands)	**2021**	2020	2019
Dividends from:			
Bank subsidiary	**$ 8,994**	$ 16,171	$ 9,565
Equity securities	**104**	45	17
Total income	**9,098**	16,216	9,582
Realized securities gains (losses)	**284**	(23)	101
Expenses	**1,008**	775	1,103
Income before equity in undistributed earnings of subsidiary	**8,374**	15,418	8,580
Equity in undistributed earnings - First Citizens Community Bank	**20,744**	9,685	10,910
Net income	**$ 29,118**	$ 25,103	$ 19,490
Comprehensive income	**$ 26,376**	$ 28,319	$ 22,782

CITIZENS FINANCIAL SERVICES, INC.
STATEMENT OF CASH FLOWS

(in thousands)	Year Ended December 31, 2021	2020	2019
Cash flows from operating activities:			
Net income	**$ 29,118**	$ 25,103	$ 19,490
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed earnings of subsidiaries	**(20,744)**	(9,685)	(10,910)
Investment securities (gains) losses, net	**(284)**	23	(101)
Other, net	**543**	14	717
Net cash provided by operating activities	**8,633**	15,455	9,196
Cash flows from investing activities:			
Purchases of equity securities	**-**	(1,339)	-
Proceeds from the sale of equity securities	**-**	168	-
Acquisition of Midcoast	**-**	(7,614)	-
Net cash used in investing activities	**-**	(8,785)	-
Cash flows from financing activities:			
Cash dividends paid	**(7,383)**	(6,539)	(6,315)
Issuance of subordinated debt	**9,869**	-	-
Purchase of treasury stock	**(1,374)**	(2,122)	(1,291)
Sale of treasury stock to employee stock purchase plan	**-**	126	-
Net cash provided by (used in) financing activities	**1,112**	(8,535)	(7,606)
Net decrease in cash	**9,745**	(1,865)	1,590
Cash at beginning of year	**5,301**	7,166	5,576
Cash at end of year	**$ 15,046**	$ 5,301	$ 7,166

21. CONSOLIDATED CONDENSED QUARTERLY DATA (UNAUDITED)

The following table presents summarized quarterly financial data for 2021 and 2020:

(in thousands, except share data) **2021**	Three Months Ended, Mar 31	June 30	Sep 30	Dec 31
Interest income	**$ 18,295**	**$ 18,075**	**$ 18,342**	**$ 18,505**
Interest expense	**1,854**	**1,863**	**1,752**	**1,636**
Net interest income	**16,441**	**16,212**	**16,590**	**16,869**
Provision for loan losses	**650**	**500**	**400**	**-**
Non-interest income	**3,998**	**2,677**	**2,618**	**2,461**
Investment securities gains, net	**237**	**29**	**234**	**51**
Non-interest expenses	**9,947**	**10,320**	**10,400**	**10,883**
Income before provision for income taxes	**10,079**	**8,098**	**8,642**	**8,498**
Provision for income taxes	**1,616**	**1,451**	**1,578**	**1,554**
Net income	**$ 8,463**	**$ 6,647**	**$ 7,064**	**$ 6,944**
Earnings Per Share Basic	**$ 2.14**	**$ 1.69**	**$ 1.79**	**$ 1.76**
Earnings Per Share Diluted	**$ 2.14**	**$ 1.69**	**$ 1.79**	**$ 1.76**

2020	Three Months Ended, Mar 31	June 30	Sep 30	Dec 31
Interest income	$ 15,339	$ 18,160	$ 18,386	$ 18,411
Interest expense	2,449	1,874	1,916	1,866
Net interest income	12,890	16,286	16,470	16,545
Provision for loan losses	400	550	550	900
Non-interest income	2,105	1,941	3,386	3,726
Investment securities gains, net	(254)	128	152	238
Non-interest expenses	8,921	11,413	9,692	10,821
Income before provision for income taxes	5,420	6,392	9,766	8,788
Provision for income taxes	889	1,054	1,759	1,561
Net income	$ 4,531	$ 5,338	$ 8,007	$ 7,227
Earnings Per Share Basic	$ 1.26	$ 1.37	$ 2.02	$ 1.83
Earnings Per Share Diluted	$ 1.26	$ 1.37	$ 2.02	$ 1.83

22. ACQUISITION OF MIDCOAST COMMUNITY BANCORP, INC.

In the third quarter of 2019, the Company announced the signing of a definitive merger agreement to acquire 100% of the outstanding equity interest of MidCoast Community Bancorp, Inc. (“MidCoast”) for $6.50 per share in cash and stock. MidCoast was a Pennsylvania Corporation that conducted its business primarily through, its wholly owned subsidiary MidCoast Community Bank, which operated from a main office in Wilmington, Delaware, and two branches in Wilmington, Delaware, and one branch in Dover, Delaware.

The transaction closed on April 17, 2020, with MidCoast Community Bank having been merged into First Citizens Community Bank, with First Citizens Community Bank as the surviving entity. The acquisition established the Company’s presence in the Wilmington and Dover, Delaware markets.

Under the terms of the merger agreement, the Company acquired all of the outstanding shares of MidCoast for a total purchase price of approximately $26,843,000. As a result of the acquisition, the Company issued 373,356 common shares and $7.6 million in cash to the former shareholders of MidCoast. The shares were issued with a value of $51.50 per share, which was based on the close price of the Company’s stock on April 17, 2020.

The acquired assets and assumed liabilities were measured at estimated fair values. Management made significant estimates and exercised significant judgment in accounting for the acquisition. Management measured loan fair values based on loan file reviews, appraised collateral values, expected cash flows, and historical loss factors of MidCoast. Real estate acquired through foreclosure was primarily valued based on appraised collateral values. The Company also recorded an identifiable intangible asset representing the core deposit base of MidCoast based on management’s evaluation of the cost of such deposits relative to alternative funding sources. Management used significant estimates including the average lives of depository accounts, future interest rate levels, and the cost of servicing various depository products.

The business combination resulted in the acquisition of loans with and without evidence of credit quality deterioration. MidCoast’s loans were deemed to have credit impairment at the acquisition date if the Company did not expect to receive all contractually required cash flows due to concerns about credit quality. Such loans were fair valued and the difference between contractually required payments at the acquisition date and cash flows expected to be collected was recorded as a non-accretable difference. At the acquisition date, the Company recorded $4,869,000 of purchased credit-impaired loans. The method of measuring carrying value of purchased loans differs from loans originated by the Company (originated loans), and as such, the Company identifies purchased loans and purchased loans with a credit quality discount and originated loans at amortized cost.

MidCoast’s loans without evidence of credit deterioration were fair valued by discounting both expected principal and interest cash flows using an observable discount rate for similar instruments that a market participant would consider in determining fair value. Additionally, consideration was given to management’s best estimates of default rates and pre-payment speeds.

The following table summarizes the purchase of MidCoast as of April 17, 2020:

(In Thousands, Except Per Share Data)		
Purchase Price Consideration in Common Stock		
Citizens Financial Services, Inc. shares issued	373,356	
Value assigned to Citizens Financial Services, Inc. common share	$ 51.50	
Purchase price assigned to MidCoast common shares exchanged for Citizens Financial Services, Inc.		$ 19,228
Purchase Price Consideration - Cash for Common Stock		
Purchase price assigned to MidCoast common shares exchanged for cash		7,615
Total Purchase Price		26,843
Net Assets Acquired:		
MidCoast Community Bancorp, Inc shareholders' equity	$ 24,330	
Adjustments to reflect assets acquired at fair value:		
Investments		
Loans		
Interest rate	1,424	
General credit	(4,375)	
Specific credit - non-amortizing	(2,135)	
Specific credit - amortizing	(966)	
Core deposit intangible	157	
Owned premises	(426)	
Other assets	65	
Deferred tax assets	2,217	
Adjustments to reflect liabilities acquired at fair value:		
Time deposits	(1,018)	
Borrowings	(497)	
Other liabilities	(13)	
		18,763
Goodwill resulting from merger		$ 8,080

The following condensed statement reflects the amounts recognized as of the acquisition date for each major class of asset acquired and liability assumed:

(In Thousands)		
Total purchase price		$ 26,843
Net assets acquired:		
Cash and cash equivalents	$ 8,637	
Loans	223,235	
Premises and equipment, net	1,787	
Accrued interest receivable	586	
Bank-owned life insurance	3,766	
Intangibles	157	
Deferred tax asset	3,402	
Other assets	2,878	
Time deposits	(123,841)	
Deposits other than time deposits	(84,985)	
Accrued interest payable	(164)	
Borrowings	(15,497)	
Other liabilities	(1,198)	
		18,763
Goodwill resulting from the MidCoast merger		$ 8,080

The Company recorded goodwill and other intangibles associated with the acquisition of MidCoast totaling $8,237,000. Goodwill is not amortized, but is periodically evaluated for impairment. The Company did not recognize any impairment from April 17, 2020 to December 31, 2021. None of the goodwill acquired is expected to be deductible for tax purposes.

Identifiable intangibles are amortized to their estimated residual values over the expected useful lives. Such lives are also periodically reassessed to determine if any amortization period adjustments are required. For the period from April 17, 2020 to December 31, 2021, no such adjustments were recorded. The identifiable intangible asset consists of core deposit intangibles which are being amortized on an accelerated basis over the useful life of such assets. The gross carrying amount of the core deposit intangible at December 31, 2021 and 2020 was $157,000, and accumulated amortization was $46,000 and 19,000 as of December 31, 2021 and 2020, respectively.

As of December 31, 2021, the current year and estimated future amortization expense for the core deposit intangibles was (in thousands):

	Core deposit intangibles	
Amortization for 2021	**$**	**27**
Estimate for year ending December 31,		
2022		24
2023		21
2024		18
2025		15
2026		12
Thereafter		21
Total	$	111

Amounts recognized separately from the acquisition include primarily legal fees, investment banking fees, system conversion costs, severance costs and contract termination costs. These costs were included in merger and acquisition expenses within non-interest expenses on the Consolidated Statement of Income and amounted to approximately $2,179,000 and $466,000 for 2020 and 2019, respectively.

Results of operations for MidCoast prior to the acquisition date are not included in the Consolidated Statement of Income for 2020.

The following table presents financial information regarding the former MidCoast operations included in our Consolidated Statement of Income from the date of acquisition through December 31, 2020 under the column “Actual from Acquisition Date through December 31, 2020”. In addition, the following table presents unaudited pro forma information as if the acquisition of MidCoast had occurred on January 1, 2019 under the “Pro Forma” columns. The table below has been prepared for comparative purposes only and is not necessarily indicative of the actual results that would have been attained had the acquisition occurred as of the beginning of the periods presented, nor is it indicative of future results. Furthermore, the unaudited proforma information does not reflect management’s estimate of any revenue-enhancing opportunities nor anticipated cost savings as a result of the integration and consolidation of the acquisition. Merger and acquisition integration costs and amortization of fair value adjustments are included in the numbers below.

(In Thousands, Except Per Share Data)	**Actual from Acquisition Date Through December 31, 2020**	**Pro Formas Twelve Months Ended December 31, 2020**	**2019**
Net interest income	$ 9,314	$ 63,860	$ 60,097
Non-interest income	1,024	11,743	8,685
Net income	4,909	23,274	22,251
Pro forma earnings per share:			
Basic		$ 5.94	$ 5.66
Diluted		$ 5.94	$ 5.66

MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. The Company's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a significant deficiency (as defined in Public Company Accounting Oversight Board Auditing Standard No. 5), or a combination of significant deficiencies, that results in there being more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis by management or employees in the normal course by management or employees in the normal course of performing their assigned functions.

Management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2021. Management's assessment did not identify any material weaknesses in the Company's internal control over financial reporting.

In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in the 2013 Internal Control-Integrated Framework. Because there were no material weaknesses discovered, management believes that, as of December 31, 2021, the Company's internal control over financial reporting was effective.

<u>/s/ Randall E. Black</u>
By: Randall E. Black
Chief Executive Officer and President
(Principal Executive Officer)
Date: March 10, 2022

<u>/s/ Stephen J. Guillaume</u>
By: Stephen J. Guillaume
Chief Financial Officer
(Principal Financial & Accounting Officer)
Date: March 10, 2022

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and the Board of Directors of
Citizens Financial Services, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Citizens Financial Services, Inc. and subsidiaries (the “Company”) as of December 31, 2021 and 2020; the related consolidated statements of income, comprehensive income, changes in stockholders’ equity, and cash flows for each of the three years in the period ended December 31, 2021; and the related notes to the consolidated financial statements (collectively, the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2021 and 2020, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2021, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

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

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements; and (2) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter, in any way, our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Allowance for Loan Losses (ALL)

Description of the Matter

The Company’s loan portfolio totaled $1.4 billion as of December 31, 2021, and the associated ALL was $17.3 million. As discussed in Notes 1 and 5 to the consolidated financial statements, determining the amount of the ALL requires significant judgment about the collectability of loans, which includes an assessment of quantitative factors such as historical loss experience within each risk category of loans and testing of certain commercial loans for impairment. Management applies additional qualitative adjustments to reflect the inherent losses that exist in the loan portfolio at the balance sheet date that are not reflected in the historical loss experience. Qualitative adjustments are made based upon changes in lending policies and practices, economic conditions, changes in the loan portfolio mix, trends in loan delinquencies and classified loans, collateral values, and concentrations of credit risk for the commercial loan portfolios.

We identified these qualitative adjustments within the ALL as critical audit matters because they involve a high degree of subjectivity. In turn, auditing management’s judgments regarding the qualitative factors applied in the ALL calculation involved a high degree of subjectivity.

How We Addressed the Matter in Our Audit

We gained an understanding of the Company’s process for establishing the ALL, including the qualitative adjustments made to the ALL. We evaluated the design and tested the operating effectiveness of controls over the Company’s ALL process, which included, among others, management’s review and approval controls designed to assess the need and level of qualitative adjustments to the ALL, as well as the reliability of the data utilized to support management’s assessment.

To test the qualitative adjustments, we evaluated the appropriateness of management’s methodology and assessed whether all relevant risks were reflected in the ALL.

Regarding the measurement of the qualitative adjustments, we evaluated the completeness, accuracy, and relevance of the data and inputs utilized in management’s estimate. For example, we compared the inputs and data to the Company’s historical loan performance data and third-party macroeconomic data, and considered the existence of new or contrary information. Furthermore, we analyzed the changes in the components of the qualitative reserves relative to changes in external market factors, the Company’s loan portfolio, various internal risk metrics, and asset quality trends.

We also utilized internal credit review specialists with knowledge to evaluate the appropriateness of management’s risk-rating processes, to ensure that the risk ratings applied to the commercial loan portfolio were reasonable.

We have served as the Company’s auditor since 1994.

/s/S.R. Snodgrass, P.C.

Cranberry Township, Pennsylvania

March 10, 2022

ITEM 9 – CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

ITEM 9A – CONTROLS AND PROCEDURES.

(a) Disclosure Controls and Procedures

The Company's management, including the Company's principal executive officer and principal financial officer, have evaluated the effectiveness of the Company's "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, (the "Exchange Act"). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the Securities and Exchange Commission (the "SEC") (1) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

(b) Internal Control Over Financial Reporting

Management's annual report on internal control over financial reporting is incorporated herein by reference to Item 8 - the Company's audited Consolidated Financial Statements in this Annual Report on Form 10-K

(c) Changes to Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the three months ended December 31, 2021 that have materially affected, or are reasonable likely to materially affect, the Company's internal control over financial reporting.

ITEM 9B – OTHER INFORMATION.

None.

ITEM 9C – DISCLOSURE REGARDING FOREIGN JURISDICTIONS THAT PREVENT INSPECIONTS.

Not applicable

PART III

ITEM 10 – DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Directors

For information relating to the directors of the Company, the section captioned *“Proposal 1. Election of Directors”* in the Company’s Proxy Statement for the 2022 Annual Meeting of Stockholders (the “2022 Proxy Statement”) is incorporated by reference.

Executive Officers

For information relating to officers of the Company, the section captioned *“Proposal 1. Election of Directors”* in the 2022 Proxy Statement is incorporated by reference.

Compliance with Section 16(a) of the Exchange Act

For information regarding compliance with Section 16(a) of the Exchange Act, the section captioned *“Other Information Relating to Directors and Executive Officers - Section 16(a) Beneficial Ownership Reporting Compliance”* in the Company’s 2022 Proxy Statement is incorporated by reference.

Disclosure of Code of Ethics

The Company has adopted a Code of Ethics that applies to directors, officers and employees of the Company and the Bank. A copy of the Code of Ethics is posted on the Company’s website at www.firstcitizensbank.com. The Company intends to satisfy the disclosure requirement of Form 8-K regarding an amendment to, or a waiver from, a provision of its Code of Ethics by posting such information on its website.

Corporate Governance

For information regarding the audit committee and its composition and the audit committee financial expert, the section captioned *“Corporate Governance – Committees of the Board of Directors”* in the Company’s 2022 Proxy Statement is incorporated by reference.

ITEM 11 – EXECUTIVE COMPENSATION

Executive Compensation

For information regarding executive and director compensation, the sections captioned *“Director Compensation”, “Executive Compensation”, “Compensation Discussion and Analysis”* and “*Compensation Committee Report”* in the Company’s 2022 Proxy Statement are incorporated by reference.

ITEM 12 – SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDERS MATTERS

(a) Security Ownership of Certain Beneficial Owners Information required by this item is incorporated herein by reference to the section captioned *“Stock Ownership”* in the Company’s 2022 Proxy Statement.

(b) Security Ownership of Management Information required by this item is incorporated herein by reference to the section captioned *“Stock Ownership”* in the Company’s 2022 Proxy Statement.

(c) Changes in Control
Management of the Company knows of no arrangements, including any pledge by any person or securities of the Company, the operation of which may at a subsequent date result in a change in control of the registrant.

(d) Equity Compensation Plan Information
The following table sets forth information as of December 31, 2021 about Company common stock that may be issued under the Company’s 2016 Restricted Stock Plan. The plan was approved by the Company’s stockholders.

Plan Category	Number of securities to be issued upon the exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in the first column)
Equity compensation plans approved by security holders	n/a	n/a	119,391
Equity compensation plans not approved by security holders	n/a	n/a	n/a
Total	n/a	n/a	119,391

ITEM 13 – CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Certain Relationships and Related Transactions

For information regarding certain relationships and related transactions, the section captioned *"Other Information Relating to Directors and Executive Officers - Transactions with Related Persons"* in the Company's 2022 Proxy Statement is incorporated by reference.

Director Independence

For information regarding director independence, the section captioned *"Corporate Governance – Director Independence"* in the Company's 2022 Proxy Statement is incorporated by reference.

ITEM 14 – PRINCIPAL ACCOUNTANT FEES AND SERVICES

For information regarding the principal accountant fees and expenses the section captioned "*Audit – Related Matters*" in the Company's 2022 Proxy Statement is incorporated by reference.

PART IV

ITEM 15 – EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

(a) The following documents are filed as a part of this report:

1. The following financial statements are incorporated by reference in Item 8:

   Report of Independent Registered Public Accounting Firm
   Consolidated Balance Sheet as of December 31, 2021 and 2020
   Consolidated Statement of Income for the Years Ended December 31, 2021, 2020 and 2019
   Consolidated Statement of Comprehensive Income for the Years Ended December 31, 2021, 2020 and 2019
   Consolidated Statement of Changes in Stockholders' Equity for the Years Ended December 31, 2021, 2020 and 2019
   Consolidated Statement of Cash Flows for the Years Ended December 31, 2021, 2020 and 2019
   Notes to Consolidated Financial Statements

2. All financial statement schedules are omitted because the required information is either not applicable, not required or is shown in the respective financial statement or in the notes thereto, which are incorporated by reference at subsection (a)(1) of this item.

3. The following Exhibits are filed herewith, or incorporated by reference as a part of this report.

3.1	Restate Articles of Incorporation of Citizens Financial Services, Inc., as amended(1)
3.2	Articles of Amendment of Restated Articles of Incorporation of Citizens Financial Services, Inc. (2)
3.3	Bylaws of Citizens Financial Services, Inc.(3)
4	Instrument defining the rights of security holders (4)
10.1	*Amended and Restated Executive Employment Agreement between Citizens Financial Services, Inc., First Citizens Community Bank and Randall E. Black(5)
10.2	*Citizens Financial Services, Inc. Directors' Deferred Compensation Plan(6)
10.3	*Citizens Financial Services, Inc. Directors' Life Insurance Program(7)
10.4	*Supplemental Executive Retirement Plan(8)
10.5	*Second Amendment to First Citizens Community Bank Supplemental Executive Retirement Plan(9)
10.6	*Change in Control Agreement, between First Citizens Community Bank, Citizens Financial Services, Inc. (as guarantor) and Mickey L. Jones (10)
10.7	*First Citizens Community Bank Annual Incentive Plan (11)
10.8	*Amended and Restated First Citizens Community Bank Annual Incentive Plan(12)
10.9	*First Citizens Community Bank Endorsement Split-Dollar Life Insurance Plan (13)
10.10	Citizens Financial Services, Inc. 2016 Equity Incentive Plan (14)
10.11	*Change in Control Agreement, between First Citizens Community Bank, Citizens Financial Services, Inc. (as guarantor) and Jeffrey L. Wilson (15)
10.12	*Change in Control Agreement, between First Citizens Community Bank, Citizens Financial Services, Inc. (as guarantor) and David Z. Richards, Jr. (16)

10.13	*Change in Control Agreement, between First Citizens Community Bank, Citizens Financial Services, Inc. (as guarantor) and Jeffrey B. Carr [17]
10.14	*First Citizens Community Bank Executive Deferred Compensation Plan [18]
10.15	*Amended and Restated First Citizens Community Bank Executive Deferred Compensation Plan
10.16	*First Citizens Community Bank Long Term Incentive Plan [19]
21	List of Subsidiaries
23	Consent of S.R. Snodgrass, P.C., Independent Registered Public Accountants
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
32.1	Section 1350 Certification of Chief Executive Officer
32.2	Section 1350 Certification of Chief Financial Officer
101	The following materials from the Company's Annual Report on Form 10-K for the year ended December 31, 2021, formatted in XBRL (Extensible Business Reporting Language): (i) The Consolidated Balance Sheet, (ii) the Consolidated Statement of Income, (iii) the Consolidated Statement of Comprehensive Income, (iv) the Consolidated Statement of Changes in Stockholders' Equity, (v) the Consolidated Statement of Cash Flows and (vi) related notes.
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

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*Management contract or compensatory plan, contract or arrangement

(1) Incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2018, as filed with the Commission on August 9, 2018.

(2) Incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K, as filed with the Commission on April 26, 2021.

(3) Incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K, as filed with the Commission on December 17, 2020.

(4) Incorporated by reference to Exhibit 4 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005, as filed with the commission on March 14, 2006.

(5) Incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, as filed with the Commission on August 9, 2012.

(6) Incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2019, as filed with the Commission on August 8, 2019.

(7) Incorporated by reference to Exhibit 10.3 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2004, as filed with the Commission on March 15, 2005.

(8) Incorporated by reference to Exhibit 10.6 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2012, as filed with the Commission on March 7, 2013.

(9) Incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2021, as filed with the Commission on November 4, 2021.

(10) Incorporated by reference to Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, as filed with the Commission on August 9, 2012.

[11] Incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013, as filed with the Commission on August 8, 2013.

[12 Incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2021, as filed with the Commission on November 4, 2021.

[13] Incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, as filed with the Commission on January 7, 2015.

[14] Incorporated by reference to Exhibit A to the Company's definitive proxy statements for the 2016 Annual Meeting of Shareholders, as filed with the Commission on March 10, 2016.

[15] Incorporated by reference to Exhibit 99.1 to the Company's Form 8-K, as filed with the Commission on December 22, 2016.

[16] Incorporated by reference to Exhibit 10.1 to the Company's Form 8-K, as filed with the Commission on December 11, 2017.

[17] Incorporated by reference to Exhibit 10.1 to the Company's Form 8-K, as filed with the Commission on December 21, 2017.

[18] Incorporated by reference to Exhibit 10.12 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2018, as filed with the Commission on March 7, 2019.

[19] Incorporated by reference to Exhibit 10.13 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2019, as filed with the Commission on March 12, 2020.

ITEM 16 – FORM 10-K SUMMARY

Not Applicable.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Citizens Financial Services, Inc.

(Registrant)

/s/ Randall E. Black
By: Randall E. Black
Chief Executive Officer and President
(Principal Executive Officer)

Date: March 10, 2022

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature and Capacity	Date
/s/ Randall E. Black Randall E. Black, Chief Executive Officer, President and Director (Principal Executive Officer)	March 10, 2022
/s/ Stephen J. Guillaume Stephen J. Guillaume, Chief Financial Officer (Principal Financial & Accounting Officer)	March 10, 2022
/s/ Robert W. Chappell Robert W. Chappell, Director	March 10, 2022
/s/ R. Joseph Landy R. Joseph Landy, Director	March 10, 2022
/s/ Roger C. Graham, Jr. Roger C. Graham, Director	March 10, 2022
/s/ E. Gene Kosa E. Gene Kosa, Director	March 10, 2022
/s/ Rinaldo A. DePaola Rinaldo A. DePaola, Director	March 10, 2022
/s/ Thomas E. Freeman Thomas E. Freeman, Director	March 10, 2022
/s/ Alletta M. Schadler Alletta M. Schadler, Director	March 10, 2022
/s/ Christopher W. Kunes Christopher W. Kunes	March 10, 2022
/s/ David Z, Richards, Jr. David Z. Richards, Jr., Director	March 10, 2022
/s/ Mickey L. Jones. Mickey L. Jones, Director	March 10, 2022
/s/ Janie M Hifiger Janie M Hilfiger, Director	March 10, 2022

Exhibit 31.1

Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer

I, Randall E. Black, certify that:

1. I have reviewed this Form 10-K of Citizens Financial Services, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 10, 2022

/s/ Randall E. Black
By: Randall E. Black
Chief Executive Officer and President
(Principal Executive Officer)

Exhibit 31.2

Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer

I, Stephen J. Guillaume, certify that:

1. I have reviewed this Form 10-K of Citizens Financial Services, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 10, 2022

/s/ Stephen J. Guillaume
By: Stephen J. Guillaume
Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)

EXHIBIT 32.1
Certification Pursuant To
18 U.S.C. Section 1350
As Added By
Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report of Citizens Financial Services, Inc. (the "Company") on Form 10-K (the "Report") for the year ended December 31, 2021, as filed with the Securities and Exchange Commission, I, Randall E. Black, Chief Executive Officer and President, of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of section 13(a) or 15 (d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of the dates and for the periods expressed in the Report.

/s/ Randall E. Black
By: Randall E. Black
Randall E. Black
Chief Executive Officer and President

Date: March 10, 2022

EXHIBIT 32.2
Certification Pursuant To
18 U.S.C. Section 1350
As Added By
Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report of Citizens Financial Services, Inc. (the "Company") on Form 10-K (the "Report") for the year ended December 31, 2020, as filed with the Securities and Exchange Commission, I, Stephen J, Guillaume, Chief Financial Officer, of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of section 13(a) or 15 (d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of the dates and for the periods expressed in the Report.

/s/ Stephen J. Guillaume
By: Stephen J. Guillaume
Stephen J. Guillaume
Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)

Date: March 10, 2022